CANON ANNUAL REPORT 2012

Fiscal Year Ended December 31, 2012

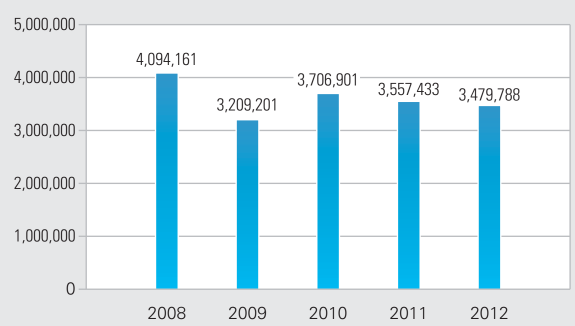
Canon

FINANCIAL HIGHLIGHTS

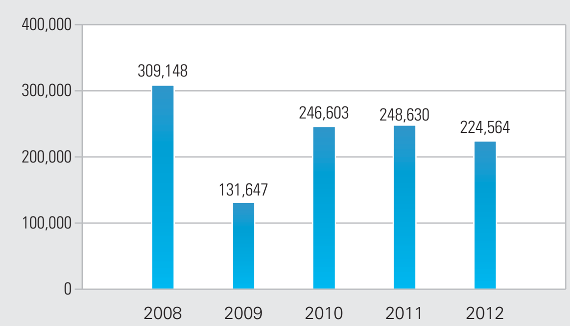
	Millions of yen (except per share amounts)			*Thousands of U.S. dollars (except per share amounts)*
	2012	2011	Change (%)	2012
Net sales	¥3,479,788	¥3,557,433	-2.2	$39,997,563
Operating profit	323,856	378,071	-14.3	3,722,483
Income before income taxes	342,557	374,524	-8.5	3,937,437
Net income attributable to Canon Inc.	224,564	248,630	-9.7	2,581,195
Net income attributable to Canon Inc. stockholders per share:				
—Basic	¥ 191.34	¥ 204.49	-6.4	$ 2.20
—Diluted	191.34	204.48	-6.4	2.20
Total assets	¥3,955,503	¥3,930,727	+0.6	$45,465,552
Canon Inc. stockholders' equity	¥2,598,026	¥2,551,132	+1.8	$29,862,368

Notes:
1. Canon's consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles.
2. U.S. dollar amounts are translated from yen at the rate of JPY87=U.S.$1, the approximate exchange rate on the Tokyo Foreign Exchange Market as of December 28, 2012, solely for the convenience of the reader.

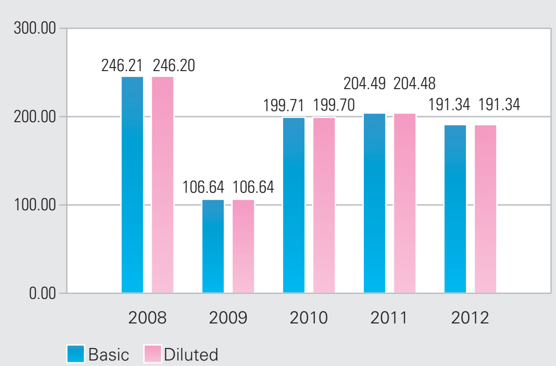
Net Sales
(Millions of yen)



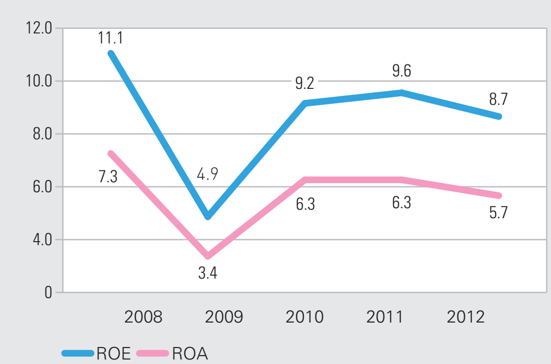
Net Income Attributable to Canon Inc.
(Millions of yen)



Net Income Attributable to Canon Inc. Stockholders per Share
(Yen)



ROE/ROA
(%)



CORPORATE PROFILE

Canon develops, manufactures and markets a growing lineup of copying machines, printers, cameras and industrial and other equipment. Through these products, the Company meets growing customer needs that are becoming increasingly diversified and sophisticated. Today, the Canon brand is recognized and trusted throughout the world.

In 1996, Canon launched its Excellent Global Corporation Plan with the aim of becoming a company worthy of admiration and respect the world over. Currently, the Company is working to achieve the overwhelming No. 1 position in its existing core businesses and expand related and peripheral businesses by strengthening its advanced solutions business, centered on innovative products, and through other measures. At the same time, Canon is nurturing its operations in the fields of medical equipment and industrial equipment, the latter including intelligent robots, to establish new core businesses. The Company is working to fulfill its responsibilities to investors and society, emphasizing sound corporate governance and stepping up the implementation of activities that contribute to environmental and social sustainability.

CORPORATE PHILOSOPHY: *Kyosei*

Canon's corporate philosophy is *kyosei*. A concise definition of this word would be "Living and working together for the common good." But Canon's definition is broader: *kyosei* is "All people, regardless of race, religion or culture, harmoniously living and working together into the future." Unfortunately, the presence of imbalances in the world in such areas as trade, income levels and the environment hinders the achievement of *kyosei*.

Addressing these imbalances is an ongoing mission, and Canon is doing its part by actively pursuing *kyosei*. Truly global companies must foster good relations, not only with their customers and the communities in which they operate, but also with nations, and they need to address environmental issues worldwide. In addition, global companies must bear responsibility for the impact of their activities on society. For this reason, Canon's goal is to contribute to global prosperity and to people's well-being, which will lead to continuing growth and bring the world closer to achieving *kyosei*.

CORPORATE GOAL

Canon sees itself growing and prospering over the next 100, and even 200, years. Toward this end, the Company has been promoting its Excellent Global Corporation Plan, launching Phase IV of the initiative in 2011. Building on the financial strengths that the Company has continuously reinforced through the implementation of the plan, Canon aims to join the ranks of the world's top 100 companies in terms of major management indicators.

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Cover Photo:
The EOS-1D X, the flagship EOS model, is an interchangeable-lens digital camera that provides a high-level of image quality performance as well as high speed. Canon retains the top position in global sales volume of interchangeable-lens digital cameras by catering to the diverse needs of a broad array of users ranging from beginners to advanced amateurs and professional photographers.

TO OUR STOCKHOLDERS

Fujio Mitarai
Chairman & CEO
Canon Inc.

In the face of the current turbulent business environment, Canon will decisively implement reforms and achieve sound business growth.

PERFORMANCE IN 2012

Looking at the global economy in fiscal 2012, ended December 31, while the United States continued to enjoy a relatively solid economic recovery, the European economy struggled in the face of financial instability and clouds began to appear over growth in China and other emerging nations. The Japanese economy realized moderate expansion driven by internal demand, but the rate of growth slowed somewhat in the second half of the year. As for foreign exchange markets, the yen maintained its high valuation, remaining mostly unchanged against the U.S. dollar from the previous year but rising significantly against the euro.

Canon's performance was affected by such factors as the worldwide economic slowdown and the historically high yen. For the year, consolidated net sales totaled ¥3,479.8 billion, down 2.2% from the previous year. Despite the highly challenging business conditions, however, we worked hard to boost the competitiveness of our products while striving to maintain and improve our sound financial structure. On a local currency basis, net sales remained mostly unchanged from fiscal 2011.

In order to boost the competitive strength of our products, we made efforts to maintain and further expand market share, further raising competitiveness through such means as launching a greater number of new products than in previous years. In addition to enjoying the No. 1 position for laser printers and digital cameras, we maintained strong market positions across all our business segments.

We also strove to maintain and improve our sound financial structure. Our stockholders' equity ratio, a reliable indicator of financial stability, rose 1.0 percentage point, from 65% in 2011 to 66% in 2012. At fiscal year-end, cash and cash equivalents stood at around ¥670 billion, equivalent to approximately 2.3 months of net sales, which we regard as an adequate level.

Consequently, although we were not able to avoid the decline in business performance, our corporate strength remains intact in terms of our product competitiveness and retaining a sound financial structure. Moreover, we believe we were successful in maintaining a robust foundation that will enable us to swiftly address future changes in the business environment and make necessary investments in a flexible manner.

With respect to stockholder return, Canon is being more proactive in returning profits to stockholders, mainly in the form of dividends, taking into consideration mid-term profit forecasts, planned future investments, cash flow and other factors. Over the 25 years since 1988, we have steadily increased dividends without ever having lowered them during this period. In fiscal 2012, Canon has decided to pay a full-year cash dividend of ¥130.00 per share, a ¥10.00 increase from fiscal 2011. This included a special ¥10.00 dividend to commemorate our 75th anniversary.

EXCELLENT GLOBAL CORPORATION PLAN

Canon launched the Excellent Global Corporation Plan in 1996 and, since that time, we have reinforced our business foundation through the plan's various phases.

During Phase I, we began by emphasizing consolidated business management over nonconsolidated business management and thoroughly shifted our focus

Key Strategies For Phase IV

1	Achieving the overwhelming No.1 position in all core businesses and expanding related and peripheral businesses
2	Developing new business through globalized diversification and establishing the Three Regional Headquarters management system
3	Establishing a world-leading globally optimized production system
4	Comprehensively reinforcing global sales capabilities
5	Building the foundations of an environmentally advanced corporation
6	Imparting a corporate culture, and cultivating human resources befitting a truly excellent global company

from partial to total optimization and on profit rather than sales. By stressing the importance of cash-flow management and comprehensively eliminating waste, we were able to reduce our debt by more than half while also significantly increasing productivity through the introduction of the cell production system and other measures.

In Phase II, we focused on reinforcing Canon's product competitiveness. We fully digitalized our copying machine and camera offerings, laying the groundwork for the successes that we enjoy today while also effectively creating a debt-free company.

During Phase III, we sought to expand Canon's business scope, broadening our businesses in the printing and medical equipment fields while actively carrying out M&A activities.

And in 2011, under the slogan "Aiming for the Summit: Speed & Sound Growth," we embarked on Phase IV, spanning the five-year period through 2015. Focusing on six key strategies, Phase IV calls for

The Excellent Global Corporation Plan

Phase I 1996–2000

Strengthened our financial structure by thoroughly eliminating wastefulness, with production reforms playing a major role, based on changing our mindset with a focus on total optimization and profitability.

Phase II 2001–2005

Recognized the need for digitalization and raised product competitiveness by enhancing our development infrastructure and reinforcing key components.

Phase III 2006–2010

Strove to achieve "Sound Growth," seeking high growth levels by establishing new businesses while raising the profitability of existing businesses. With the global economy plunging into the global recession, shifted direction towards "improving the quality of management."

Set up an even stronger financial structure and increased momentum towards a dramatic leap forward from now.

Phase IV 2011–2015

Tackle again the challenge of achieving "Sound Growth" through timely change in advance of changes in the times.

Slogan:
"Aiming for the Summit: Speed & Sound Growth"

proactive, speedy reforms ahead of the dramatic changing times along with the achievement of sound business growth through the further expansion of our corporate scale while maintaining high profitability.

STRATEGY 1

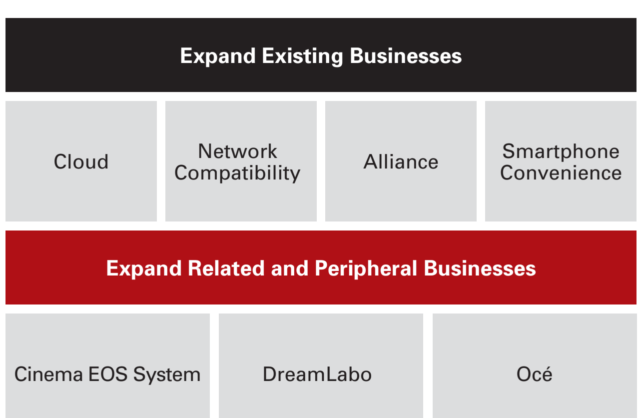
With respect to **achieving the overwhelming No.1 position in all core businesses and expanding related and peripheral businesses,** we have comprehensively upgraded Canon's office multifunction device (MFD) and production printing system lineups, from low-speed to high-speed models, for both monochrome and color devices. In addition to fully rounding out the imageRUNNER ADVANCE series, we have introduced new products developed jointly with Océ, which became a consolidated Canon subsidiary in 2010. Furthermore, our sales companies around the world have strengthened their solutions business, which supports enhanced productivity in the office.

As for interchangeable-lens digital cameras, Canon further reinforced its EOS series, including the launch of high-resolution models featuring compact, lightweight designs. Accordingly, we were able to retain our No.1 share worldwide in terms of unit sales. In September 2012, meanwhile, we unveiled Canon's first non-reflex camera. Moreover, our Cinema EOS System has attracted warm acclaim throughout the world, capturing a high market share in a short time. In October 2012, we added to our lineup the EOS C500, a digital cinema camera capable of shooting high-quality 4K-resolution video, or four times the resolution of full-HD video.

In February 2012, Canon unveiled the DreamLabo 5000 commercial photo printer, marking our entry into the retail photo printing market.

In July 2012, we released the Canon MREAL System. Integrating the real world with the virtual world of computer graphics, MR (mixed reality) systems employ image processing technologies to streamline various business processes, including product design. We have received numerous inquiries, not only from the automotive and construction sectors—with whom we have collaborated since the initial development stage—but also heavy machinery manufacturers and educational institutions.

Achieving the Overwhelming No.1 Position



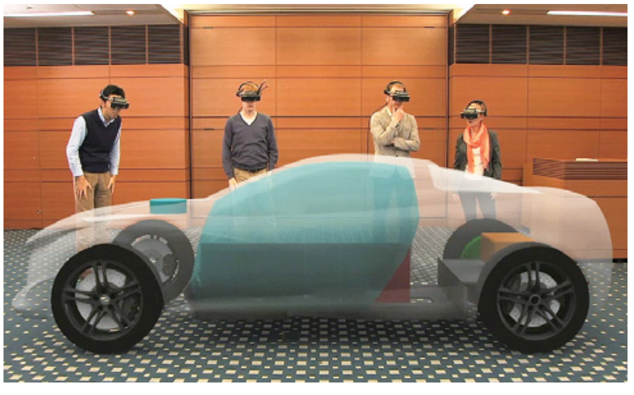
Amid growing awareness about safety and reliability, as well as the ongoing shift from analog to digital, Canon launched a full-HD network camera in 2012. In this field, users are demanding various software functions, such as detection, tracking and image retrieval. For this reason, we will accelerate business expansion while pursuing M&A opportunities.

STRATEGY 2

Seeking to diversify our operations globally, Canon established R&D facilities in Japan, the United States and Europe. Under this strategy of **developing new business through globalized diversification and establishing the Three Regional Headquarters management system,** we have identified two fields that we are strengthening as new core businesses: medical equipment and industrial equipment.

In the medical device segment, we are making use of the imaging technologies we have amassed over many years to create new levels of value in such areas as medical imaging diagnostics. In Japan, we are working with Kyoto University toward the practical application of innovative medical imaging equipment. As part of this collaboration, we have brought two technologies to the clinical evaluation stage in 2012. One relates to photoacoustic mammography devices capable of diagnosing breast cancer more accurately than before and with minimal bodily impact during examination. The other relates to adaptive optics scanning laser ophthalmoscopy (AO-SLO), which contributes to the examination of the retina at the cellular level and the detection of lifestyle-related diseases. Meanwhile, Canon U.S.A. established its own R&D department in 2012 and reached collaborative research agreements with two hospitals affiliated with Harvard Medical School to develop biomedical optical imaging and medical robotics technologies. This collaborative project aims to develop and commercialize unique medical devices for a variety of applications.

As for the industrial equipment segment, we are harnessing Canon's group-wide strengths to create a new business domain with the aim of building it into a ¥1 trillion business in the future. Canon already supplies a variety of industrial equipment, including



The MR System can be used not only in the design and manufacturing sectors, but also in a wide range of industries and fields. Satisfied with the functionality and quality offered by the MR System, Canon launched the system in July 2012.

Global Diversification

Develop a Global R&D Structure
New Innovation Centers in the U.S. and Europe

U.S.	Europe
Establish Institutes with responsibilities spanning basic research to leading-edge technology application	Promote diversification utilizing Océ as a foothold

lithography equipment, vacuum thin-film deposition equipment and organic LED panel manufacturing equipment. We believe, however, that we can open new frontiers through the combination of individual elemental technologies. Particularly within the field of factory automation, for example, expectations are high for intelligent robots. One technology being developed for such robots is Super Machine Vision, which enables the positions and orientations of various objects to be monitored three-dimensionally with micron-level precision—a capability that far exceeds human vision.

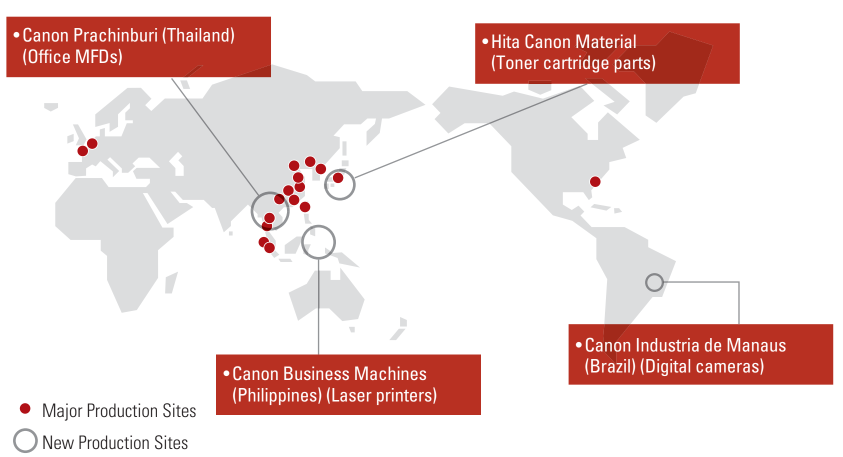
STRATEGY 3

With respect to manufacturing, Canon is pursuing a strategy of **establishing a world-leading globally optimized production system.** We carry out comprehensive evaluations to ensure the optimization of our production bases. We analyze trends in each country from multiple perspectives, paying close attention to such factors as wages, taxation systems, infrastructure and country risk. The criterion we use when determining where to base our production is the ratio of labor costs to total manufacturing costs. Currently, we manufacture high-value-added products in Japan, while products with lower added value and a higher labor cost ratio are produced elsewhere. In addition, in the case of consumables, for example, we promote localized production, in which the entire process—from production to sales and even the recycling of used products—is carried out within a single region.

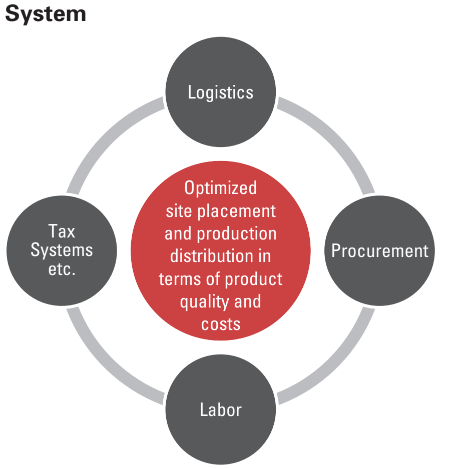
Based on these policies, in 2012 we expanded our production facilities at Canon Hi-Tech (Thailand) in the northeast region of Thailand, thus reinforcing our production system for inkjet printer products. We also established new companies in Thailand, the Philippines and Brazil, where we plan to start manufacturing office MFDs, laser printers, digital cameras and other products in 2013.

Since 2010, Canon has carried out the localized production of toner cartridges in the United States. Thanks to progress in automation, the ratio of labor costs to total manufacturing costs for toner cartridges has fallen significantly, so we plan to replicate this business model in Europe and other regions.

Accelerate Cost Reduction by Expansion of New Production Sites



Globally Optimized Production System



STRATEGY 4

We are also **comprehensively reinforcing our global sales capabilities** in a proactive manner, particularly in emerging nations. In China, for example, we are working hard to tap markets in regional cities, and in 2012 the number of sales bases in China increased from 21 to 31. The importance of strengthening our sales power in emerging nations outside of China is also growing. At the top of the list is India, where we fortified our sales system by switching our distribution channels from an agency-based sales approach to direct sales. We are also focusing on the development of Canon-brand shops in India. In 2012, we opened 43 such outlets, with plans to increase the number to 300 by 2014. Meanwhile, in Russia, which joined the World Trade Organization (WTO) in August 2012, we are also working to reinforce our sales activities.

Brazil is the world's third-largest market for compact digital cameras, but import taxes have a major impact on competitiveness. For this reason, in July 2013 we plan to start local production in the city of Manaus, which will enhance our sales appeal in the country.

STRATEGY 5

In addition to fulfilling our social responsibilities to the natural environment, Canon strives to become a company that simultaneously achieves progressive corporate growth and protects the environment. Committed to **building the foundations of an environmentally advanced corporation,** we are working to minimize the environmental impact of our operations and cut carbon dioxide emissions while raising the performance of our products. Initiatives here include developing energy-saving technologies and materials with low environmental burden. In 1990, we launched our Toner Cartridge Collection and Recycling Program and now carry out the localized recycling of cartridges in the United States, Japan, China and France. In 1996, we also started a collection service in Japan for used ink cartridges, and this program has since been expanded to include Asia, Oceania, North America and Europe.

STRATEGY 6

In order to ensure that Canon develops as a truly excellent global company worthy of admiration and respect

Capturing Growth in Emerging Markets

Managers from Group companies worldwide gather at the Canon Global Management Institute in Japan to study corporate strategies and engage in cross-cultural exchanges.

worldwide for 100, and even 200, years, it is crucial to have exceptional global human resources. We believe that our global workforce must be not only capable of winning in the face of global competition but also capable of delivering innovation. This is because, throughout our history, we have continuously transformed our company based on our enterprising spirit.

Canon is committed to **imparting a corporate culture, and cultivating human resources befitting a truly excellent global company.** To this end, we already have numerous local human resources in management positions at our sales companies around the world. For example, in Europe, our largest regional market, the presidents of all but one of our sales companies are from the region. At the same time, we have around 1,000 Japanese employees stationed at our sales companies around the world. We will continue endeavoring to acknowledge and respond flexibly to the diversified value perspectives of local communities, respecting their cultures and customs while striving to foster global human resources who can excel on the world stage.

IN CONCLUSION

The global economy in 2013 is expected to remain challenging for the foreseeable future. However, as new administrations take office in such key countries as Japan, the United States and China, there are expectations that various economic stimulus measures will gradually bear fruit. As such, we believe that we will see a recovery trend in the second half that should gather momentum.

Amid these circumstances, we feel that the markets in which we operate will recover in a similar fashion. Accordingly, we will focus on returning Canon to a growth trajectory while closely monitoring market trends. Our basic policy for 2013, which marks the third year of Phase IV of our Excellent Global Corporation Plan, is to decisively implement reforms and achieve sound business growth in the face of the current turbulent business environment. Targeting solid increases in both sales and profit, we will steadily implement measures based on the six key strategies described above.

In 2012, we celebrated Canon's 75th anniversary, having overcome numerous difficulties and achieved dramatic progress since the company's foundation. Looking around the world, there are many examples of companies that have delivered innovation and growth for 100 years or more. For companies willing to continually transform themselves, the potential is unlimited.

Going forward, we will continue striving to reinforce Canon's technological capabilities. At the same time, we will prevail in the face of the challenging business environment while relentlessly targeting productivity improvements and cost reductions. At this early stage of the economic upturn, we will exploit our increasingly robust business structure to steer Canon toward a path of steady growth.

We look forward to your ongoing understanding and support.

Fujio Mitarai
Chairman & CEO
Canon Inc.

AT A GLANCE

Business Units	Main Products

OFFICE BUSINESS UNIT


Office Multifunction Devices (MFDs)


Digital Production Printing Systems


Laser Printers


High Speed Continuous Feed Printers

- Office Multifunction Devices (MFDs)
- Office Copying Machines
- Personal-Use Copying Machines
- Laser MFDs
- Laser Printers
- Digital Production Printing Systems
- High Speed Continuous Feed Printers
- Wide-Format Printers
- Document Solution

IMAGING SYSTEM BUSINESS UNIT


Interchangeable-Lens Digital Cameras

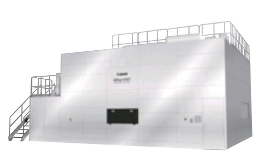

Digital Camcorders


Inkjet Printers


Broadcast Equipment

- Interchangeable-Lens Digital Cameras
- Compact Digital Cameras
- Digital Camcorders
- Digital Cinema Cameras
- Interchangeable Lenses
- Inkjet Printers
- Large-Format Inkjet Printers
- Commercial Photo Printers
- Image Scanners
- Broadcast Equipment
- Calculators

INDUSTRY AND OTHERS BUSINESS UNIT


Flat-Panel-Display Lithography Equipment


Ophthalmic Equipment

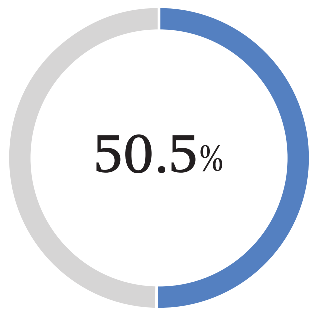

Semiconductor Lithography Equipment

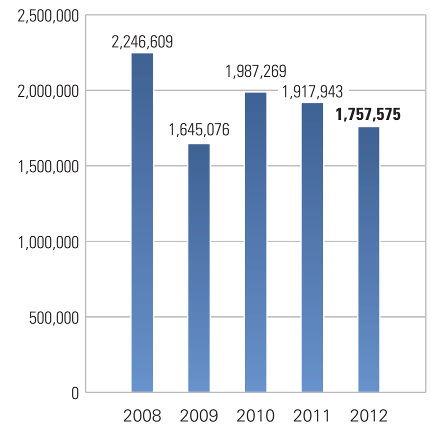

Document Scanners

- Semiconductor Lithography Equipment
- Flat-Panel-Display Lithography Equipment
- Digital Radiography Systems
- Ophthalmic Equipment
- Vacuum Thin-Film Deposition Equipment
- Organic LED Panel Manufacturing Equipment
- Micromotors
- Computers
- Handy Terminals
- Document Scanners

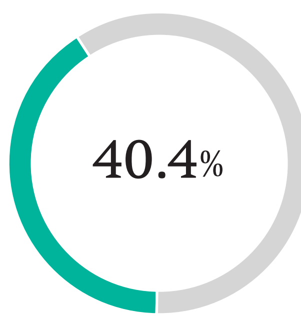
Outline	**Composition of Sales** *(%)*	**Net Sales** *(Millions of yen)*

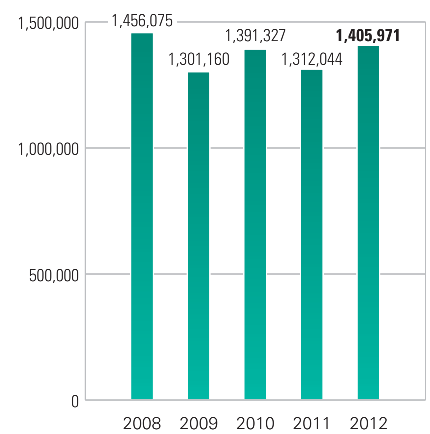
In this segment, Canon offers a comprehensive range of multifunction devices (MFDs), printers, and other equipment featuring high image quality, high resolution, and high speed. Leveraging these products, Canon works in close collaboration with various Group companies and alliance partners to deliver optimal solutions tailored to match the customer's business operations. These include various document solutions, such as office document management and the output of records. At the same time, the Company provides top-quality services and support in a swift and reliable manner.



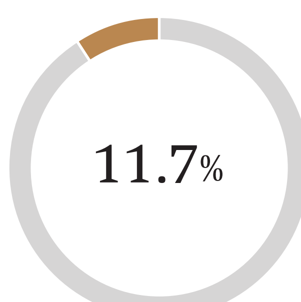


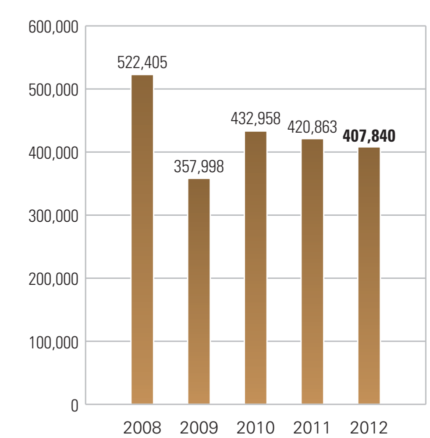
Canon's offerings in this segment include digital cameras, digital camcorders, digital cinema cameras, interchangeable lenses, inkjet printers, and calculators. Canon's digital cameras, digital camcorders and digital cinema cameras, designed to deliver unparalleled image quality, have earned particularly high acclaim worldwide, thanks to in-house developed lenses, CMOS image sensors, and image processors. Also widely popular are Canon's inkjet printers, which are easy to use and produce beautiful pictures at high speeds.





Applying optical technologies and image-processing technologies amassed over many years, Canon provides high-value-added products to a wide range of industries. The Company is already prominent globally as a manufacturer of flat-panel- display lithography equipment and semiconductor lithography equipment. In addition, Canon is focusing on the medical equipment field - one of its next generation core businesses. The Company is aggressively promoting sales of its cutting-edge digital radiography systems and ophthalmic equipment, which employ Canon's highly regarded medical imaging technologies.

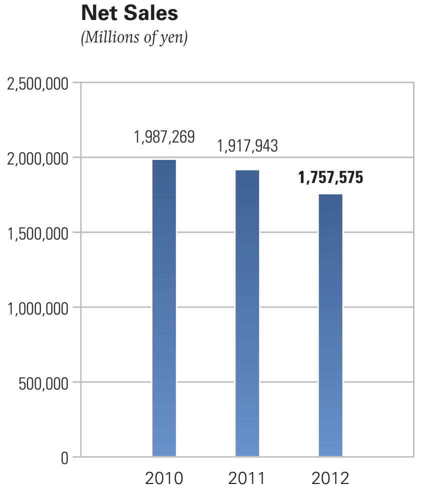




Note: The percentage figures for the three business units presented in the pie charts above do not add up to 100% because "Eliminations," used in consolidated accounting, were not included in calculation considerations.

OFFICE BUSINESS UNIT

Canon has expanded the functions of its office multifunction devices, which realize enhanced coordination with IT systems and are compatible with various types of system application software, offering an optimal usage environment for all sorts of document-related tasks.



2012 REVIEW

The market for office network multifunction devices (MFDs) was generally firm, with solid demand on earthquake disaster restoration in Japan as well as growing demand in Asia and Oceania. In these circumstances, Canon boosted domestic sales by proactively cultivating new customers, and generated particularly strong sales of its imageRUNNER ADVANCE C5000 series. We also posted increased unit sales in the Americas, and even in Europe, where the market contracted moderately. In particular in emerging European markets, such as Russia, we posted healthy growth in sales of color devices. In China, the imageRUNNER ADVANCE C2000 series of low-and medium-speed color models drove expansion in unit sales. Elsewhere in Asia and also in Oceania, sales exceeded the previous year's levels.

The market for digital production printing systems benefited from growth in Asia and generally steady demand in other regions. In these circumstances, in Japan, we reported increased unit sales of light-production monochrome models and mid-production color models, and in other Asian markets, unit sales were also up. In the Americas and Europe, the synergistic benefits of our alliance with Océ began to appear: in addition to the mid-production monochrome Océ VarioPrint 6000 series, the monochrome Océ VarioPrint 135 series and the color imagePRESS C6010/C7010VPS series, both jointly developed by Canon and Océ, were highly praised and very well received. Furthermore, we enjoyed steadily increasing sales via the Océ channel.

Moreover, sales in Europe of laser MFDs, laser printers, and personal-use MFDs for individual and SOHO use were higher than the previous year in both volume and value terms, thanks to strenuous marketing efforts in the face of difficult market conditions.

In the area of OEM-brand laser MFDs and laser printers, while the market for color laser MFDs expanded, with the exception of a few regions, the relatively larger market for monochrome machines continued to shrink. As a result, we were not able to prevent a decline in both unit sales and sales revenue from sales to OEM customers.

As a result, the Office Business Unit reported consolidated net sales of ¥1,757.6 billion, down 8.4% from the previous year.

2013 INITIATIVES

Going forward, Canon will promote business expansion aimed at capturing the top share of the market for office-use devices. At the core of this effort is the imageRUNNER ADVANCE series, featuring a now complete, extensive lineup ranging from low-speed to high-speed models, as well as monochrome and color models. We will also extensively reinforce our solutions and services business based on the benefits from the integration of our regional sales companies and the sales subsidiaries of Océ, with the intention of attracting more international corporate clients. To address flourishing demand in emerging nations, meanwhile, we will strengthen our strategic measures, including by launching region-specific models placing top priority on the end-user.

In the production printing sector, we will seek to enter the enormous offset printing market. Here, we will integrate the technological strengths of Canon and Océ to achieve both further advances in printing speed and cost reduction, as well as improved workflow harmony, with the aim of becoming a top player in the market.

With respect to laser printers, we will strive to boost market share and profitability by launching new products, centering on the high-volume printers class.

The imageRUNNER ADVANCE C5255 is a medium-to-high-speed MFD that offers enhanced productivity, image print quality, and security together with much improved operability thanks to a Quick Startup Mode.

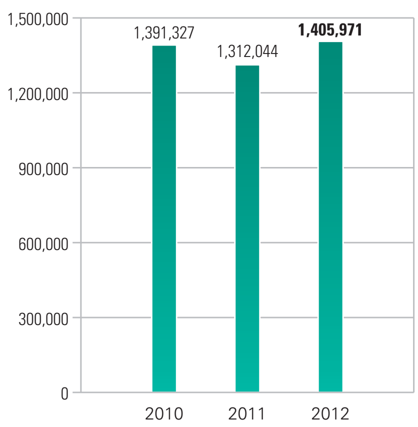
The Océ VarioPrint 135, combines a new Océ-developed engine with high-performance Canon finishers and a scanner. The two companies jointly developed this system to meet a wide range of high-speed, high-volume monochrome printing needs.

The imagePRESS C7010VPS, jointly developed with Océ, delivers high-image-quality, high-precision printing that rivals offset printing, with a printing speed of up to 70 ppm for both color and monochrome output.

IMAGING SYSTEM BUSINESS UNIT

Canon's digital SLR cameras, which use groundbreaking technology such as proprietary lenses, CMOS image sensors, and image processors, lead the world with their high image quality and contribute to sales.

Net Sales
(Millions of yen)



2012 REVIEW

The market for interchangeable-lens digital cameras showed growth across all regions. The advanced-amateur models, EOS 5D Mark III and EOS 60D, as well as the entry-level EOS Rebel series drove sales beyond the previous year's level both in volume and value terms. Moreover, Canon retained the world's top share in shipments of interchangeable-lens digital cameras. In addition, we released the EOS M, which was our first camera to employ a non-reflex operating system and the EOS 6D, the world's smallest and most compact full-size digital camera. Furthermore, our EOS-1D X flagship model, released in June 2012, was used extensively by professional photographers at the London Olympics.

In compact digital cameras, Canon launched attractive new products such as the PowerShot ELPH 110 HS (IXUS 125 HS in some areas) and the PowerShot A2300. The year-on-year decline in sales volume was thus slight despite declining demand for compact digital cameras worldwide.

Digital video camcorders are also facing a downtrend in global demand. Against that backdrop, Canon pursued a profit-oriented strategy, and its HFG10, a high-end high-definition model, captured the top market share in its price range. Moreover, amid a very positive reception for the Cinema EOS System in the motion picture production industry, we added products supporting 4K resolution, including the EOS C500 Digital Cinema Camera, to our lineup.

In broadcast equipment, Canon enjoyed greater demand from domestic broadcasters and received numerous inquiries in Europe associated with large-scale sporting events. Accordingly, sales of broadcast equipment increased in 2012, driven by the DIGISUPER 95 field zoom lens.

Demand for inkjet printers declined in 2012, impacted by economic recession. Nevertheless, Canon swiftly recovered from the situation in Thailand, where flooding had caused shortages in supplies. Specifically, we focused on expanding sales centered on new products, such as the PIXMA PRO series (the lineup of which is now complete) and the PIXMA MG6300 series. As a result, we reported a year-on-year increase in sales volume despite a difficult market environment.

In large format inkjet printers, we reported a steady rise in sales volume, thanks largely to new models targeting the graphic arts community. To broaden our business domain, we unveiled DreamLabo 5000, a commercial photo printer.

As a result, sales at the Imaging System Business Unit increased 7.2%, to ¥1,406.0 billion.

2013 INITIATIVES

The market for interchangeable-lens digital cameras is expected to grow around 10% annually for the foreseeable future. In this context, Canon plans to maintain its strong competitiveness and become the overwhelming No. 1 player.

Amid dramatic market changes caused by the proliferation of smartphones and other devices, Canon will promote a photography culture based on unique perspectives in order to always stay one step ahead and provide forms of enjoyment for users. Here, we will deploy our deep knowledge of photography culture combined with our expertise in input/output devices. In compact digital cameras, we will utilize our image processing technologies amassed to date to create new levels of value. With respect to inkjet printers, we will make full use of our broad lineup, from personal-use to professional models, to achieve further growth in sales volume.

In addition, Canon will focus on broadening sales of DreamLabo 5000, a commercial photo printer launched to address the growing retail photo market. As for large format inkjet printers, we will seek to further boost sales by offering a comprehensive lineup.

The EOS 5D Mark III, with a newly developed CMOS image sensor and image processor, boasts outstanding image quality suitable for creating professional-like still image compositions and movies.

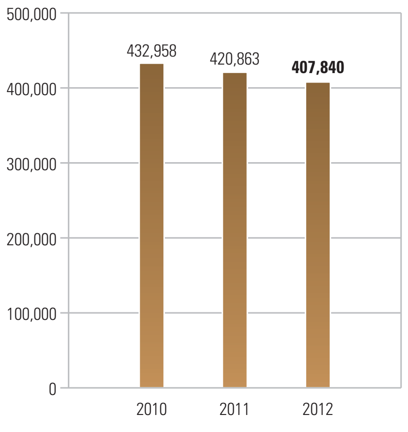
The EOS Rebel T4i (EOS 650D in some areas) is an entry-level, interchangeable-lens digital camera that delivers much enhanced autofocus performance for both still pictures and video and improved capabilities for high-speed continuous shooting and image quality.

The PIXMA MG6300 Series of home-use inkjet printers offers easy operability with features like advanced wireless printing and a touch panel, together with a cutting-edge design.

INDUSTRY AND OTHERS BUSINESS UNIT

Canon, through its semiconductor lithography equipment, achieves ever higher levels of performance and functionality to meet the strict cutting-edge demands of the industry, while focusing on the development of future technologies. These technologies also serve as a driving force behind Canon's optical and control technologies.

Net Sales
(Millions of yen)



2012 REVIEW

In semiconductor lithography equipment, capital investment for memory devices was weak due to the depressed PC market. However, investment in semiconductor production equipment for image sensors and logic devices was firm, thanks to increased demand for smartphones and tablet devices. Against this backdrop, Canon worked to attract orders from semiconductor devices makers, centering on i-line steppers. Notable among these was the FPA-5510iZ, suited to image sensor manufacturing, and the FPA-3030i5+, a new product suited to manufacturing green devices designed to reduce environmental stress. As a result, the decline in sales of semiconductor lithography equipment was slight, both in volume and value terms.

As for flat-panel-display lithography equipment, capital investment by makers of small-to-mid-sized panels used in smartphones and other devices was solid. However, capital investment in large-sized panel manufacturing, where Canon excels, was weak, leading to declines in overall sales of flat-panel-display lithography equipment, both in volume and value terms.

In medical equipment, Canon worked hard to bolster sales of mainstay digital radiography systems, centering on wireless-type and dynamic imaging equipment. In the ophthalmic equipment field, we launched the OCT–HS100, our first optical coherence tomography (OCT) device. Also contributing to higher sales were M&A activities conducted by subsidiaries.

With respect to document scanners manufactured by Canon Electronics Inc., overall sales in volume terms increased year on year, thanks to sales recovery in North America, as well as healthy sales in China, India, and elsewhere in Asia.

Sales of organic LED panel manufacturing equipment made by Canon Tokki Corporation rose steadily on the back of growing demand for smartphones and tablet devices.

Sales of magnetic head and hard disk thin-film deposition equipment made by Canon ANELVA Corporation declined due to a weak PC sector but sales of semiconductor thin-film deposition equipment increased significantly, boosted by brisk demand for semiconductor devices used in smartphones and the like.

There was a decline in sales of die bonders made by Canon Machinery Inc., as semiconductor device manufacturers failed to bolster capital investment, but sales of rechargeable battery-related devices used in automobiles and smartphones increased.

As a result, consolidated net sales of the Industry and Others Business Unit amounted to ¥407.8 billion, down 3.1% from the previous year.

2013 INITIATIVES

Going forward, Canon will focus on the medical equipment and industrial equipment fields as core areas for new business expansion.

In the medical equipment field, Canon will target further business expansion by bolstering sales of digital radiography systems with high-value-added functions such as wireless connectivity and dynamic imaging and also by working to boost sales of OCT devices, which we added to our lineup in 2012. In addition, we will endeavor to swiftly commercialize our business in mammography device, which incorporates photoacoustic technologies that have minimal impact on the body and enable more precise diagnoses of breast cancer than before.

In the industrial equipment field, Canon boasts a diversity of world-leading technologies in such areas as lithography equipment, as well as in businesses handled by Canon Group companies like vacuum thin-film deposition and organic LED panel manufacturing equipment. Leveraging this advantage, we will harness our technologies to address various market needs. In this way, we will open up new domains and step up efforts to make industrial equipment into a ¥1 trillion business in the future.

The FPA-3030i5+ is a category of semiconductor lithography equipment aimed at manufacturers of low-environmental-impact green devices like LEDs and MEMS devices for smartphones and other electronics, and the market for such equipment is expected to grow.

The CXDI-80C Wireless is a compact, lightweight, wireless, high-sensitivity digital radiography system that features an industry-first* 11x14 cassette size.

* As of September 2011, among medical X-ray digital imaging equipment, based on Canon research

The FC7100 system enables ultrathin film composition in an ultrahigh vacuum and so contributes to the rapid growth of mobile handsets as a technology that is indispensable to making devices smaller and more energy efficient.

2012 TOPICS

OFFICE BUSINESS UNIT

imageRUNNER ADVANCE C2230

imageRUNNER ADVANCE LINEUP NOW COMPLETE; CORE MODELS UPGRADED

Canon is working to reinforce its lineup of office multifunction devices (MFDs), and our imageRUNNER ADVANCE series is a cornerstone of this lineup. In 2012, we launched the 4000 series of low- and medium-speed monochrome MFDs to meet a diversity of needs, irrespective of office size. Now complete, the imageRUNNER ADVANCE series features a broad lineup, ranging from low- to high-speed devices, as well as both monochrome and color offerings.

During the year, we also introduced second-generation versions of our mainstay monochrome and color models, with improvements in such areas as operability, productivity, and security. In addition, we raised their energy-saving performance through enhanced equipment management. This is achieved through functions such as the high-speed start-up mode and automatic shutdown of devices in the same network. Thanks to such initiatives, Canon won the 2013 “Line of the Year” award for “Energy Efficiency” for its MFPs. The newly created award was announced by Buyers Laboratory LLC (BLI), a world-renowned independent analysis provider of document imaging products.

IMAGING SYSTEM BUSINESS UNIT

The 64th Annual Technology & Engineering Emmy® Awards

CANON WINS 2012 TECHNOLOGY AND ENGINEERING EMMY® AWARD

In 2012, Canon made a full-fledged entry into the motion picture production market with its Cinema EOS System. As the first step, the Company unveiled the EOS C300 digital cinema camera, capable of reproducing beautiful images close to those of 35mm motion picture film. The camera incorporates a Canon-developed large-format CMOS image sensor that is the same size as a super 35mm motion picture frame. Since then, we added to our lineup the EOS C500 digital cinema camera, which adopts the same large-format CMOS sensor and meets the 4K standard. Canon is continually working to improve image capture technologies to meet the ever-increasing needs of the motion picture and television production markets.

Our work on CMOS sensors used in the Cinema EOS System has been highly acclaimed as a breakthrough in technology that makes a significant contribution to broadcast technology development. As a result, Canon received a Technology and Engineering Emmy® Award in 2012 from the National Academy of Television Arts & Sciences, in the category of Improvements to Large Format CMOS Imagers for Use in High Definition Broadcast Video Cameras. This recognition came just a year after the product launch in the U.S.

Emmy® and the Emmy statuette are the trademark property of the Academy of Television Arts & Sciences (ATAS) / the National Academy of Television Arts & Sciences (NATAS)

IMAGING SYSTEM BUSINESS UNIT

PIXMA PRO SERIES OF PROFESSIONAL-USE INKJET PRINTERS LAUNCHED

Committed to meeting strong demand among professionals for high-resolution photograph printing, Canon launched three new models, which completed the rollout of its PIXMA PRO series. The first is the PIXMA PRO-1, featuring a significantly broadened color gamut as well as high productivity, highlighted by a new 12-color pigment ink system with large-volume ink tanks. The PIXMA PRO-10, meanwhile, boasts a new 10-color pigment ink system together with a high level of texture and depth perception. Also, there is the PIXMA PRO-100, which is equipped with a new eight-color dye ink system for superior expression of coloration and gloss.

All three models utilize Canon's Optimum Image Generating (OIG) System, which selects the optimal ink mixture and ink droplet arrangement, ensuring high-image-quality photograph prints best suited to the paper medium. The two models with pigment ink systems also feature our newly developed Chroma Optimizer, which ensures uniformity of gloss perception as well as enhanced black density to suppress the amount of light reflected from the paper surface.

PIXMA PRO series

INDUSTRY AND OTHERS BUSINESS UNIT

CANON MAKES FULL-FLEDGED ENTRY INTO OCT MARKET WITH LAUNCH OF FIRST CANON-BRAND PRODUCT

Optical coherence tomography (OCT) devices are used in ophthalmology departments of hospitals and clinics to obtain tomographic images of the retina and image analysis results. The system enables observation of retinal structures that cannot be seen from the surface and so is essential for providing higher quality diagnosis. The OCT market is forecasted to grow at around 6%*1 annually on a volume basis.

Seeking to make a full-fledged entry into the OCT market, Canon welcomed OPTOPOL Technology S.A., a Polish company, as a consolidated subsidiary in 2010, and since then has worked to commercialize OCT products.

In September 2012, Canon unveiled its first own-brand OCT, the OCT-HS100, capable of examining the retina three-dimensionally. With the addition of the Canon-brand OCT to our product lineup, we aim to provide a comprehensive range of ophthalmology diagnostic equipment and will expand our business further.

OCT-HS100

*1 Based on Canon research.

CORPORATE GOVERNANCE

Canon maintains sound corporate governance as part of efforts to maximize its stockholders' value and become a truly excellent global corporation.

BASIC POLICY AND CORPORATE GOVERNANCE STRUCTURE

Canon recognizes that management supervision functions and management transparency are vital to strengthening its corporate governance and further raising corporate value. Canon's basic governance structure comprises the General Meeting of Shareholders, the Board of Directors and the Audit & Supervisory Board. Furthermore, the Executive Committee and management committees are dedicated to addressing key issues. All of these bodies work together to ensure the appropriate management of the Group through an internal auditing structure underpinned by the Corporate Audit Center and an information disclosure system for management activities.

The San-ji ("Three Selfs") spirit are an important guiding principle to become a truly excellent global corporation.

BOARD OF DIRECTORS

Important business matters are discussed and ratified during meetings of the Board of Directors and Executive Committee. As of December 31, 2012, the board consisted of 18 directors. In order to facilitate more practical and efficient decision making, the board is entirely composed of internal directors who have well-developed knowledge of the Company's affairs. Also, the board is supported by various management committees that address important management issues in their specific fields. These committees complement the Company's management system by business unit, facilitate efficient decision making and realize a mutual supervisory function for such matters as compliance and ethics.

Directors and Audit & Supervisory Board Members *(as of December 31, 2012)*

Chairman & CEO

Fujio Mitarai

Executive Vice President & CFO

Toshizo Tanaka
Group Executive, Finance & Accounting Headquarters
Group Executive, Facilities Management Headquarters

Executive Vice President & CTO

Toshiaki Ikoma
Group Executive, Corporate R&D

Executive Vice President

Kunio Watanabe
Group Executive, Corporate Planning Development Headquarters

Senior Managing Directors

Yoroku Adachi
President & CEO, Canon U.S.A., Inc.

Yasuo Mitsuhashi
Chief Executive, Peripheral Products Operations

Shigeyuki Matsumoto
Group Executive, Device Technology Development Headquarters

Toshio Homma
Group Executive, Procurement Headquarters

Masaki Nakaoka
Chief Executive, Office Imaging Products Operations

Haruhisa Honda
Group Executive, Production Engineering Headquarters

Managing Directors

Hideki Ozawa
President & CEO, Canon (China) Co., Ltd.

Masaya Maeda
Chief Executive, Image Communication Products Operations

Directors

Yasuhiro Tani
Group Executive, Digital System Technology Development Headquarters

Makoto Araki
Group Executive, Information & Communication Systems Headquarters

Hiroyuki Suematsu
Group Executive, Environment and Quality Headquarters

Shigeyuki Uzawa
Chief Executive, Optical Products Operations

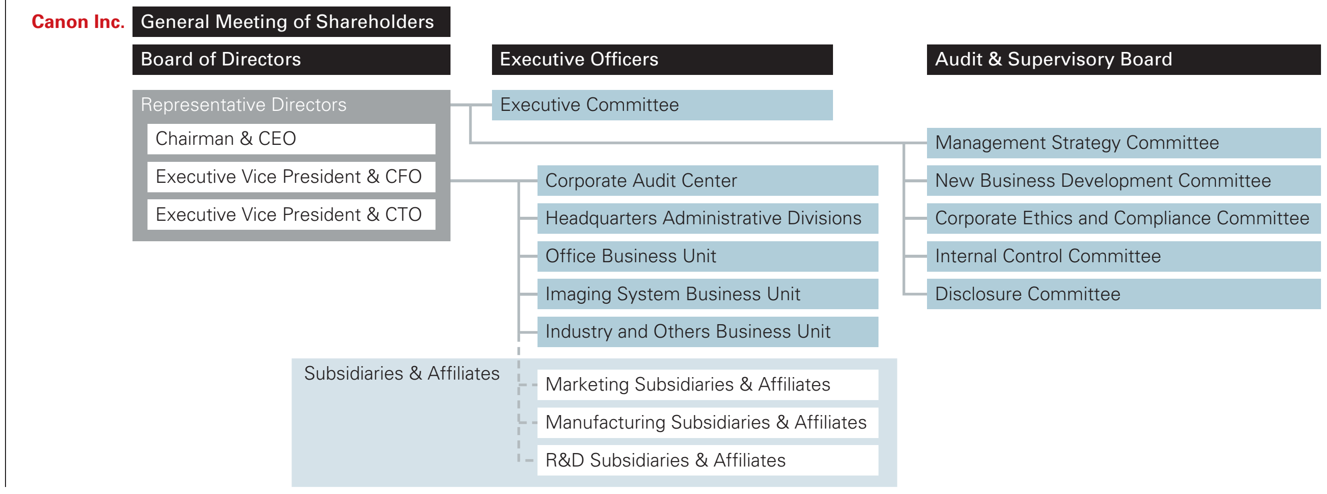
Kenichi Nagasawa
Group Executive, Corporate Intellectual Property & Legal Headquarters

Naoji Otsuka
Chief Executive, Inkjet Products Operations

Audit & Supervisory Board Members

Shunji Onda
Kengo Uramoto
Tadashi Ohe *(Outside)*
Kazunori Watanabe *(Outside)*
Kuniyoshi Kitamura *(Outside)*

Governance Structure *(as of December 31, 2012)*



EXECUTIVE OFFICER SYSTEM

Canon is endeavoring to realize more flexible and efficient management operations by maintaining an appropriately sized organization of directors and promoting capable human resources with accumulated executive knowledge across specific business areas.

Executive officers are appointed and dismissed by the Board of Directors and have a term of office of one year. The number of executive officers was 17 as of December 31, 2012.

AUDITING SYSTEM

Canon has five members on the Audit & Supervisory Board, including three outside corporate auditors who have no personal, capital or business affiliations with the Company. Canon has notified the stock exchanges in Tokyo, Osaka, Nagoya, Fukuoka and Sapporo of the designation of these outside members of the Audit & Supervisory Board as independent auditors, as provided under the regulations of the stock exchanges. Audit & Supervisory Board members' duties include attending meetings of the Board of Directors and of the Executive Committee, listening to business reports from directors, carefully examining documents related to important decisions and conducting strict audits of the Group's business and assets. Audit & Supervisory Board members also work closely with independent auditors and the Corporate Audit Center, which is in charge of monitoring the Company's compliance, risk management and internal control systems in addition to providing assessments and recommendations as required.

INTERNAL CONTROL COMMITTEE

In response to the Sarbanes-Oxley Act, including Section 404, which came into force during 2006, Canon continues to reinforce internal control systems and implement appropriate measures. The Internal Control Committee is responsible for Groupwide internal controls, including securing credibility of financial reporting.

In order to strengthen internal controls, Canon conducts comprehensive evaluations of internal controls across areas that include accounting, management oversight, legal compliance, IT systems and the promotion of corporate ethics. As of December 31, 2012, internal control over financial reporting has been assessed as effective by the management and an independent registered public accounting firm. (Please refer to pages 93 and 95.)

At Group companies worldwide, employees carry with them compliance cards.

OTHER COMMITTEES

The Corporate Ethics and Compliance Committee, in addition to the Disclosure Committee, is a key body of Canon's management committees. The Corporate Ethics and Compliance Committee reviews and approves policies and measures concerning law-abiding and corporate ethics matters. The Disclosure Committee works to ensure strict compliance with disclosure regulations as prescribed by stock exchanges.

COMPLIANCE

Shortly after its founding, Canon established the San-ji ("Three Selfs") Sprit principles: "self-motivation," or taking the initiative and being proactive in all things; "self-management," or conducting oneself responsibly and being accountable for all one's actions; and "self-awareness," or understanding one's situation and role in it. In 2001, Canon established the Canon Group Code of Conduct, inspired by the above Three Selfs. The Code has been translated into 13 languages from Japanese and each Group company makes efforts to enforce the Code.

Detailed policies and measures concerning the compliance activities of Canon are decided at the Corporate Ethics and Compliance Committee. With management by the Compliance Office, these policies and measures are mainly carried out by compliance leaders at each headquarters and Group company.

DISCLOSURE

Canon makes every effort to disclose information on its management and business strategies as well as its performance results to all stakeholders in an accurate, fair and timely manner. To this end, Canon holds regular briefings and posts the latest information on its website together with a broad range of disclosure materials.

Canon has formulated its own Disclosure Guidelines and

Significant Differences in Corporate Governance Practices between Canon and U.S. Companies Listed on the NYSE

Section 303A of the New York Stock Exchange (the "NYSE") Listed Company Manual (the "Manual") provides that companies listed on the NYSE must comply with certain corporate governance standards. However, foreign private issuers whose shares have been listed on the NYSE, such as Canon Inc. (the "Company"), are permitted, with certain exceptions, to follow the laws and practices of their home country in place of the corporate governance practices stipulated under the Manual. In such circumstances, the foreign private issuer is required to disclose the significant differences between the corporate governance practices under Section 303A of the Manual and those required in Japan. A summary of these differences as they apply to the Company is provided below.

1. Directors

Currently, the Company's board of directors does not have any director who could be regarded as an "independent director" under the NYSE Corporate Governance Rules for U.S. listed companies. Unlike the NYSE Corporate Governance Rules, the Corporation Law of Japan (the "Corporation Law") does not require Japanese companies with the Audit & Supervisory Board such as the Company, to appoint independent directors as members of the board of directors. The NYSE Corporate Governance Rules require non-management directors of U.S. listed companies to meet at regularly scheduled executive sessions without the presence of management. Unlike the NYSE Corporate Governance Rules, however, the Corporation Law does not require companies to implement an internal corporate organ or committee comprised solely of independent directors. Thus, the Company's board of directors currently does not include any non-management directors.

2. Committees

Under the Corporation Law, the Company may choose to:

(i) have an audit committee, nomination committee and compensation committee and abolish the post of the Audit & Supervisory Board Members; or

(ii) have the Audit & Supervisory Board.

The Company has elected to have the Audit & Supervisory Board, whose duties include monitoring and reviewing the management and reporting the results of these activities to the shareholders or board of directors of the Company. While the NYSE Corporate Governance Rules provide that U.S. listed companies must have an audit committee, nominating committee and compensation committee, each composed entirely of independent directors, the Corporation Law does not require companies to have specified committees, including those that are responsible for director nomination, corporate governance and executive compensation.

The Company's board of directors nominates candidates for directorships and submits a proposal at the general meeting of shareholders for shareholder approval. Pursuant to the Corporation Law, the shareholders then vote to elect directors at the meeting. The Corporation Law requires that the total amount or calculation method of compensation for directors and Audit & Supervisory Board Members be determined by a resolution of the general meeting of shareholders respectively, unless the amount or calculation method is provided under the Articles of Incorporation. As the Articles of Incorporation of the Company do not provide an amount or calculation method, the amount of compensation for the directors and the Audit & Supervisory Board Members of the Company is determined by a resolution of the general meeting of shareholders.

established the Disclosure Committee, which makes decisions regarding information disclosure, including necessity, content and timing. The Disclosure Committee makes such decisions after receiving reports on information that might need to be disclosed from the person in charge of the disclosure working group at each headquarters.

COUNTERING ANTISOCIAL FORCES

Canon has formulated a basic policy stipulating that no Canon Group company shall maintain relationships of any kind with antisocial forces that represent a threat to social order and security. To uphold this basic policy, Canon has established a department dedicated to activities aimed at countering such parties while reinforcing cooperative ties with applicable public authorities. In addition, Canon's Employment Regulations include a clause prohibiting such relationships, and the Company continues to step up efforts to ensure strict employee adherence.

RISK MANAGEMENT

As Canon pursues business expansion in various fields on a global scale, the business and other risks to which it may be exposed continue to diversify. With the goal of eliminating such risks altogether, while honoring the trust placed in it by its stakeholders, Canon works diligently to avoid or minimize its exposure, to this end assigning specifically designated management committees to address key issues.

In particular, the Executive Committee and various management committees engage in careful discussions regarding significant risk factors. The Corporate Audit Center preemptively identifies risk factors through audit activities. Also, Canon formulates in-house rules to guard against those risks and, in accordance with the policies formulated by the Internal Control Committee, strives to identify and assess relevant risks associated with individual business processes.

The allotment of compensation for each director from the total amount of compensation is determined by the Company's board of directors, and the allotment of compensation to each Audit & Supervisory Board Member is determined by consultation among the Company's Audit & Supervisory Board Members.

3. Audit Committee

The Company avails itself of paragraph (c)(3) of Rule 10A-3 of the Security Exchange Act, which provides that a foreign private issuer which has established the Audit & Supervisory Board shall be exempt from the audit committee requirements, subject to certain requirements which continue to be applicable under Rule 10A-3.

Pursuant to the requirements of the Corporation Law, the shareholders elect the Audit & Supervisory Board Members by resolution of a general meeting of shareholders. The Company currently has five Audit & Supervisory Board Members, although the minimum number of Audit & Supervisory Board Members required pursuant to the Corporation Law is three.

Unlike the NYSE Corporate Governance Rules, Japanese laws and regulations, including the Corporation Law, do not require the Audit & Supervisory Board Members to be experts in accounting or to have any other area of expertise. Under the Corporation Law, the Audit & Supervisory Board may determine the auditing policies and methods for investigating the business and assets of a Company, and may resolve other matters concerning the execution of the Audit & Supervisory Board Member's duties. The Audit & Supervisory Board prepares auditors' reports and may veto a proposal for the nomination of the Audit & Supervisory Board Members, accounting auditors and the determination of the amount of compensation for the accounting auditors put forward by the board of directors.

Under the Corporation Law, the half or more of a company's Audit & Supervisory Board Members must be "outside" Audit & Supervisory Board Members. These are individuals who are prohibited to have ever been a director, executive officer, manager, or employee of the Company or its subsidiaries. The Company's current Audit & Supervisory Board Member system meets these requirements. In addition, pursuant to the regulations of the Japanese stock exchanges, the Company is required to have one or more "independent director(s) or independent Audit & Supervisory Board Member(s)" which terms are defined under the relevant regulations of the Japanese stock exchanges as "outside directors" or "outside Audit & Supervisory Board Members" (each of which terms is defined under the Corporation Law) who are unlikely to have any conflict of interests with shareholders of the Company.

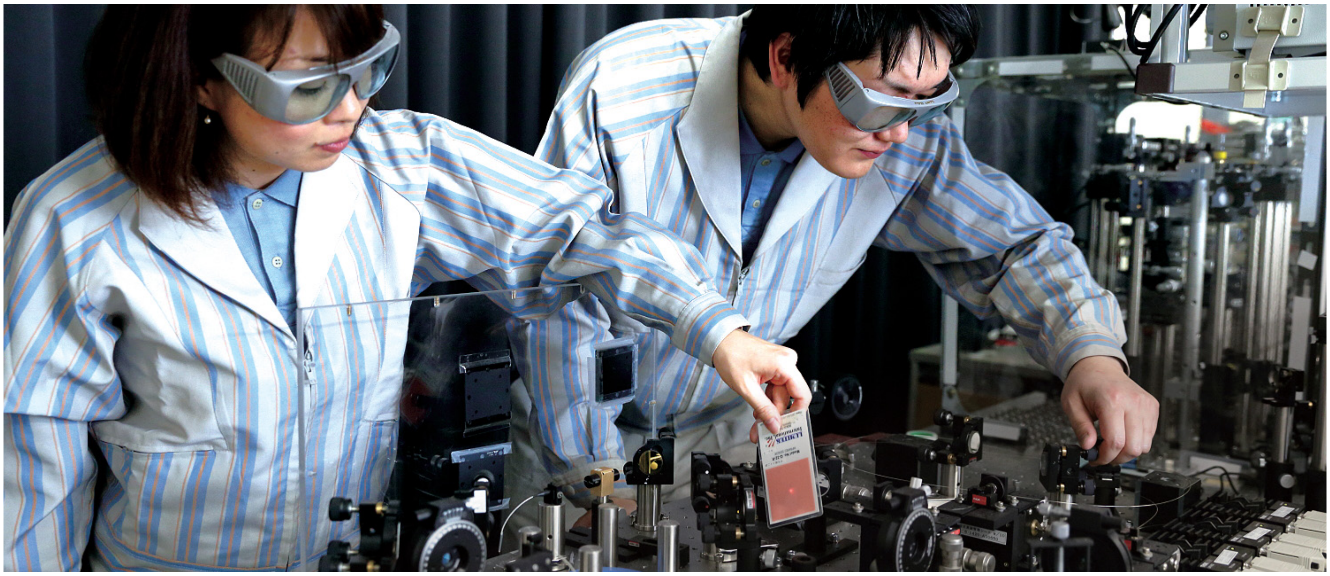
Among the five members on the Company's board of auditors, three are outside Audit & Supervisory Board Members. In addition, all such three outside Audit & Supervisory Board Members are also qualified as independent Audit & Supervisory Board Members under the regulations of the Japanese stock exchanges.

The qualifications for an "outside" or "independent" Audit & Supervisory Board Member under the Corporation Law or the regulations of the Japanese stock exchanges are different from the audit committee independence requirement under the NYSE Corporate Governance Rules.

4. Shareholder Approval of Equity Compensation Plans

The NYSE Corporate Governance Rules require that shareholders be given the opportunity to vote on all equity compensation plans and any material revisions of such plans, with certain limited exceptions. Under the Corporation Law, a Company is required to obtain shareholder approval regarding the stock options to be issued to directors and Audit & Supervisory Board Members as part of remuneration of directors and Audit & Supervisory Board Members.

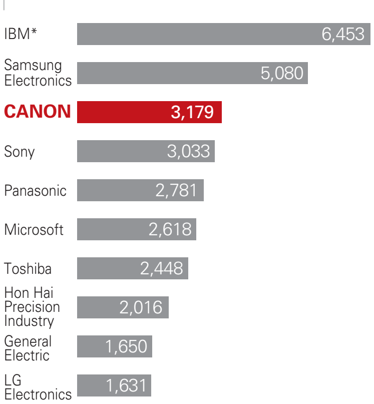
RESEARCH & DEVELOPMENT



Terahertz radiation, which lies between radio waves and visible light on the electromagnetic spectrum, make it possible to see the interior of opaque objects and evaluate their properties. Canon aims to contribute to a diverse array of fields where this technology can be applied, starting with healthcare, by forging ahead with terahertz imaging research.

Seeking new possibilities, Canon is establishing an R&D structure spanning Japan, the United States and Europe under the Three Regional Headquarters management system. At the same time, Canon will develop the medical and industrial fields into new business pillars.

2012 Top Ten U.S. Patent Holders by Company



*IBM is an abbreviation for International Business Machines Corporation.

Note: Number of patents for 2012 based on preliminary figures released by IFI CLAIMS Patent Services.

UPGRADING OUR GLOBAL R&D STRUCTURE

Canon's growth to date has been attributable to employing strong technologies to develop competitive products, mainly in Japan, and then disseminating those offerings around the world. Going forward, the Company will expand and upgrade its R&D organizations in Europe and the; United States, laying the foundation for the Three Regional Headquarters system that Canon envisions.

In the United States, Canon will set up centers to pursue activities ranging from research into fundamental technologies in healthcare and other new business fields to the application of cutting-edge technologies. In Europe, we will step up R&D in new business fields, spearheaded by existing R&D facilities.

R&D EXPENSES AND PATENTS

Canon is bolstering R&D activities to enable the ongoing development of innovative products and services. In the year under review, R&D expenses amounted to ¥296.5 billion, down 3.7%, or ¥11.3 billion, from the previous year. The ratio of R&D expenses to net sales was 8.5%. By segment, the Company allocated ¥99.5 billion (33.6% of total R&D expenses) to the Office Business Unit, ¥84.0 billion

(28.3%) to the Imaging System Business Unit, and ¥25.6 billion (8.6%) to the Industry and Others Business Unit. Basic R&D expenses not allocated to specific business units amounted to ¥87.4 billion (29.5%.) This focus on R&D activities has cemented Canon's high status in the field of intellectual property. In 2012, Canon was granted 3,179 patents in the United States, ranking it third in the world and the top-ranked Japanese company for an eighth successive year.

REINFORCING CORE TECHNOLOGIES

Canon is concentrating efforts on pre-competitive fields, involving research that can take more than ten years. At the same time, the Company is continually bolstering activities centered on key parts and key devices in order to enhance the competitiveness of its products. In CMOS image sensors, we successfully developed a 120-megapixel device. Going forward, we target further advances in ultrahigh-resolution and ultrahigh-sensitivity devices while also considering applications for these technologies in various fields other than digital cameras.

The CK project, collaboration between Canon and Kyoto University, targets the practical application of innovative medical imaging equipment. (Exterior of Clinical Research Center for Medical Equipment Development (CRCMeD) where the project has been proceeding)

MEDICAL AND INDUSTRIAL EQUIPMENT

Canon is working to establish two new business pillars: medical equipment and industrial equipment.

In medical device, for some years Canon has been involved in the "CK Project" in collaboration with Kyoto University. Under the project, two of our technologies have been brought to the clinical evaluation stage. One relates to a photoacoustic mammography device capable of diagnosing breast cancer more accurately than before, with minimal bodily impact during examination. The other relates to adaptive optics scanning laser ophthalmoscopy (AO-SLO), which contributes to the examination of the retina at the cellular level and the detection of lifestyle-related diseases. We have started clinical evaluation into AO-SLO with a number of universities and medical research institutes in Japan and abroad with the aim of commercializing this technology at an early stage. Meanwhile, Canon U.S.A., Inc. has established its R&D department to conduct joint research with Massachusetts General Hospital and Brigham and Women's Hospital, both affiliated with Harvard Medical School. This collaborative project focuses on development and commercialization of unique medical devices in the area of biomedical optical imaging and medical robotic technologies, among others. Accordingly, Canon is moving forward in establishing a global R&D system for medical devices.

Canon has integrated high-precision machine vision technology with information technology to develop intelligent robots that think and act on their own accord, one of many areas where it has applied these technologies.

In the industrial equipment field, Canon is working to develop intelligent robots and other systems through cutting-edge application technologies by integrating high-precision machine vision technology with information technology that operates as the brains of robotic systems. Canon is proceeding with R&D of these application technologies with a view to use them beyond intelligent robots in fields like risk prediction and the support and care of senior citizens.

PRODUCTION

"Man-machine cell" production systems integrate processes where robots excel with processes that can only be performed by people to sharply enhance the productivity of cell production systems. (Canon Hi-Tech Thailand Ltd.)

In addition to establishing a globally optimized production system, Canon seeks improved quality and productivity by putting a priority on conducting production operations itself to ensure the progress of its manufacturing expertise.

Reinforcement of Production Capacity

2012: Commenced operations

Mar. Canon Zhongshan Business Machines Co., Ltd.; expansion (China)
Laser printers

May Hita Canon Materials Inc. (Japan)
Toner cartridge parts

Jun. Canon Inc., Taiwan; expansion (Taiwan)
Lenses, digital cameras

2013: To commence operations

Apr. Canon Prachinburi (Thailand) Ltd. (Thailand)
Office multifunction devices, service parts

Apr. Canon Business Machines (Philippines), Inc. (Philippines)
Laser printers, accessories, parts

Jul. Canon Indústria de Manaus Ltda. (Brazil)
Digital cameras

ESTABLISHING A GLOBALLY OPTIMIZED PRODUCTION SYSTEM

Canon aims to establish a globally optimized production system that identifies the most suitable locations for the production of individual products based on a comprehensive assessment of various considerations. These factors include cost, taxation, logistics, the ease of parts procurement, and the workforce in each country and region. An optimized system will lead to additional improvements in productivity for the entire Canon Group.

In 2012, several manufacturing sites, including Hita Canon Materials Inc., started production. We also established new companies in Thailand, Philippines, and Brazil, where we are preparing to construct new production bases. In these ways, we are reinforcing our production system globally to meet growing demand for our products.

IMPROVING PRODUCTIVITY

Canon continues to expedite production in optimal locations. At the same time, by putting a priority on conducting production operations in-house, we proceed to raise quality and reduce costs through progress in manufacturing by making full use of the expertise and insights of individual workers engaged in production. To this end, the Company has adopted a cell production system—an approach that fully utilizes the creativity of individual workers. Canon continues to improve productivity by making efforts to increase production efficiencies in cell production while rolling out "man-machine cell" production systems that integrate manual and automated processes.

For some time, Canon has prioritized in-house manufacturing, especially of image sensors and other key parts. At present, we are broadening this strategy to include molds and production equipment, as well as automation of production itself. In the United States, for example, we have implemented a business model for toner cartridges that incorporates everything from automated production to sales, collection, and recycling in the region of consumption of our products, and we plan to apply this model in Europe as well. In Japan, moreover, we plan to automate the assembly process for interchangeable lenses for digital SLR cameras, which requires a high degree of precision, in 2013. In addition to creating high-value-added products, Canon will expedite efforts to raise productivity in order to strengthen the cost-competitiveness of manufacturing products in Japan.

Meanwhile, by implementing IT innovations that link development, design, production, logistics, and sales and seek to achieve further efficiencies, Canon aims to establish advanced supply chain management that is capable of withstanding fluctuations in demand.

ENVIRONMENTAL FRIENDLY MANUFACTURING; ENHANCED PRODUCT QUALITY

In addition to efforts aimed at boosting productivity, Canon promotes manufacturing operations that are friendly to the global environment while striving to improve overall product quality. With respect to manufacturing, in 2012 we prioritized purchases of environmentally friendly products and parts and actively shifted to transportation modes that have minimal environmental impact. In addition, we have changed our quality-related slogan from "Canon Quality" to "Quality as Priority: Customers' Safety, Smartness, and Satisfaction." To offer customers products that are safe while also providing peace of mind and satisfaction, we implement stringent quality control measures at every stage, from planning, development and production to sales and after-sales service.

The Canon Group internally manufactures functional parts, circuit boards and other major components, and even the molds and manufacturing equipment used to create parts. (Canon Precision Inc.)

Belief in "Internal Production"

In-House Production	Automation	Man-Machine Cell
• Cost Reduction • Product Differentiation •Technology Protection • Production Flexibility • Lead Time Reduction • Quality Improvement	• Production Efficiency Improvement • Production Localization	• Production Efficiency Improvement • Cost Reduction from Design Phase • Lead Time Reduction • Further Automation

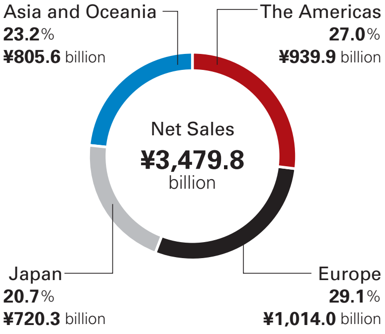
Internal Production

SALES & MARKETING

At the San Francisco showroom, recently opened by Canon Solutions America, Inc., visitors can experience a wide range of Canon products through displays and demonstrations of input to output devices such as office multifunction devices. In addition, workshops and classes of photography and photo printing are offered.

Canon reinforces its sales and marketing capabilities by providing innovative products and advanced solutions tailored to meet the characteristics of each region.

Composition of Sales by Region



GENERAL REVIEW

In all existing core businesses, Canon is strengthening its sales, marketing, and service capabilities by responding to actual conditions based on analyses of the features of each region.

In 2012, Canon sought to tap markets in China's regional cities, and also focused on upgrading its sales bases in India and other emerging nations.

In the office equipment sector, we forged strongly ahead with our strategy of integrating Canon's regional sales companies with the sales subsidiaries of Océ. This enabled us to offer a broad range of printing solutions. We also worked to bolster sales while expediting efforts to deliver advanced solutions and services that raise productivity.

For consumers, we launched products tailored to the market needs of specific countries and regions while taking steps to reinforce sales in emerging nations, with the aim of achieving sales expansion in excess of economic growth.

JAPAN

In the year under review, sales in Japan amounted to ¥720.3 billion, equivalent to 20.7% of consolidated net sales.

During the year, Canon opened the Nishi-Tokyo Data Center, which is one of the most advanced facilities of its type in Japan and is equipped with a multiple-level security system. In this way, we built a foundation for providing highly profitable outsourced services. Utilizing the Center, we also worked to expand and upgrade our cloud computing services.

In Russia, which entered the World Trade Organization in August, 2012, we are vigorously advancing our marketing activities. (A camera sales outlet in Moscow)

THE AMERICAS

In the Americas sales came to ¥939.9 billion (27.0% of consolidated net sales.)

Underscoring Canon's commitment to meet the needs of the film and television production industries, Canon U.S.A. expanded in 2012 the capabilities of its recently established Hollywood Professional Technology and Support Center, in order to strengthen its sales network and bolster service and support for professionals, including filmmakers utilizing the Cinema EOS System. Also, from June 2012, Canon reorganized its camera and video distribution strategy in Brazil to direct sales from distributor channels in an effort to expand its sales network within the country.

EUROPE (EUROPE, MIDDLE EAST, AFRICA)

In Europe sales amounted to ¥1,014.0 billion (29.1% of consolidated net sales.)

In 2012, under difficult economic circumstances, Canon Europe Ltd. further strengthened its sales and marketing functions in emerging markets, such as Russia and Ukraine, by increasing its sales force and through high profile marketing activities such as signing on as an official sponsor of UEFA EURO 2012, Europe's premier football tournament. In addition, Canon Europe has expedited expansion in the graphic arts field and business services field through the integration of Océ. This has contributed to broadened growth opportunities and its sales performance.

Canon is rapidly expanding its sales networks to meet strong demand from emerging markets. (Canon-brand shop in India)

ASIA AND OCEANIA

In 2012, sales in Asia and Oceania amounted to ¥805.6 billion, or 23.2% of consolidated net sales.

During the year, Canon (China) Co., Ltd. opened its fourth regional headquarters in Chengdu City, Sichuan Province, thus enhancing our responsiveness to growing demand in China's interior regions. In Vietnam, which has enjoyed high growth in recent years, we established Canon Marketing Vietnam Company Limited to accelerate efforts to build a framework for importing and selling Canon Group products. In Australia's challenging business environment, Canon worked to improve the efficiency of sales activities and increase the market share of its products in the local market.

CORPORATE SOCIAL RESPONSIBILITY

Canon Marketing (Thailand) Co., Ltd. has donated 29 electricity-generating wind turbines to schools across Thailand since it initiated the "Clean Energy for Green World" project in 2008.

Canon is promoting CSR activities with the aim of becoming a truly excellent global corporation that is admired and respected the world over.

Canon led the industry in launching a recycling program in Japan for ink cartridges in 1996 and has expanded the program's coverage area in the years since then.

CANON'S BASIC APPROACH TO CSR

Canon recognizes that its corporate activities are supported by the development of society as a whole, and contributes to the realization of a better society as a good corporate citizen, effectively leveraging its advanced technological strengths, global business deployment, and diverse, specialized human resources.

ENVIRONMENTAL ACTIVITIES

In line with "Action for Green," the Canon Environmental Vision, Canon strives to support both enriched lifestyles and the global environment.

In 2012, nine models among Canon's imageRUNNER ADVANCE series were approved under the CFP (Carbon Footprint of Products) Communication Program, operated by the Japan Environmental Management Association for Industry (JEMAI.) They were the first office multifunction devices to be approved under the program. The aim of the program is to allow "visualization" of the amount of greenhouse gas emitted over the entire lifecycle of products or services, from raw materials acquisition to disposal and/or recycling. The program also complies with ISO 14067, a set of requirements and guidelines for carbon footprint quantification and communication that is expected to become an international standard in 2013. Canon will continue pursuing CFP initiatives in its ongoing quest to understand and minimize the environmental impact of its activities across entire product lifecycles.

WWF

Canon Europe is a Conservation Imaging Partner of the World Wide Fund for Nature (WWF) and supports its activities such as projects that raise awareness of climate change in the Arctic.

In 2012, Canon Ambassador Thorsten Milse, a professional photographer, accompanied and worked with a team of WWF experts and scientists in the Last Ice Area expedition. He also dedicated his time to documenting the Arctic environment to raise awareness of the need for protection. Canon Europe renewed this partnership until 2014. Canon and WWF share the hope that the power of images will expose the state of the environment in the rapidly changing Arctic landscape.

Canon Europe is working with World Wide Fund for Nature (WWF) as a Conservation Imaging Partner with the aim of restoring and forestalling destruction of the earth's natural environment and creating a future where people and nature can coexist in harmony.
©Thorsten Milse, Canon Ambassador

Wildlife Protection in Yellowstone National Park

Canon U.S.A. supports "Eyes on Yellowstone," an educational and research program to manage and protect endangered wildlife species and promote education at Yellowstone National Park. Canon's imaging equipment has been used to monitor the lives of animals, create a video library, and gather information since 1995.

The "Eyes on Yellowstone" program releases videos of wildlife in their natural environment online. These videos are used to educate children around the world.

SOCIAL CONTRIBUTION ACTIVITIES

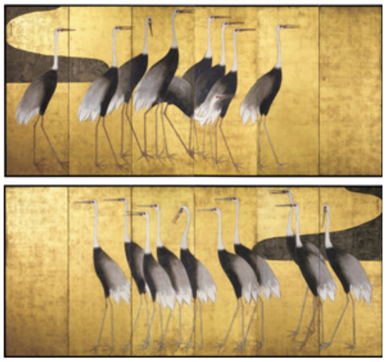
Canon conducts wide-ranging social contribution activities in all parts of the world, as a "good corporate citizen."

Third Assistance Program Decided by the Canon Foundation

The Canon Foundation was established with the aim of contributing to the lasting prosperity of human society and the welfare of mankind. It has designated research assistance programs in two domains: "Creation of industrial infrastructure" (contributing to industrial development) and "Pursuit of ideals" (targeting improved human wisdom.) In 2012, the Foundation decided on its third research assistance program, covering 17 specific projects.

The Tsuzuri Project

Canon and the non-profit organization Kyoto Culture Association jointly promote a project called the "Tsuzuri Project" (Official title: Cultural Heritage Inheritance Project.) The aim of the project is to preserve original cultural assets while maximizing the effective use of high-resolution facsimiles of cultural



In 2012, the Tsuzuri Project created a high-resolution facsimile of folding screens with pictures of flocks of cranes, which belong to the Freer Gallery of Art, Smithsonian Institution (Washington, D.C.), and donated them to the Tokyo Metropolitan Foundation for History and Culture.

assets. These facsimiles are created by blending Canon's latest digital technology and traditional Japanese crafts, such as gold leaf craftwork. As a result of the project, original cultural assets can be kept in the more favorable environment of museums while copies can be used for educational purposes and public exhibits. Since the program began in 2007, the cumulative total of items reproduced and donated under the project has reached 25 (as of December, 2012.)

"Colorful Classroom" Project Launched at "Hope Schools" in China

In 2012, Canon China teamed up with Nippon Paint Co., Ltd. and the China Youth Development Foundation (CYDF) to launch the "Colorful Classroom" project at three "Hope Schools" supported by China Canon Group. The aim of the project is to raise the observation skills, imaginative power, and aesthetic consciousness of Chinese children through images and colors. In addition to donating digital cameras, inkjet printers, and other devices, Canon sent employees to the schools to conduct photography classes for the children.

ADDRESSING THE ISSUE OF CONFLICT MINERALS

The term "conflict minerals" refers to certain minerals originating in the Democratic Republic of the Congo and adjoining countries in Africa, the profit from the trade of which, provided through the global supply chain, is alleged to be funding armed groups in that region. In the United States, legislation was enacted requiring publicly listed companies to disclose their usage of such minerals, which went into effect in January 2013.

Seeking to ensure that customers use its products with peace of mind, the Canon Group has clarified its basic stance on the issue, working together with business partners and industry entities with the aim of avoiding the use of conflict minerals. Canon has held briefing sessions for relevant domestic and overseas partners since November 2012, and launched conflict minerals inspections of its products since the end of January 2013, beginning with major products. In terms of both legal compliance and CSR, Canon is making steady progress in preparation for disclosing conflict minerals-related information to the U.S. Securities and Exchange Commission as scheduled in 2014.

Without regard to national origin, race, and other matters of background, Canon hires, trains, and promotes personnel that can excel as a member of a global enterprise so that it can grow sustainability as a global company.

CULTIVATING DIVERSE HUMAN RESOURCES

Canon works constantly to foster global human resources capable of performing on the world stage, by taking advantage of international training programs and the like. Given our priority to keep production in-house, it is important for us to cultivate personnel with world-class skills and expertise on a global scale. In 2012, we stepped up training programs aimed at acquiring the knowledge and skills necessary to advance our industrial equipment business, identified as a new core domain for Canon.

FINANCIAL SECTION

TABLE OF CONTENTS

FINANCIAL OVERVIEW

GENERAL

The following discussion and analysis provides information that management believes to be relevant to understanding Canon's consolidated financial condition and results of operations. References in this discussion to the "Company" are to Canon Inc. and, unless otherwise indicated, references to the financial condition or operating results of "Canon" refer to Canon Inc. and its consolidated subsidiaries.

OVERVIEW

Canon is one of the world's leading manufacturers of plain paper copying machines, office multifunction devices ("MFDs"), laser printers, cameras, inkjet printers, semiconductor lithography equipment and flat-panel -display ("FPD") lithography equipment. Canon earns revenues primarily from the manufacture and sale of these products domestically and internationally. Canon's basic management policy is to contribute to the prosperity and well-being of the world while endeavoring to become a truly excellent global corporate group targeting continued growth and development.

Canon divides its businesses into three segments: the Office Business Unit, the Imaging System Business Unit, and the Industry and Others Business Unit.

Economic environment

Looking back at the global economy in 2012, in the United States there were signs of improvement in employment conditions and housing issues as the economy continued to grow moderately. In Europe, the economic downturn in Southern European countries spread to Germany and other major countries, having a serious impact on the overall European economy. Economic growth in emerging markets such as China and India slowed down somewhat due to lagging exports and the effects of tight monetary policies. In Japan, despite the reconstruction demand seen at the beginning of the year from the previous year's earthquake in Japan and flooding in Thailand, the economy entered a phase of recession during the latter half of the year due to the slowdown in the global economy and reduced domestic demand. As for the global economy overall, the effects of the European financial crisis were felt worldwide, leading to a widespread slowdown.

Market environment

As for the markets in which Canon operates amid these conditions, while demand for office color MFDs showed growth in Japan and other regions, demand for laser printers remained sluggish mainly in European markets. Demand for interchangeable-lens digital cameras continued to display strong growth across global markets while demand for compact digital cameras shrunk not only in developed countries, but also in China and some emerging nations. Overall demand for inkjet printers also waned due to the weak economy. In the industry and others segment, demand for semiconductor lithography equipment remained restrained due to weak capital investment for memory devices while lithography equipment used in the production of FPD encountered sluggish demand for large-size FPD panels despite the healthy market for mid- and small-size FPD panels used mainly in smartphones and tablet PCs.

The average value of the yen during the year was ¥79.96 against the U.S. dollar, a slight depreciation compared with the previous year, and ¥102.80 against the euro, a year-on-year appreciation of approximately ¥8.

Summary of operations

Owing to the economic slowdown mainly in Europe and the high valuation of the yen against the euro, combined with the cooling off of demand in China during the latter half of the year, the Canon Group faced increasingly challenging conditions across all of its businesses. Amid this harsh environment, although Canon continued Group-wide efforts to expand sales, mainly for competitively priced products such as interchangeable-lens digital cameras and office equipment, net sales for the year declined 2.2% to ¥3,479.8 billion (U.S.$39,998 million). The gross profit ratio declined by 1.4 points year on year to 47.4% due to the significant impact of the strong yen and product mix. Thanks to Group-wide efforts to thoroughly reduce spending such as research and development ("R&D") expenses, operating expenses decreased by 2.4% to ¥1,326.1 billion (U.S.$15,243 million). Operating profit decreased 14.3% to ¥323.9 billion (U.S.$3,722 million). Other income (deductions) achieved a turnaround of ¥22.2 billion (U.S.$256 million) owing to an improvement in foreign currency exchange gain, resulting in income before income taxes of ¥342.6 billion (U.S.$3,937 million), a decrease of 8.5% year on year. Net income attributable to Canon Inc. decreased by 9.7% to ¥224.6 billion (U.S.$2,581 million) from the previous year.

Key performance indicators

The following are the key performance indicators ("KPIs") that Canon uses in managing its business. The changes from year to year in these KPIs are set forth in the table shown on page 35.

Revenues

As Canon pursues the goal to become a truly excellent global company, one indicator upon which Canon's management places strong emphasis is revenue. The following are some of the KPIs related to revenue that management considers to be important.

Net sales is one such KPI. Canon derives net sales primarily from the sale of products and, to a much lesser extent, provision of services associated with its products. Sales vary depending on such factors as product demand, the number and size of transactions within the reporting period, market acceptance for new products, and changes in sales prices. Other factors involved are market share and market environment. In addition, management considers the evaluation of net sales by segment to be important for the purpose of assessing Canon's sales performance in various segments, taking into account recent market trends.

Gross profit ratio (ratio of gross profit to net sales) is another KPI for Canon. Through its reforms of product development, Canon has been striving to shorten product development lead times in order to launch new, competitively priced products at a faster pace. Furthermore, Canon has further achieved cost reductions through enhancement of efficiency in its production. Canon believes that these achievements have contributed to improving Canon's gross profit ratio, and will continue pursuing the curtailment of product development lead times and reductions in production costs.

Operating profit ratio (ratio of operating profit to net sales) and R&D expense to net sales ratio are considered to be KPIs by Canon. Canon is focusing on two areas for improvement. Canon is striving to control and reduce its selling, general and administrative expenses as its first key point. Secondly, Canon's R&D policy is designed to maintain a certain level of spending in core technology to sustain Canon's leading position in its current business areas and to seek possibilities in other markets. Canon believes such investments will create the basis for future success in its business and operations.

Cash flow management

Canon also places significant emphasis on cash flow management. The following are the KPIs with regard to cash flow management that Canon's management believes to be important.

Inventory turnover measured in days is a KPI because it measures the adequacy of supply chain management. Inventories have inherent risks of becoming obsolete, physically damaged or otherwise decreasing significantly in value, which may adversely affect Canon's operating results. To mitigate these risks, management believes that it is crucial to continue reducing work-in-process inventories by decreasing production lead times in order to promptly recover related product expenses, while balancing risks of supply chain disruptions by optimizing finished goods inventories in order to avoid losing potential sales opportunities.

Canon's management seeks to meet its liquidity and capital requirements primarily with cash flow from operations. Management also seeks debt-free operations. For a manufacturing company like Canon, it generally takes considerable time to realize profit from a business as the process of R&D, manufacturing and sales has to be followed for success. Therefore, management believes that it is important to have sufficient financial strength so that the Company does not have to rely on external funds. Canon has continued to reduce its dependency on external funds for capital investments in favor of generating the necessary funds from its own operations.

Canon Inc. stockholders' equity to total assets ratio is another KPI for Canon. Canon believes that its stockholders' equity to total assets ratio measures its long-term sustainability. Canon also believes that achieving a high or rising stockholders' equity ratio indicates that Canon has maintained a strong financial position or further improved its ability to fund debt obligations and other unexpected expenses. In the long-term, Canon will be able to maintain a high level of stable investments for its future operations and development. As Canon puts strong emphasis on its R&D activities, management believes that it is important to maintain a stable financial base and, accordingly, a high level of its stockholders' equity to total assets ratio.

KEY PERFORMANCE INDICATORS

	2012	2011	2010	2009	2008
Net sales (Millions of yen)	**¥3,479,788**	¥3,557,433	¥3,706,901	¥3,209,201	¥4,094,161
Gross profit to net sales ratio	**47.4%**	48.8%	48.1%	44.5%	47.3%
R&D expense to net sales ratio	**8.5%**	8.7%	8.5%	9.5%	9.1%
Operating profit to net sales ratio	**9.3%**	10.6%	10.5%	6.8%	12.1%
Inventory turnover measured in days	**57 days**	46 days	35 days	39 days	47 days
Debt to total assets ratio	**0.1%**	0.3%	0.3%	0.3%	0.4%
Canon Inc. stockholders' equity to total assets ratio	**65.7%**	64.9%	66.4%	69.9%	67.0%

Note: Inventory turnover measured in days; Inventory divided by net sales for the previous six months, multiplied by 182.5.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and based on the selection and application of significant accounting policies which require management to make significant estimates and assumptions. These estimates and assumptions include future market conditions, net sales growth rate, gross margin and discount rate. Though Canon believes that the estimates and assumptions are reasonable, actual future results may differ from these estimates and assumptions. Canon believes that the following are the more critical judgment areas in the application of its accounting policies that currently affect its financial condition and results of operations.

Revenue recognition

Canon generates revenue principally through the sale of office and imaging system products, equipment, supplies, and related services under separate contractual arrangements. Canon recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred and title and risk of loss have been transferred to the customer or services have been rendered, the sales price is fixed or determinable, and collectibility is probable.

Revenue from sales of office products, such as office MFDs and laser printers, and imaging system products, such as digital cameras and inkjet printers, is recognized upon shipment or delivery, depending upon when title and risk of loss transfer to the customer.

Revenue from sales of optical equipment, such as semiconductor lithography equipment and FPD lithography equipment that are sold with customer acceptance provisions related to their functionality, is recognized when the equipment is installed at the customer site and the specific criteria of the equipment functionality are successfully tested and demonstrated by Canon. Service revenue is derived primarily from separately priced product maintenance contracts on equipment sold to customers and is measured at the stated amount of the contract and recognized as services are provided.

Canon also offers separately priced product maintenance contracts for most office products, for which the customer typically pays a stated base service fee plus a variable amount based on usage. Revenue from these service maintenance contracts is measured at the stated amount of the contract and recognized as services are provided and variable amounts are earned.

Revenue from the sale of equipment under sales-type leases is recognized at the inception of the lease. Income on sales-type leases and direct-financing leases is recognized over the life of each respective lease using the interest method. Leases not qualifying as sales-type leases or direct-financing leases are accounted for as operating leases and the related revenue is recognized ratably over the lease term. When equipment leases are bundled with product maintenance contracts, revenue is first allocated considering the relative fair value of the lease and non-lease deliverables based upon the estimated relative fair values of each element. Lease deliverables generally include equipment, financing and executory costs, while non-lease deliverables generally consist of product maintenance contracts and supplies.

For all other arrangements with multiple elements, Canon allocates revenue to each element based on its relative selling price if such element meets the criteria for treatment as a separate unit of accounting. Otherwise, revenue is deferred until the undelivered elements are fulfilled and accounted for as a single unit of accounting.

Canon records estimated reductions to sales at the time of sale for sales incentive programs including product discounts, customer promotions and volume-based rebates. Estimated reductions to sales are based upon historical trends and other known factors at the time of sale. In addition, Canon provides price protection to certain resellers of its products, and records reductions to sales for the estimated impact of price protection obligations when announced.

Estimated product warranty costs are recorded at the time revenue is recognized and are included in selling, general and administrative expenses. Estimates for accrued product warranty costs are based on historical experience, and are affected by ongoing product failure rates, specific product class failures outside of the baseline experience, material usage and service delivery costs incurred in correcting a product failure.

Allowance for doubtful receivables

Allowance for doubtful receivables is determined using a combination of factors to ensure that Canon's trade and financing receivables are not overstated due to uncollectibility. These factors include the length of time receivables are past due, the credit quality of customers, macroeconomic conditions and historical experience. Also, Canon records specific reserves for individual accounts when Canon becomes aware of a customer's inability to meet its financial obligations to Canon, such as in the case of bankruptcy filings or deterioration in the customer's operating results or financial position. If circumstances related to customers change, estimates of the recoverability of receivables would be further adjusted.

Valuation of inventories

Inventories are stated at the lower of cost or market value. Cost is determined by the average method for domestic inventories and principally the first-in, first-out method for overseas inventories. Market value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make a sale. Canon routinely reviews its inventories for their salability and for indications of obsolescence to determine if inventories should be written-down to market value. Judgments and estimates must be made and used in connection with establishing such allowances in any accounting period. In estimating the market value of its inventories, Canon considers the age of the inventories and the likelihood of spoilage or changes in market demand for its inventories.

Impairment of long-lived assets

Long-lived assets, such as property, plant and equipment, and acquired intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the carrying amount of the asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Determining the fair value of the asset involves the use of estimates and assumptions.

Property, plant and equipment

Property, plant and equipment are stated at cost. Depreciation is calculated principally by the declining-balance method, except for certain assets which are depreciated by the straight-line method over the estimated useful lives of the assets.

Goodwill and other intangible assets

Goodwill and other intangible assets with indefinite useful lives are not amortized, but are instead tested for impairment annually in the fourth quarter of each year, or more frequently if indicators of potential impairment exist. Canon performs its impairment test of goodwill using the two-step approach at the reporting unit level, which is one level below the operating segment level. All goodwill is assigned to the reporting unit or units that benefit from the synergies arising from each business combination. If the carrying amount assigned to the reporting unit exceeds the fair value of the reporting unit, Canon performs the second step to measure an impairment charge in the amount by which the carrying amount of a reporting unit's goodwill exceeds its implied fair value. Determining the fair value of the reporting unit involves the use of estimates and assumptions. Intangible assets with finite useful lives consist primarily of software, license fees, patented technologies and customer relationships. Software and license fees are amortized using the straight-line method over the estimated useful lives, which range from 3 years to 5 years for software and 5 years to 10 years for license fees. Patented technologies are amortized using the straight-line method principally over the estimated useful life of 3 years. Customer relationships are amortized principally using the declining-balance method over the estimated useful life of 5 years.

Income tax uncertainties

Canon considers many factors when evaluating and estimating income tax uncertainties. These factors include an evaluation of the technical merits of the tax positions as well as the amounts and probabilities of the outcomes that could be realized upon settlement. The actual resolutions of those uncertainties will inevitably differ from those estimates, and such differences may be material to the financial statements.

Valuation of deferred tax assets

Canon currently has significant deferred tax assets, which are subject to periodic recoverability assessments. Realization of Canon's deferred tax assets is principally dependent upon its achievement of projected future taxable income. Canon's judgments regarding future profitability may change due to future market conditions, its ability to continue to successfully execute its operating restructuring activities and other factors. Any changes in these factors may require possible recognition of significant valuation allowances to reduce the net carrying value of these deferred tax asset balances. When Canon determines that certain deferred tax assets may not be recoverable, the amounts, which may not be realized, are charged to income tax expense and will adversely affect net income.

Employee retirement and severance benefit plans

Canon has significant employee retirement and severance benefit obligations that are recognized based on actuarial valuations. Inherent in these valuations are key assumptions, including discount rates and expected return on plan assets. Management must consider current market conditions, including changes in interest rates, in selecting these assumptions. Other assumptions include assumed rate of increase in compensation levels, mortality rate, and withdrawal rate. Changes in these assumptions inherent in the valuation are reasonably likely to occur from period to period. Actual results that differ from the assumptions are accumulated and amortized over future periods and, therefore, generally affect future pension expenses. While management believes that the assumptions used are appropriate, the differences may affect employee retirement and severance benefit costs in the future.

In preparing its financial statements for fiscal 2012, Canon estimated a weighted-average discount rate of 1.9% for Japanese plans and 4.6% for foreign plans and a weighted-average expected long-term rate of return on plan assets of 3.1% for Japanese plans and 5.4% for foreign plans. In estimating the discount rate, Canon uses available information about rates of return on high-quality fixed-income governmental and corporate bonds currently available and expected to be available during the period to the maturity of the pension benefits. Canon establishes the expected long-term rate of return on plan assets based on management's expectations of the long-term return of the various plan asset categories in which it invests. Management develops expectations with respect to each plan asset category based on actual historical returns and its current expectations for future returns.

Decreases in discount rates lead to increases in actuarial pension benefit obligations which, in turn, could lead to an increase in service cost and amortization cost through amortization of actuarial gain or loss, a decrease in interest cost, and vice versa. For fiscal 2012, a decrease of 50 basis points in the discount rate increases the projected benefit obligation by approximately ¥83,396 million (U.S.$959 million). The net effect of changes in the discount rate, as well as the net effect of other changes in actuarial assumptions and experience, is deferred until subsequent periods.

Decreases in expected returns on plan assets may increase net periodic benefit cost by decreasing the expected return amounts, while differences between expected value and actual fair value of those assets could affect pension expense in the following years, and vice versa. For fiscal 2012, a change of 50 basis points in the expected long-term rate of return on plan assets would cause a change of approximately ¥3,725 million (U.S.$43 million) in net periodic benefit cost. Canon multiplies management's expected long-term rate of return on plan assets by the value of its plan assets, to arrive at the expected return on plan assets that is included in pension expense. Canon defers recognition of the difference between this expected return on plan assets and the actual return on plan assets. The net deferral affects future pension expense.

Canon recognizes the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of its pension plans in its consolidated balance sheets, with a corresponding adjustment to accumulated other comprehensive income (loss), net of tax.

CONSOLIDATED RESULTS OF OPERATIONS

SUMMARY OF OPERATIONS

	Millions of yen					*Thousands of U.S. dollars*
	2012	change	2011	change	2010	**2012**
Net sales	**¥3,479,788**	**-2.2%**	¥3,557,433	-4.0%	¥3,706,901	**$39,997,563**
Operating profit	**323,856**	**-14.3%**	378,071	-2.4%	387,552	**3,722,483**
Income before income taxes	**342,557**	**-8.5%**	374,524	-4.7%	392,863	**3,937,437**
Net income attributable to Canon Inc.	**224,564**	**-9.7%**	248,630	+0.8%	246,603	**2,581,195**

Sales

Canon's consolidated net sales in fiscal 2012 totaled ¥3,479,788 million (U.S.$39,998 million), representing a 2.2% decrease from the previous fiscal year. This decrease of net sales was due primarily to economic slowdown mainly in Europe and the high valuation of the yen against the euro combined with the cooling off of demand in China during the latter half of the year. Canon Group faced increasingly challenging conditions across all of its businesses.

Overseas operations are significant to Canon's operating results and generated 79.3% of total net sales in fiscal 2012. Such sales are denominated in the applicable local currency and are subject to fluctuations in the value of the yen to those currencies. Despite efforts to reduce the impact of currency fluctuations on operating results, including localization of manufacturing in some regions along with procuring parts and materials from overseas suppliers, Canon believes such fluctuations have had and will continue to have a significant effect on its results of operations.

The average value of the yen in fiscal 2012 was ¥79.96 to the U.S. dollar, and ¥102.80 to the euro, representing a slight depreciation to the U.S. dollar, and an appreciation of approximately ¥8 against the euro, compared with the previous year. The effects of foreign exchange rate fluctuations negatively affected net sales by approximately ¥54,300 million in fiscal 2012. This impact consisted of approximately ¥69,200 million of unfavorable impact for euro denominated sales and favorable impact of ¥9,500 million for the U.S. dollar denominated sales and ¥5,400 million for other foreign currency denominated sales.

Cost of sales

Cost of sales principally reflects the cost of raw materials, parts and labor used by Canon in the manufacture of its products. A portion of the raw materials used by Canon is imported or includes imported materials. Many of these raw materials are subject to fluctuations in world market prices accompanied by fluctuations in foreign exchange rates that may affect Canon's cost of sales. Other components of cost of sales include depreciation expenses, maintenance expenses, light and fuel expenses, and rent expenses. The ratio of cost of sales to net sales for fiscal 2012 and 2011 was 52.6% and 51.2%, respectively.

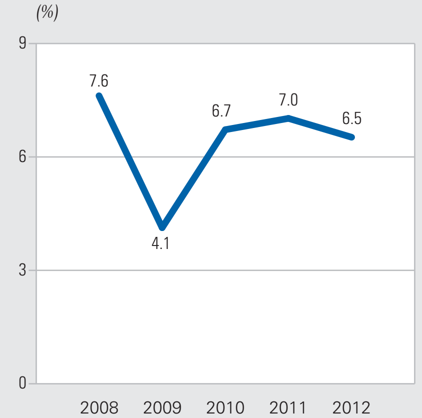
Gross profit

Canon's gross profit in fiscal 2012 decreased by 5.0% to ¥1,649,966 million (U.S.$18,965 million) from fiscal 2011. The gross profit ratio declined by 1.4 points year on year to 47.4%. The deteriorated gross profit ratio was mainly the result of such factors as the sharp appreciation of the yen to the euro and falling product prices accompanied by the rise in prices of materials.

Operating expenses

The major components of operating expenses are payroll, R&D, advertising expenses and other marketing expenses. Owing to Group-wide efforts to thoroughly reduce spending, total operating expenses decreased by 2.4% to ¥1,326,110 million (U.S.$15,243 million) in fiscal 2012.

Return on Sales
(%)



Operating profit

Operating profit in fiscal 2012 decreased 14.3% to a total of ¥323,856 million (U.S.$3,722 million) from fiscal 2011. The ratio of operating profit to net sales decreased 1.3% to 9.3% from fiscal 2011.

Other income (deductions)

Other income (deductions) for fiscal 2012 achieved a turnaround of ¥22,248 million (U.S.$256 million), owing primarily to an improvement in foreign currency exchange gain.

Income before income taxes

Income before income taxes in fiscal 2012 was ¥342,557 million (U.S.$3,937 million) a decrease of 8.5% from fiscal 2011, and constituted 9.8% of net sales.

Income taxes

Provision for income taxes in fiscal 2012 decreased by ¥10,303 million (U.S.$118 million) from fiscal 2011. The effective tax rate during fiscal 2012 remained consistent with fiscal 2011. The effective tax rate for fiscal 2012 was 32.1%, which was lower than the statutory tax rate in Japan. This was mainly due to the increase in tax credit for R&D expenses.

Net income attributable to Canon Inc.

As a result, net income attributable to Canon Inc. in fiscal 2012 decreased by 9.7% to ¥224,564 million (U.S.$2,581 million), which represents 6.5% of net sales.

Segment information

Canon divides its businesses into three segments: the Office Business Unit, the Imaging System Business Unit and the Industry and Others Business Unit.

- **The Office Business Unit** mainly includes Office MFDs / Office copying machines / Personal-use copying machines / Laser MFDs / Laser printers / Digital production printing systems / High speed continuous feed printers / Wide-format printers / Document solution
- **The Imaging System Business Unit*** mainly includes Interchangeable-lens digital cameras / Compact digital cameras / Digital camcorders / Digital cinema cameras / Interchangeable lenses / Inkjet printers / Large-format inkjet printers / Commercial photo printers / Image scanners / Broadcast equipment / Calculators
- **The Industry and Others Business Unit** mainly includes Semiconductor lithography equipment / FPD lithography equipment / Digital radiography systems / Ophthalmic equipment / Vacuum thin-film deposition equipment / Organic LED panel manufacturing equipment / Micromotors / Computers / Handy terminals / Document scanners

* The "Consumer Business Unit" has been renamed the "Imaging System Business Unit" to be more consistent with its strategy to expand the business. This change in segment description has no impact on any financial information of this segment.

Sales by segment

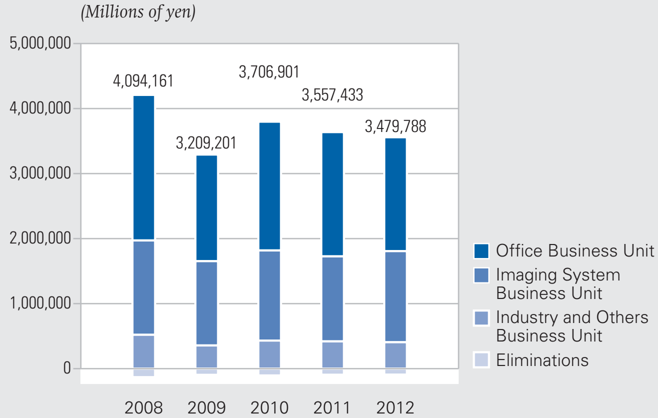
Please refer to the table of sales by segment in Note 23 of the Notes to Consolidated Financial Statements.

Canon's sales by segment are summarized as follows:

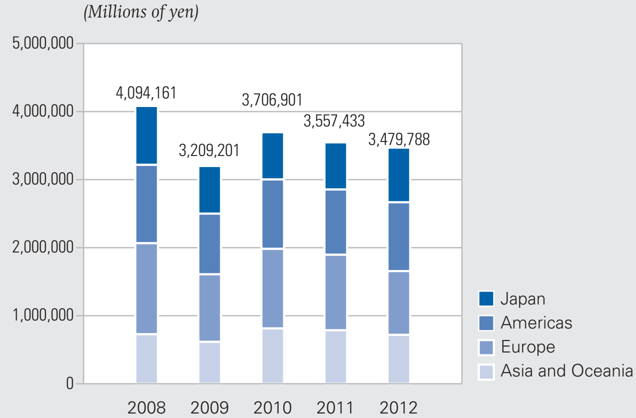
SALES BY SEGMENT

	Millions of yen					Thousands of U.S. dollars
	2012	change	2011	change	2010	**2012**
Office	**¥1,757,575**	**-8.4%**	¥1,917,943	-3.5%	¥1,987,269	**$20,202,011**
Imaging System	**1,405,971**	**+7.2%**	1,312,044	-5.7%	1,391,327	**16,160,586**
Industry and Others	**407,840**	**-3.1%**	420,863	-2.8%	432,958	**4,687,816**
Eliminations	**(91,598)**	**—**	(93,417)	—	(104,653)	**(1,052,850)**
Total	**¥3,479,788**	**-2.2%**	¥3,557,433	-4.0%	¥3,706,901	**$39,997,563**

Sales by Segment
(Millions of yen)



Sales by Geographic Area
(Millions of yen)



Sales of the Office Business Unit constituting 50.5% of consolidated net sales. Sales volume of both monochrome and color MFDs increased, favored by the continued strong demand for color MFDs, such as imageRUNNER ADVANCE C5000/C2000-series models. As for laser printers, sales volumes declined mainly in Europe due to deterioration in business sentiment. Consequently, combined with the appreciation of the yen, sales for the segment totaled ¥1,757,575 million (U.S.$20,202 million), a decline of 8.4% in fiscal 2012.

Sales of the Imaging System Business Unit constituting 40.4% of consolidated net sales. Sales of interchangeable-lens digital cameras increased thanks to the competitively priced EOS Rebel series along with the EOS 5D Mark III and EOS 60D advanced-amateur models. As for compact digital cameras, despite the significant deterioration of market conditions, sales volume remained at the same level as the previous year thanks to robust sales of the PowerShot ELPH 110 HS and PowerShot A2300. With respect to inkjet printers, sales volume surpassed that for the year-ago period owing to the early restoration of production following the flooding in Thailand. Furthermore, the company successfully entered new markets with the launch of its CINEMA EOS SYSTEM lineup of professional cinematography products, targeting Hollywood and the broader motion picture and television production market, along with the new DreamLabo 5000, targeting the commercial photo printing market. As a result, amid the effects of the strong yen, sales for the segment increased by 7.2% year on year to ¥1,405,971 million (U.S.$16,161 million) in fiscal 2012.

Sales of the Industry and Others Business Unit constituted 11.7% of consolidated net sales in fiscal 2012. Among semiconductor lithography equipment, while sales of i-line steppers remained at the same level as the previous year owing to demand for image sensors and LED elements, sales volume overall decreased due to restrained capital expenditure for memory devices. As for FPD lithography equipment, unit sales dropped substantially in the face of shrinking demand for equipment used in the production of large-size panels, an area in which Canon is particularly strong. Consequently, combined with the appreciation of the yen, sales for the segment totaled ¥407,840 million (U.S.$4,688 million), a decrease of 3.1% year on year in fiscal 2012.

Intersegment sales of ¥91,598 million (U.S.$1,053 million), representing 2.6% of total sales, are eliminated from the total sales of the three segments, and are described as "Eliminations."

Sales by geographic area

Please refer to the table of sales by geographic area in Note 23 of the Notes to Consolidated Financial Statements.

A geographical analysis indicates that net sales in fiscal 2012 increased in Japan and Asia and Oceania while decreased in Americas and Europe.

In Japan, sales increased by 3.7% in fiscal 2012 supported by the moderate economic recovery.

In the Americas, despite the admirable sales performance of interchangeable-lens digital cameras and solid growth in MFDs, laser printer market weakness caused sales to decline by 2.3% in fiscal 2012.

In Europe, although interchangeable-lens digital cameras showed solid growth, weak demand for laser printers along with the sharp appreciation of the yen against the euro caused sales to decrease by 8.9% in fiscal 2012.

In Asia and Oceania, although the speed of economic expansion in China slowed down slightly in the latter half of the year, owing to the solid demand for interchangeable-lens digital cameras in emerging economies, net sales increased by 2.2% in fiscal 2012.

A summary of net sales by geographic area is provided below.

Operating profit by segment

Please refer to the table of segment information in Note 23 of the Notes to Consolidated Financial Statements.

Operating profit for the Office Business Unit in fiscal 2012 decreased by ¥55,687 million (U.S.$640 million) to ¥203,578 million (U.S.$2,340 million). This decrease resulted from the decrease in sales and appreciation of the yen against the euro.

Operating profit for the Imaging System Business Unit in fiscal 2012 decreased by ¥976 million (U.S.$11 million) to ¥210,318 million (U.S.$2,417 million). This decrease resulted primarily from the appreciation of the yen against the euro.

Operating profit for the Industry and Others Business Unit in fiscal 2012 declined by ¥18,390 million (U.S.$211 million), largely owing to the decrease in sales.

SALES BY REGION

	Millions of yen					*Thousands of U.S. dollars*
	2012	change	2011	change	2010	**2012**
Japan	**¥ 720,286**	**+3.7%**	¥ 694,450	-0.2%	¥ 695,749	**$ 8,279,149**
Americas	**939,873**	**-2.3%**	961,955	-6.0%	1,023,299	**10,803,138**
Europe	**1,014,038**	**-8.9%**	1,113,065	-5.1%	1,172,474	**11,655,609**
Asia and Oceania	**805,591**	**+2.2%**	787,963	-3.4%	815,379	**9,259,667**
Total	**¥3,479,788**	**-2.2%**	¥3,557,433	-4.0%	¥3,706,901	**$39,997,563**

Note: This summary of net sales by geographic area is determined by the location where the product is shipped to the customers.

FOREIGN OPERATIONS AND FOREIGN CURRENCY TRANSACTIONS

Canon's marketing activities are performed by subsidiaries in various regions in local currencies, while the cost of sales is generally in yen. Given Canon's current operating structure, appreciation of the yen has a negative impact on net sales and the gross profit ratio. To reduce the financial risks from changes in foreign exchange rates, Canon utilizes derivative financial instruments, which consist principally of forward currency exchange contracts.

The operating profit on foreign operation sales is usually lower than that from domestic operations because foreign operations consist mainly of marketing activities. Marketing activities are generally less profitable than production activities, which are mainly conducted by the Company and its domestic subsidiaries. Please refer to the table of geographic information in Note 23 of the Notes to Consolidated Financial Statements.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents in fiscal 2012 decreased by ¥106,549 million (U.S.$1,225 million) to ¥666,678 million (U.S.$7,663 million), compared with ¥773,227 million in fiscal 2011 and ¥840,579 million in fiscal 2010. Canon's cash and cash equivalents are typically denominated both in Japanese yen and in U.S. dollar, with the remainder denominated in foreign currencies.

Net cash provided by operating activities in fiscal 2012 decreased by ¥85,485 million (U.S.$983 million) from the previous year to ¥384,077 million (U.S.$4,415 million). Cash flow from operating activities consisted of the following key components: the major component of Canon's cash inflow is cash received from customers, and the major components of Canon's cash outflow are payments for parts and materials, selling, general and administrative expenses, R&D expenses and income taxes.

For fiscal 2012, cash inflow from cash received from customers decreased due to the decrease of sales. There were no significant changes in Canon's collection rates. Cash outflow for payments for parts and materials increased, as a result of our efforts to optimize inventory levels in order to avoid losing potential sales opportunities while simultaneously increasing flexibility in response to unexpected risks and events. This has led to an increase in inventory turnover days. Cash outflow for payments for selling, general and administrative expenses decreased owing to thorough spending cuts across the Canon Group implemented after the earthquake in fiscal 2011 to control expenses more efficiently. Cash outflow for income taxes decreased due to decrease of taxable income.

Net cash used in investing activities in fiscal 2012 was ¥212,740 million (U.S.$2,445 million), decreasing by ¥43,803 million (U.S.$503 million), from ¥256,543 million in fiscal 2011, due to the net effect of increased capital investment focused on boosting production and reducing the amount of time deposits included in short-term investments. The purchases of fixed assets, which totaled ¥316,211 million (U.S.$3,635 million) in fiscal 2012, were focused on items relevant to raising production capacity and reducing production cost.

Canon defines "free cash flow" by deducting the cash flows from investing activities from the cash flows from operating activities. For fiscal 2012, free cash flow totaled ¥171,337 million (U.S.$1,970 million) as compared with ¥213,019 million for fiscal 2011. Canon's management recognizes that constant and intensive investment in facilities and R&D is required to maintain and strengthen the competitiveness of its products. Canon's management seeks to meet its capital requirements with cash flow principally earned from its operations. Therefore, its capital resources are primarily sourced from internally generated funds. Accordingly, Canon has included the information with regard to free cash flow as its management frequently monitors this indicator, and believes that such indicator is beneficial to the understanding of investors. Furthermore, Canon's management believes that this indicator is significant in understanding Canon's current liquidity and the alternatives of use in financing activities because it takes into consideration its operating and investing activities. Canon refers to this indicator together with relevant U.S. GAAP financial measures shown in its consolidated statements of cash flows and consolidated balance sheets for cash availability analysis.

Net cash used in financing activities totaled ¥319,739 million (U.S.$3,675 million) in fiscal 2012, mainly resulting from repurchase of treasury stock of ¥149,968 million (U.S.$1,724 million), and the dividend payout of ¥142,362 million (U.S.$1,636 million). The Company paid dividends in fiscal 2012 of ¥120.00 per share.

To the extent Canon relies on external funding for its liquidity and capital requirements, it generally has access to various funding sources, including the issuance of additional share capital, long-term debt or short-term loans. While Canon has been able to obtain funding from its traditional financing sources and from the capital markets, and believes it will continue to be able to do so in the future, there can be no assurance that adverse economic or other conditions will not affect Canon's liquidity or long-term funding in the future.

Short-term loans (including the current portion of long-term debt) amounted to ¥1,866 million (U.S.$21 million) at December 31, 2012 compared with ¥8,343 million at December 31, 2011. Long-term debt (excluding the current portion) amounted to ¥2,117 million (U.S.$24 million) at December 31, 2012 compared with ¥3,368 million at December 31, 2011.

Canon's long-term debt mainly consists of lease obligations.

In order to facilitate access to global capital markets, Canon obtains credit ratings from two rating agencies: Moody's Investors Services, Inc. ("Moody's") and Standard and Poor's Ratings Services ("S&P"). In addition, Canon maintains a rating from Rating and Investment Information, Inc. ("R&I"), a rating agency in Japan, for access to the Japanese capital market.

As of March 15, 2013, Canon's debt ratings are: Moody's: Aa1 (long-term); S&P: AA (long-term), A-1+ (short-term);

and R&I: AA+ (long-term). Canon does not have any rating downgrade triggers that would accelerate the maturity of a material amount of its debt. A downgrade in Canon's credit ratings or outlook could, however, increase the cost of its borrowings.

Increase in property, plant and equipment on an accrual basis in fiscal 2012 amounted to ¥270,457 million (U.S.$3,109 million) compared with ¥226,869 million in fiscal 2011 and ¥158,976 million in fiscal 2010. For fiscal 2013, Canon projects its increase in property, plant and equipment will be approximately ¥265,000 million (U.S.$3,046 million).

Employer contributions to Canon's worldwide defined benefit pension plans were ¥30,421 million (U.S.$350 million) in fiscal 2012, ¥30,510 million in fiscal 2011, and ¥21,435 million in fiscal 2010. In addition, employer contributions to Canon's worldwide defined contribution pension plans were ¥13,021 million (U.S.$150 million) in fiscal 2012, ¥12,511 million in fiscal 2011, and ¥11,780 million in fiscal 2010.

Working capital in fiscal 2012 decreased by ¥21,636 million (U.S.$249 million), to ¥1,237,821 million (U.S.$14,228 million), compared with ¥1,259,457 million in fiscal 2011 and ¥1,233,488 million in fiscal 2010. Canon believes its working capital will be sufficient for its requirements for the foreseeable future. Canon's capital requirements are primarily dependent on management's business plans regarding the levels and timing of purchases of fixed assets and investments. The working capital ratio (ratio of current assets to current liabilities) for fiscal 2012 was 2.47 compared to 2.41 for fiscal 2011 and to 2.38 for fiscal 2010.

Return on assets (net income attributable to Canon Inc. divided by the average of total assets) was 5.7% in fiscal 2012, compared to 6.3% in fiscal 2011 and 6.3% in fiscal 2010.

Return on Canon Inc. stockholders' equity (net income attributable to Canon Inc. divided by the average of total Canon Inc. stockholders' equity) was 8.7% in fiscal 2012 compared with 9.6% in fiscal 2011 and 9.2% in fiscal 2010.

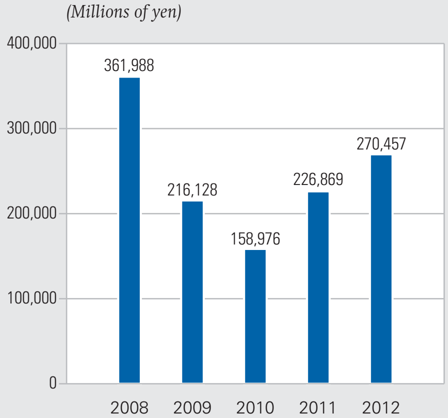
The debt to total assets ratio was 0.1%, 0.3% and 0.3% as of December 31, 2012, 2011 and 2010, respectively. Canon had short-term loans and long-term debt of ¥3,983 million (U.S.$46 million) as of December 31, 2012, ¥11,711 million as of December 31, 2011 and ¥11,331 million as of December 31, 2010.

OFF-BALANCE SHEET ARRANGEMENTS

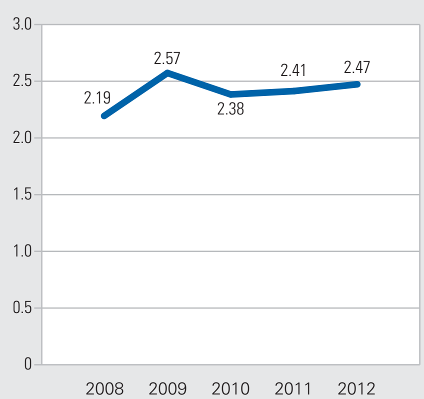
As part of its ongoing business, Canon does not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Canon provides guarantees for bank loans of its employees, affiliates and other companies. Canon would have to perform under a guarantee if the borrower defaults on a payment within the contract periods of 1 year to 30 years in the case of employees with housing loans, and 1 year to 10 years in the case of affiliates and other companies. The maximum amount of undiscounted payments Canon would have had to make in the event of default by all borrowers was ¥13,333 million (U.S.$153 million) at December 31, 2012. The carrying amounts of the liabilities recognized for Canon's obligations as a guarantor under those guarantees at December 31, 2012 were insignificant.

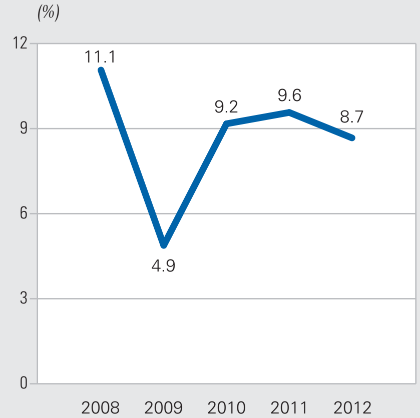
Increase in Property, Plant and Equipment
(Millions of yen)



Working Capital Ratio



Return on Canon Inc. Stockholders' Equity
(%)



CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following summarizes Canon's contractual obligations at December 31, 2012.

		Payments due by period			
Millions of yen	***Total***	*Less than 1 year*	*1-3 years*	*3-5 years*	*More than 5 years*
Contractual obiligations:					
Long-term debt:					
Capital lease obligations	**¥ 3,535**	¥ 1,503	¥ 1,775	¥ 243	¥ 14
Other long-term debt	**129**	44	35	30	20
Operating lease obligations	**75,807**	25,101	27,808	13,152	9,746
Purchase commitments for:					
Property, plant and equipment	**39,520**	39,520	—	—	—
Parts and raw materials	**65,311**	65,311	—	—	—
Other long-term liabilities:					
Contribution to defined benefit pension plans	**40,064**	40,064	—	—	—
Total	**¥224,366**	¥171,543	¥29,618	¥13,425	¥9,780

Note: The table does not include provisions for uncertain tax positions and related accrued interest and penalties, as the specific timing of future payments related to these obligations cannot be projected with reasonable certainty. See Note 13, Income Taxes in the Notes to Consolidated Financial Statements for further details. Contribution to defined benefit pension plans reflects the expected amount only for the next fiscal year, since contributions beyond the next fiscal year are not currently determinable due to uncertainties related to changes in actuarial assumptions, returns on plan assets and changes to plan membership.

		Payments due by period			
Thousands of U.S. dollars	***Total***	*Less than 1 year*	*1-3 years*	*3-5 years*	*More than 5 years*
Contractual obiligations:					
Long-term debt:					
Capital lease obligations	**$ 40,632**	$ 17,276	$ 20,402	$ 2,793	$ 161
Other long-term debt	**1,483**	506	402	345	230
Operating lease obligations	**871,345**	288,517	319,632	151,172	112,024
Purchase commitments for:					
Property, plant and equipment	**454,253**	454,253	—	—	—
Parts and raw materials	**750,701**	750,701	—	—	—
Other long-term liabilities:					
Contribution to defined benefit pension plans	**460,506**	460,506	—	—	—
Total	**$2,578,920**	$1,971,759	$340,436	$154,310	$112,415

Canon provides warranties of generally less than one year against defects in materials and workmanship on most of its consumer products. Estimated product warranty related costs are established at the time revenue are recognized and are included in selling, general and administrative expenses. Estimates for accrued product warranty costs are primarily based on historical experience, and are affected by ongoing product failure rates, specific product class failures outside of the baseline experience, material usage and service delivery costs incurred in correcting a product failure. As of December 31, 2012, accrued product warranty costs amounted to ¥12,163 million (U.S.$140 million).

At December 31, 2012, commitments outstanding for the purchase of property, plant and equipment were approximately ¥39,520 million (U.S.$454 million), and commitments outstanding for the purchase of parts and raw materials were approximately ¥65,311 million (U.S.$751 million), both for use in the ordinary course of its business. Canon anticipates that funds needed to fulfill these commitments will be generated internally through operations.

During fiscal 2013, Canon expects to contribute ¥18,610 million (U.S.$214 million) to its Japanese defined benefit pension plans and ¥21,454 million (U.S.$247 million) to its foreign defined benefit pension plans.

Canon's management believes that current financial resources, cash generated from operations and Canon's potential capacity for additional debt and/or equity financing will be sufficient to fund current and future capital requirements.

RESEARCH AND DEVELOPMENT, PATENTS AND LICENSES

Year 2012 marks the second year of the Excellent Global Corporation Plan, its 5-year (2011–2015) management plan. The slogan of the fourth phase ("Phase IV") is "Aiming for the Summit - Speed & Sound Growth" and there are three core strategies related to R&D:

- Achieve the overwhelming No.1 position in all core businesses and expand related and peripheral businesses;
- Develop new business through globalized diversification and establish the Three Regional Headquarters management system; and
- Build the foundations of an environmentally advanced corporation.

Canon has been striving to implement the three R&D related strategies as follows:

- Achieve the overwhelming No.1 position in all core businesses and expand related and peripheral businesses: Continue to introduce competitive products through innovation and aim at gaining profit through solutions and services.
- Develop new business through globalized diversification and establish the Three Regional Headquarters management system: Reinforce the businesses of commercial printing sector, medical imaging sector, industrial equipment sector and security and safety sector to develop into Canon's new pillars. Seek talents in Japan, US, and Europe to foster promising technologies and enhance R&D capabilities in global-scale dimensions by enabling product development in specialized area of each region, with actively utilizing M&A.
- Build the foundations of an environmentally advanced corporation: Focus on energy- and resource-conserving technologies to create products with the highest environmental performance.

Canon has developed and strengthened relationships with universities and other research institutes, such as Kyoto University, Tokyo Institute of Technology, Osaka University, Stanford University, the University of Arizona, the New Energy and Industrial Technology Development Organization and the National Institute of Advanced Industrial Science and Technology to assist with fundamental research and to develop cutting-edge technologies. Additionally, Canon has entered into respective collaborative research agreements with Massachusetts General Hospital (MGH) and Brigham and Women's Hospital (BWH) to develop and commercialize unique medical devices.

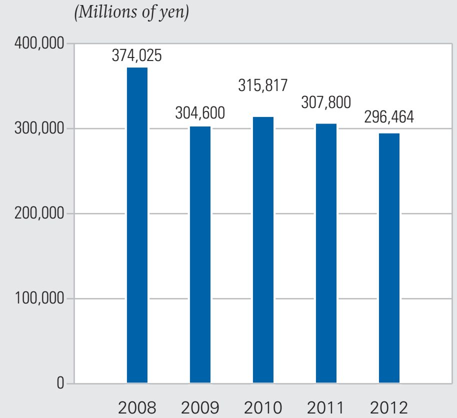
Canon has fully introduced 3D-CAD systems across the Canon Group, boosting R&D efficiency to curtail product development times and costs. Moreover, Canon enhanced and evolved its simulation, measurement, and analysis technologies by establishing leading-edge facilities, including one of Japan's highest-performance cluster computers. As such, Canon has succeeded in further reducing the need for prototypes, dramatically lowering costs and shortening product development lead times.

Canon's consolidated R&D expenses were ¥296,464 million (U.S.$3,408 million) in fiscal 2012, ¥307,800 million in fiscal 2011 and ¥315,817 million in fiscal 2010. The ratios of R&D expenses to the consolidated total net sales for fiscal 2012, 2011 and 2010 were 8.5%, 8.7% and 8.5%, respectively.

Canon believes that new products protected by patents will not easily allow competitors to compete with them, and will give them an advantage in establishing standards in the market and industry. According to the United States patent annual list, released by IFI CLAIMS® Patent Services, Canon obtained the third greatest number of private sector patents in fiscal 2012.

R&D Expenses

(Millions of yen)



MARKET RISK EXPOSURES

Canon is exposed to market risks, including changes in foreign currency exchange rates, interest rates and prices of marketable securities and investments. In order to hedge the risks of changes in foreign currency exchange rates, Canon uses derivative financial instruments.

Equity price risk

Canon holds marketable securities included in current assets, which consist generally of highly-liquid and low-risk instruments. Investments included in noncurrent assets are held as long-term investments. Canon does not hold marketable securities and investments for trading purposes.

Maturities and fair values of such marketable securities and investments with original maturities of more than three months, all of which were classified as available-for-sale securities, were as follows at December 31, 2012.

	Millions of yen		*Thousands of U.S. dollars*	
Available-for-sale securities	*Cost*	*Fair value*	*Cost*	*Fair value*
Due within one year	¥ 30	¥ 30	$ 345	$ 345
Due after one year through five years	953	990	10,954	11,379
Due after five years through ten years	1,010	985	11,609	11,322
Equity securities	14,866	21,335	170,874	245,230
	¥16,859	¥23,340	$193,782	$268,276

Foreign currency exchange rate and interest rate risk

Canon operates internationally, exposing it to the risk of changes in foreign currency exchange rates. Derivative financial instruments are comprised principally of foreign currency exchange contracts utilized by the Company and certain of its subsidiaries to reduce the risk. Canon assesses foreign currency exchange rate risk by continually monitoring changes in the exposures and by evaluating hedging opportunities. Canon does not hold or issue derivative financial instruments for trading purposes. Canon is also exposed to credit-related losses in the event of non-performance by counterparties to derivative financial instruments, but it is not expected that any counterparties will fail to meet their obligations. Most of the counterparties are internationally recognized financial institutions and selected by Canon taking into account their financial condition, and contracts are diversified across a number of major financial institutions.

Canon's international operations expose Canon to the risk of changes in foreign currency exchange rates. Canon uses foreign exchange contracts to manage certain foreign currency exchange exposures principally from the exchange of U.S. dollars and euros into Japanese yen. These contracts are primarily used to hedge the foreign currency exposure of forecasted intercompany sales and intercompany trade receivables which are denominated in foreign currencies. In accordance with Canon's policy, a specific portion of foreign currency exposure resulting from forecasted intercompany sales are hedged using foreign exchange contracts which principally mature within three months.

The following table provides information about Canon's major derivative financial instruments related to foreign currency exchange transactions existing at December 31, 2012. All of the foreign exchange contracts described in the following table have a contractual maturity date in 2013.

Millions of yen	*U.S.$*	*Euro*	*Others*	*Total*
Forwards to sell foreign currencies:				
Contract amounts	¥220,742	¥172,641	¥26,889	¥420,272
Estimated fair value	(12,365)	(11,444)	(1,600)	(25,409)
Forwards to buy foreign currencies:				
Contract amounts	¥ 38,826	¥ 27,737	¥ —	¥ 66,563
Estimated fair value	136	611	—	747

Thousands of U.S. dollars	*U.S.$*	*Euro*	*Others*	*Total*
Forwards to sell foreign currencies:				
Contract amounts	$2,537,264	$1,984,379	$309,070	$4,830,713
Estimated fair value	(142,126)	(131,540)	(18,391)	(292,057)
Forwards to buy foreign currencies:				
Contract amounts	$ 446,276	$ 318,816	$ —	$ 765,092
Estimated fair value	1,563	7,023	—	8,586

All of Canon's long-term debt is fixed rate debt. Canon expects that fair value changes and cash flows resulting from reasonable near-term changes in interest rates will be immaterial. Accordingly, Canon believes interest rate risk is insignificant. See also Note 10 of the Notes to Consolidated Financial Statements.

Changes in the fair value of derivative financial instruments designated as cash flow hedges, including foreign exchange contracts associated with forecasted intercompany sales, are reported in accumulated other comprehensive income (loss). These amounts are subsequently reclassified into earnings through other income (deductions) in the same period as the hedged items affect earnings. Substantially all such amounts recorded in accumulated other comprehensive income (loss) at year-end are expected to be recognized in earnings over the next twelve months. Canon excludes the time value component from the assessment of hedge effectiveness. Changes in the fair value of a foreign exchange contract for the period between the date that the forecasted intercompany sales occur and its maturity date are recognized in earnings and not considered hedge ineffectiveness.

The amount of the hedging ineffectiveness was not material for the years ended December 31, 2012, 2011 and 2010. The amounts of net losses excluded from the assessment of hedge effectiveness (time value component) which was recorded in other income (deductions) was ¥221 million (U.S.$3 million), ¥457 million and ¥302 million for the years ended December 31, 2012, 2011 and 2010, respectively.

Canon has entered into certain foreign currency exchange contracts to manage its foreign currency exposures. These foreign currency exchange contracts have not been designated as hedges. Accordingly, the changes in fair values of these contracts are recorded in earnings immediately.

LOOKING FORWARD

Looking at prospects for the global economy, Canon expects the U.S. economy to realize an accelerated recovery and emerging economies such as China to maintain solid growth. Canon believes, however, that European economies are likely to remain sluggish due to the debt crisis. The global economy as a whole is likely, Canon thinks, to show moderate growth, while the Japanese economy will likely head into solid recovery driven by the economic reconstruction policy and weakening of the yen against other currencies.

Fiscal 2013 represents the third year of Phase IV (2011–2015) of the Excellent Global Corporation Plan, a year in which Canon will implement various measures and in line with a basic policy Canon has established to implement sharp reforms and achieve sound business growth in the face of the current turbulent business environment.

In order to achieve its targets, Canon has set and will actively pursue the following five priority goals.

- ***Reinforcing Business by Creating Outstanding Hit Products***
  Canon aims to develop next-generation products and create business models that take into account the dramatic changes taking place in the market such as the popularization of smartphones and cloud computing. Canon will further reinforce business profitability, realizing timely launches of new products that are of sound development quality leveraging the technology of prototype-less development, and filtering down the selection of products through a process of selection and concentration.
- ***Securely Launching New Businesses and Achieving Sound Expansion***
  Canon plans to work to fundamentally strengthen its business, targeting the rapidly growing market for network camera systems. Canon plans to also work to further strengthen its "CINEMA EOS SYSTEM" and boost the profitability of its MR System "MREAL." Additionally, Canon will take full advantage of M&A opportunities to further broaden the range of its business.
- ***Thoroughly Strengthening Sales in Accordance with Respective Market Characteristics***
  In the office products domain, Canon plans to leverage its integration with sales subsidiaries of Océ N.V. to thoroughly strengthen direct sales and the solution and service business, while in the consumer products domain, Canon plans to strengthen sales in emerging markets and launch products suited to the country's or region's market characteristics in order to achieve sales expansion that is higher than economic growth.
- ***Relentlessly Pursuing Cost Reductions and Accelerating Optimization of Global Production***
  Canon plans to accelerate the application of automated and robot-based production. Canon plans to also expand its application of in-house production, which has focused

mainly on key components, to include general parts and molds, and production equipment. Additionally, Canon plans to promote a globally optimized production structure through agile production strategies always suited to the characteristics of each global base.

- ***Concentrating on Cultivation of Technological Themes that Lead the Way to the Future***
  Canon plans to accelerate innovation by further filtering down key themes and concentrating resources to obtain a steady stream of basic patents.

Office Business Unit

In 2012, Canon was able to maintain its revenue from sales of MFDs, services and solutions despite a strong yen and the deceleration of the global economy. The consolidation of Océ N.V. has brought many strategic assets to Canon, including expertise, resources and innovation.

The importance of connectivity, systems integration, business-workflow and web services continues to grow in the office imaging space and such added value is increasingly offered together with MFDs, printers and other hardware products as customer solutions. Canon seeks to maintain its leading position in these core markets.

In 2012, Canon expanded its offering with the launch of the imageRUNNER ADVANCE 4000, 6200, 8200 and imageRUNNER ADVANCE C5200 series and Océ VarioPrint 110/120/135, which are monochrome digital presses jointly developed with Océ N.V.

As for Production Printing Product (PPP), Canon strengthened its innovation capabilities in business services to accelerate the development of higher added value services as well as continued to invest in new products in order to expand its business in existing and new markets. To enter the Poster print market, Canon launched a new wide format printer, the ColorWave 650. Canon also introduced InfiniStream, which enables the vision of high-volume just-in-time production of customized folding cartons, with the industry's fastest liquid toner technology. As for solutions Canon introduced imageWARE Desktop Version 3, a software program that enhances the imageRUNNER ADVANCE ecosystem by enabling seamless document management. Canon also launched new service offerings for the Canon Business Imaging Online, Canon's unique cloud-based platform, while joining forces with major players in the technology industry. To maintain and enhance its competitive edge and to meet increasingly sophisticated customer demands, Canon plans to continue reinforcing its hardware and software product line-ups and solutions capability.

Although there is heightened uncertainty about the future of the laser printer market with the ongoing economic downturn in Europe and the deceleration of growth in emerging markets, Canon's laser printer business continues to occupy a large share and strong position in the market. In the monochrome laser printer market, the transition to a low price segment is expected to expand sales in the micro office/home office market and in emerging markets. Canon expects an expansion in the color laser printer market to be driven by increasing demand for color printing. Moreover, Canon plans to aggressively launch new products in the MFDs market and to drive Canon's business growth.

However, Canon is experiencing fierce competition with competitors focused on the laser printer market and an eventual decline in sales prices is becoming a major threat. Growth of the tablet PC and smartphone market, which affects users' printing behavior and may also lead to a decrease in demand for printing, is becoming a new threat.

In response, Canon aims to promote technological developments in order to introduce in a timely manner competitive products across the office business unit, and to pursue business efficiency through continuous cost reduction and optimization of its supply chain.

Imaging System Business unit

The demand for high-resolution digital photos remained high, and as a result the interchangeable lens digital camera market continued to show robust growth in 2012. By market category, growth remained strong in developed countries, and was particularly robust in Asia outside Japan and other emerging markets, which contributed to overall global growth in the imaging system business unit. By product category, the digital single-lens-reflex ("SLR") camera market showed steady growth, while mirrorless cameras represented a new category stimulating consumer demand.

In terms of interchangeable lens digital cameras, on top of the need for higher resolution and more compact and lightweight sizes, there is also consumer demand for video recording functions which manufacturers are meeting with a full high definition (HD) format, which is becoming a standard feature. Canon believes there remains considerable room for future growth in this category through development of new products based on state-of-the-art technology. In emerging markets, sales volumes of interchangeable lens digital cameras are still increasing rapidly.

As for the interchangeable lens market, interchangeable lens digital cameras have made dramatic advances in popularity, and further growth is expected in the future. Canon will continue to endeavor to market products that meet customer needs, such as lenses equipped with an image stabilization function, so as to expand sales and market share.

Overall, the compact digital camera market shrank year-on-year due to ongoing economic stagnation and the rapid growth of tablet PCs and smartphones. However, Canon's position in the compact market improved such that Canon now maintains a higher market share compared to the previous fiscal year.

In the digital camera market, Canon faced intense price competition. This combined with the value of the yen remaining at historical highs throughout most of 2012, placed serious constraints on Canon's profit margins. Throughout the industry, there has been a strong tendency toward reliance on EMS (electronic manufacturing services), and intense price competition is expected to continue for the foreseeable future. Canon's strategies to address these challenges include boosting the added value of products, pressing forward with 100% internal production leveraging the economies of scale that come with being the industry leader, and building an optimum cost structure to combat the pressures that might return should the yen strengthen again.

The main recording media for digital camcorders has become flash memory and the shift from SD to HD is ongoing. The market for conventional camcorders has been shrinking primarily because many popular devices include a movie function. On the other hand, new categories like web cameras and action cameras are emerging and expanding. Canon aims to expand sales in this market with a robust product lineup including higher added value based around Canon's distinctive high-definition, high-resolution technologies also found in Canon's professional line. Canon plans to expand lineup of "CINEMA EOS SYSTEM" in the business-use digital video camcorder field. CINEMA EOS SYSTEM consists of new interchangeable lens digital cinema camcorders, EF Lenses and new EF Cinema Lenses. Canon is widely aiming to solidify its top position in the motion picture production market by introducing a new series of interchangeable lens cinema camcorders and cinema lenses to the market not only cinema but also broadcast, sports, documentary, etc. as the CINEMA EOS SYSTEM.

In 2012, Canon experienced robust growth in the field of projectors for business applications, and in particular brighter, installation type projectors. In this installation market, Canon launched the new install-type WUX5000, WX6000 and SX6000 with great success in 2012. Moving forward, Canon expects to extend its competitive product lineup based around the optical technology on which the company prides itself, and push for expanded sales.

In the field of network cameras for industrial surveillance and management applications, the fiscal year 2012 achieved double-digit growth. The four HD-compatible products Canon launched in the second half of 2011 have increased the importance of mega-pixels and image analysis and also achieved significant growth in terms of both units sold and monetary amount.

In the broadcast TV lens market, gradual market expansion has continued due to market growth in emerging economies although demand arising from the switchover to high-definition broadcast formats in developed countries dropped off. Despite the economic slump in Europe, the slowdown of exports to China and the progressive lowering of equipment prices, Canon still has a large share of the TV lens market with high value-added products. Canon's successful introduction in 2012 of a new field lens for international level sporting events contributed to increased revenue.

In 2012, the consumer inkjet printer market declined compared to 2011, due to a worldwide economic downturn and competitor's withdrawal from the business. Vendors introduced new product functions which make it easy to print from smartphone, tablet PC and the cloud computing environment, as well as functions which improve operability for users.

Such vendors also expanded their lineup of products from conventional home use to emerging market and business area use.

The large-format inkjet printer market decreased slightly in 2012 from the previous year, amid the situation of dropping in capital spending caused by the downturn in the European economy and the slowdown of the growth rate in the Asian economy. In this environment, Canon was able to increase sales of large-format inkjet printer units in 2012 compared to 2011. In the first quarter of 2012, Canon was unable to supply enough units to the market primarily as a result of supply delays caused by the floods in Thailand. However, owing to a keen focus on recovering production quickly, Canon has been able to exceed unit sales levels for each quarter from the second quarter of 2012 compared to the same quarter in the prior year. Because the overall market declined in 2012, Canon was accordingly able to increase its share of the market. Canon increased the unit sales of large-format inkjet printers in part by launching new products for the graphic art market and expanding sales channels.

Industry and Others Business Unit

In fiscal 2012, the market for semiconductor lithography equipment decreased approximately 30% from the previous year. In the memory segment, equipment investment by chip makers remained low primarily because supply continued to outweigh demand. However, image sensor, logic device and automotive device makers steadily increased their equipment investments, drawn by the growing market for smartphones, tablet PCs and hybrid cars. At the same time, some manufacturers started to invest in i-line steppers for small diameter wafers used in power devices and LEDs, as well as for new markets such as 3D mountings for silicon Via (TSV).

As a result, Canon's shipments of semiconductor lithography equipment in 2012 slightly decreased from the previous year. Shipments for memory makers remained low while i-line steppers for image sensor production enjoyed brisk sales. In addition, Canon released new i-line stepper FPA-3030i5+ suitable for the production of the green devices such as LEDs and power devices, which currently occupies a high share of automotive device and LEDs markets. Canon also released new KrF stepper FPA-6300ES6a with greatly improved productivity compared to conventional equipment.

In 2012, the market for FPD lithography equipment generally slowed because of a deterioration of panel makers' earnings. Overall the market for 8th generation large-sized panel production declined 60% from the previous year while the market for 5.5-6th generation small-to-mid-sized panel production maintained high growth due to the brisk market of smartphones and tablet PCs.

As a result, Canon's shipments of FPD lithography equipment decreased from the previous year primarily due to decline in the market for large-sized panels, where Canon is particularly competitive, and the delay in the development of new products for small-to-mid-sized panels, for which the market has maintained a healthy growth.

Canon expects FPD lithography equipment investments by panel makers to recover in 2013 mainly led by Chinese makers. Canon aims to turn around the market share by revamping its product lineup including products for small-to-mid-sized panels.

In the medical equipment business, the digital radiography (DR) market continued to expand in 2012, mainly in the emerging markets such as Asia. Moreover, the digital systems market of developed countries continued to experience a rapid transition from the digitalization format of computed radiography (CR) to the newest DR format. While competition increased with a growing number of new players, the target market of Canon DR products showed steady growth.

As a result, Canon accelerated sales of Canon's static DR products; CXDI-401C/G, CXDI-401C/G COMPACT, CXDI-501C/G, and CXDI-80C Wireless, all launched in fiscal year 2011, led the revenue increase for fiscal year 2012. Canon's dynamic DR product, CXDI-50RF, also recorded consistent sales growth, contributing to the overall sales expansion in DR business.

Regarding the ophthalmic products, the optical coherence tomography ("OCT") market continued to expand in 2012, and Canon expects a further increase in both volume and competition in the market. In the OCT market, Canon launched the first Canon-brand OCT, OCT HS-100, in September 2012. This product was the result of collaboration with Optopol Technology, S.A. (Poland), a Canon Group consolidated subsidiary since 2010.

Canon's fiscal year 2012 ophthalmic product sales were supported by increased sales of TX-20/TX-20P a full auto tonometer and CR-2 Plus high-end non-mydriatic retinal camera, both released in 2011, and RK-F2, a full auto refkeratometer released in 2012.

With the addition of OCT to Canon's product portfolio, Canon strives to further increase sales in the ophthalmic equipment market.

Sales of document scanners manufactured by Canon Electronics Inc. recovered in North America in addition to brisk sales in China, India and other Asian countries. As a result, overall unit sales increased.

Sales of organic LED panel manufacturing equipment made by Canon Tokki Corporation recorded steady sales from aggressive capital investment by organic LED panel manufacturers on the back of increasing demand for smartphones and tablet PCs.

Sales of film deposition equipment, made by Canon ANELVA Corporation, for magnetic heads and hard discs fell due to the weak PC market, while sales of semiconductor film deposition equipment significantly increased as demand for semiconductor devices used in smartphones was robust.

Although sales of die bonders manufactured by Canon Machinery Inc. decreased due to slow capital investment by semiconductor manufacturers, sales of equipment related to secondary batteries used in automobiles and smartphones increased.

Forward looking statements

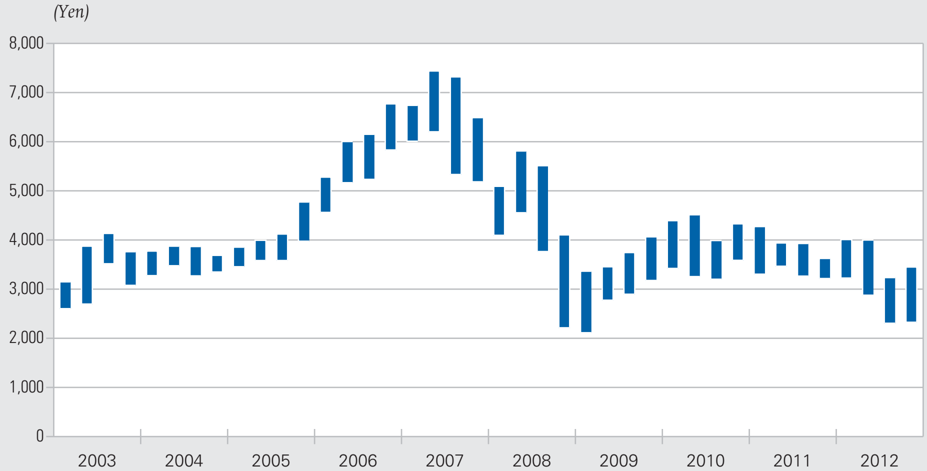
The foregoing discussion and other disclosure in this report contains forward-looking statements that reflect management's current views with respect to certain future events and financial performance. Actual results may differ materially from those projected or implied in the forward-looking statements. Further, certain forward-looking statements are based upon assumptions of future events that may not prove to be accurate. The following important factors could cause actual results to differ materially from those projected or implied in any forward-looking statements: foreign currency exchange rate fluctuations; the uncertainty of Canon's ability to implement its plans to localize production and other measures to reduce the impact of foreign currency exchange rate fluctuations; uncertainty as to economic conditions in Canon's major markets; uncertainty of continued demand for Canon's high-value-added products; Canon's ability to continue to develop products and to market products that incorporate new technology on a timely basis, are competitively priced, and achieve market acceptance; the possibility of losses resulting from foreign currency transactions designed to reduce financial risks from changes in foreign currency exchange rates; and inventory risk due to shifts in market demand.

TEN-YEAR FINANCIAL SUMMARY

	Millions of yen (except per share amounts)			
	2012	2011	2010	2009
Net sales:				
Domestic	**¥ 720,286**	¥ 694,450	¥ 695,749	¥ 702,344
Overseas	**2,759,502**	2,862,983	3,011,152	2,506,857
Total	**3,479,788**	3,557,433	3,706,901	3,209,201
Percentage of previous year	**97.8%**	96.0%	115.5%	78.4%
Net income attributable to Canon Inc.	**224,564**	248,630	246,603	131,647
Percentage of sales	**6.5%**	7.0%	6.7%	4.1%
Advertising	**83,134**	81,232	94,794	78,009
Research and development expenses	**296,464**	307,800	315,817	304,600
Depreciation of property, plant and equipment	**211,973**	210,179	232,327	277,399
Increase in property, plant and equipment	**270,457**	226,869	158,976	216,128
Long-term debt, excluding current installments	**¥ 2,117**	¥ 3,368	¥ 4,131	¥ 4,912
Canon Inc. stockholders' equity	**2,598,026**	2,551,132	2,645,782	2,688,109
Total assets	**3,955,503**	3,930,727	3,983,820	3,847,557
Per share data:				
Net income attributable to Canon Inc. stockholders per share:				
Basic	**¥ 191.34**	¥ 204.49	¥ 199.71	¥ 106.64
Diluted	**191.34**	204.48	199.70	106.64
Dividend per share	**130.00**	120.00	120.00	110.00
Stock price:				
High	**4,015**	4,280	4,520	4,070
Low	**2,308**	3,220	3,205	2,115
Average number of common shares in thousands	**1,173,648**	1,215,832	1,234,817	1,234,482
Number of employees	**196,968**	198,307	197,386	168,879

Common Stock Price Range (Tokyo Stock Exchange)

(Yen)



							Thousands of U.S. dollars (except per share amounts)
	2008	2007	2006	2005	2004	2003	**2012**
	¥ 868,280	¥ 947,587	¥ 932,290	¥ 856,205	¥ 849,734	¥ 801,400	**$ 8,279,149**
	3,225,881	3,533,759	3,224,469	2,897,986	2,618,119	2,396,672	**31,718,414**
	4,094,161	4,481,346	4,156,759	3,754,191	3,467,853	3,198,072	**39,997,563**
	91.4%	107.8%	110.7%	108.3%	108.4%	108.8%	**97.8%**
	309,148	488,332	455,325	384,096	343,344	275,730	**2,581,195**
	7.6%	10.9%	11.0%	10.2%	9.9%	8.6%	**6.5%**
	112,810	132,429	116,809	106,250	111,770	100,278	**955,563**
	374,025	368,261	308,307	286,476	275,300	259,140	**3,407,632**
	304,622	309,815	235,804	205,727	174,397	168,636	**2,436,471**
	361,988	428,549	379,657	383,784	318,730	210,038	**3,108,701**
	¥ 8,423	¥ 8,680	¥ 15,789	¥ 27,082	¥ 28,651	¥ 59,260	**$ 24,333**
	2,659,792	2,922,336	2,986,606	2,604,682	2,209,896	1,865,545	**29,862,368**
	3,969,934	4,512,625	4,521,915	4,043,553	3,587,021	3,182,148	**45,465,552**
	¥ 246.21	¥ 377.59	¥ 341.95	¥ 288.63	¥ 258.53	¥ 209.21	**$ 2.20**
	246.20	377.53	341.84	288.36	257.85	207.17	**2.20**
	110.00	110.00	83.33	66.67	43.33	33.33	**1.49**
	5,820	7,450	6,780	4,780	3,880	4,140	**46.15**
	2,215	5,190	4,567	3,460	3,273	2,607	**26.53**
	1,255,626	1,293,296	1,331,542	1,330,761	1,328,048	1,317,974	
	166,980	131,352	118,499	115,583	108,257	102,567	

Notes:
1. U.S. dollar amounts are translated from yen at the rate of U.S.$1 = JPY87, the approximate exchange rate on the Tokyo Foreign Exchange Market as of December 28, 2012.
2. The Company made a three-for-two stock split on July 1, 2006. The average number of common shares and the per share data for the periods prior to the stock split have been adjusted to reflect the stock split.

CONSOLIDATED BALANCE SHEETS

Canon Inc. and Subsidiaries
December 31, 2012 and 2011

	Millions of yen		Thousands of U.S. dollars (Note 2)
ASSETS	**2012**	2011	**2012**
Current assets:			
Cash and cash equivalents (Note 1)	¥ 666,678	¥ 773,227	$ 7,662,966
Short-term investments (Note 3)	28,322	125,517	325,540
Trade receivables, net (Note 4)	573,375	533,208	6,590,517
Inventories (Note 5)	551,623	476,704	6,340,494
Prepaid expenses and other current assets (Notes 7, 13 and 18)	262,258	244,649	3,014,460
Total current assets	2,082,256	2,153,305	23,933,977
Noncurrent receivables (Note 19)	19,702	16,772	226,460
Investments (Note 3)	56,617	51,790	650,770
Property, plant and equipment, net (Notes 6 and 7)	1,260,364	1,190,836	14,486,943
Intangible assets, net (Note 9)	135,736	138,030	1,560,184
Other assets (Notes 7, 9, 12 and 13)	400,828	379,994	4,607,218
Total assets	¥3,955,503	¥3,930,727	$45,465,552

LIABILITIES AND EQUITY			
Current liabilities:			
Short-term loans and current portion of long-term debt (Note 10)	¥ 1,866	¥ 8,343	$ 21,448
Trade payables (Note 11)	325,235	380,532	3,738,333
Accrued income taxes (Note 13)	60,057	45,900	690,310
Accrued expenses (Notes 12 and 19)	291,348	299,422	3,348,828
Other current liabilities (Notes 6, 13 and 18)	165,929	159,651	1,907,230
Total current liabilities	844,435	893,848	9,706,149
Long-term debt, excluding current installments (Note 10)	2,117	3,368	24,333
Accrued pension and severance cost (Note 12)	272,131	249,604	3,127,943
Other noncurrent liabilities (Note 13)	82,518	70,240	948,483
Total liabilities	1,201,201	1,217,060	13,806,908
Commitments and contingent liabilities (Note 19)			
Equity:			
Canon Inc. stockholders' equity:			
Common stock			
Authorized 3,000,000,000 shares; issued 1,333,763,464 shares in 2012 and 2011	174,762	174,762	2,008,759
Additional paid-in capital	401,547	401,572	4,615,483
Legal reserve (Note 14)	61,663	59,004	708,770
Retained earnings (Note 14)	3,138,976	3,059,298	36,080,184
Accumulated other comprehensive income (loss) (Note 15)	(367,249)	(481,773)	(4,221,253)
Treasury stock, at cost; 180,972,173 shares in 2012 and 132,231,296 shares in 2011	(811,673)	(661,731)	(9,329,575)
Total Canon Inc. stockholders' equity	2,598,026	2,551,132	29,862,368
Noncontrolling interests	156,276	162,535	1,796,276
Total equity	2,754,302	2,713,667	31,658,644
Total liabilities and equity	¥3,955,503	¥3,930,727	$45,465,552

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME

Canon Inc. and Subsidiaries
Years ended December 31, 2012, 2011 and 2010

	Millions of yen			*Thousands of U.S. dollars (Note 2)*
	2012	2011	2010	**2012**
Net sales	**¥3,479,788**	¥3,557,433	¥3,706,901	**$39,997,563**
Cost of sales (Notes 6, 9, 12 and 19)	**1,829,822**	1,820,670	1,923,813	**21,032,437**
Gross profit	**1,649,966**	1,736,763	1,783,088	**18,965,126**
Operating expenses (Notes 1, 6, 9, 12, 16 and 19):				
Selling, general and administrative expenses	**1,029,646**	1,050,892	1,079,719	**11,835,011**
Research and development expenses	**296,464**	307,800	315,817	**3,407,632**
	1,326,110	1,358,692	1,395,536	**15,242,643**
Operating profit	**323,856**	378,071	387,552	**3,722,483**
Other income (deductions):				
Interest and dividend income	**6,792**	8,432	6,022	**78,069**
Interest expense	**(1,022)**	(988)	(1,931)	**(11,747)**
Other, net (Notes 1, 3, 18 and 21)	**12,931**	(10,991)	1,220	**148,632**
	18,701	(3,547)	5,311	**214,954**
Income before income taxes	**342,557**	374,524	392,863	**3,937,437**
Income taxes (Note 13)	**110,112**	120,415	140,160	**1,265,655**
Consolidated net income	**232,445**	254,109	252,703	**2,671,782**
Less: Net income attributable to noncontrolling interests	**7,881**	5,479	6,100	**90,587**
Net income attributable to Canon Inc.	**¥ 224,564**	¥ 248,630	¥ 246,603	**$ 2,581,195**

	Yen			*U.S. dollars (Note 2)*
Net income attributable to Canon Inc. stockholders per share (Note 17):				
Basic	**¥ 191.34**	¥ 204.49	¥ 199.71	**$ 2.20**
Diluted	**191.34**	204.48	199.70	**2.20**
Cash dividends per share	**130.00**	120.00	120.00	**1.49**

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Canon Inc. and Subsidiaries
Years ended December 31, 2012, 2011 and 2010

	Millions of yen			*Thousands of U.S. dollars (Note 2)*
	2012	2011	2010	**2012**
Consolidated net income	**¥232,445**	¥254,109	¥252,703	**$2,671,782**
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	**133,735**	(54,086)	(126,918)	**1,537,184**
Net unrealized gains and losses on securities	**3,265**	(2,116)	(146)	**37,529**
Net gains and losses on derivative instruments	**(4,880)**	(449)	767	**(56,092)**
Pension liability adjustments	**(12,787)**	(38,377)	(9,327)	**(146,978)**
	119,333	(95,028)	(135,624)	**1,371,643**
Comprehensive income (Note 15)	**351,778**	159,081	117,079	**4,043,425**
Less: Comprehensive income (loss) attributable to noncontrolling interests	**10,824**	1,765	(563)	**124,414**
Comprehensive income attributable to Canon Inc.	**¥340,954**	¥157,316	¥117,642	**$3,919,011**

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF EQUITY

Canon Inc. and Subsidiaries

	Millions of yen								
	Common stock	*Additional paid-in capital*	*Legal reserve*	*Retained earnings*	*Accumulated other comprehensive income (loss)*	*Treasury stock*	Total Canon Inc. stockholders' equity	*Noncontrolling interests*	*Total equity*
Balance at December 31, 2009	¥174,762	¥404,293	¥54,687	¥2,871,437	¥(260,818)	¥(556,252)	¥2,688,109	¥191,291	¥2,879,400
Acquisition of subsidiaries								19,168	19,168
Equity transactions with noncontrolling interests and other		(3,787)		(13,453)	(680)	55,250	37,330	(43,214)	(5,884)
Dividends paid to Canon Inc. stockholders				(136,103)			(136,103)		(136,103)
Dividends paid to noncontrolling interests								(2,827)	(2,827)
Transfer to legal reserve			3,243	(3,243)			—		—
Comprehensive income (loss):									
Net income				246,603			246,603	6,100	252,703
Other comprehensive income (loss), net of tax (Note 15):									
Foreign currency translation adjustments					(122,667)		(122,667)	(4,251)	(126,918)
Net unrealized gains and losses on securities					(222)		(222)	76	(146)
Net gains and losses on derivative instruments					833		833	(66)	767
Pension liability adjustments					(6,905)		(6,905)	(2,422)	(9,327)
Total comprehensive income (loss)							117,642	(563)	117,079
Repurchase of treasury stock, net		(81)		(4)		(61,111)	(61,196)		(61,196)
Balance at December 31, 2010	174,762	400,425	57,930	2,965,237	(390,459)	(562,113)	2,645,782	163,855	2,809,637
Equity transactions with noncontrolling interests and other		1,193		(609)			584	(247)	337
Dividends paid to Canon Inc. stockholders				(152,784)			(152,784)		(152,784)
Dividends paid to noncontrolling interests								(2,838)	(2,838)
Transfer to legal reserve			1,074	(1,074)			—		—
Comprehensive income :									
Net income				248,630			248,630	5,479	254,109
Other comprehensive income (loss), net of tax (Note 15):									
Foreign currency translation adjustments					(53,251)		(53,251)	(835)	(54,086)
Net unrealized gains and losses on securities					(2,017)		(2,017)	(99)	(2,116)
Net gains and losses on derivative instruments					(462)		(462)	13	(449)
Pension liability adjustments					(35,584)		(35,584)	(2,793)	(38,377)
Total comprehensive income							157,316	1,765	159,081
Repurchase of treasury stock, net		(46)		(102)		(99,618)	(99,766)		(99,766)
Balance at December 31, 2011	¥174,762	¥401,572	¥59,004	¥3,059,298	¥(481,773)	¥(661,731)	¥2,551,132	¥162,535	¥2,713,667
Equity transactions with noncontrolling interests and other		**(16)**		**152**	**(1,866)**		**(1,730)**	**(13,591)**	**(15,321)**
Dividends paid to Canon Inc. stockholders				**(142,362)**			**(142,362)**		**(142,362)**
Dividends paid to noncontrolling interests								**(3,492)**	**(3,492)**
Transfer to legal reserve			**2,659**	**(2,659)**			**—**		**—**
Comprehensive income:									
Net income				**224,564**			**224,564**	**7,881**	**232,445**
Other comprehensive income (loss), net of tax (Note 15):									
Foreign currency translation adjustments					**132,704**		**132,704**	**1,031**	**133,735**
Net unrealized gains and losses on securities					**3,148**		**3,148**	**117**	**3,265**
Net gains and losses on derivative instruments					**(4,882)**		**(4,882)**	**2**	**(4,880)**
Pension liability adjustments					**(14,580)**		**(14,580)**	**1,793**	**(12,787)**
Total comprehensive income							**340,954**	**10,824**	**351,778**
Repurchase of treasury stock, net		**(9)**		**(17)**		**(149,942)**	**(149,968)**		**(149,968)**
Balance at December 31, 2012	**¥174,762**	**¥401,547**	**¥61,663**	**¥3,138,976**	**¥(367,249)**	**¥(811,673)**	**¥2,598,026**	**¥156,276**	**¥2,754,302**

	Thousands of U.S. dollars (Note 2)								
	Common stock	*Additional paid-in capital*	*Legal reserve*	*Retained earnings*	*Accumulated other comprehensive income (loss)*	*Treasury stock*	Total Canon Inc. stockholders' equity	*Noncontrolling interests*	*Total equity*
Balance at December 31, 2011	$2,008,759	$4,615,770	$678,207	$35,164,345	$(5,537,621)	$ (7,606,104)	$29,323,356	$1,868,219	$31,191,575
Equity transactions with noncontrolling interests and other		(184)		1,748	(21,448)		(19,884)	(156,219)	(176,103)
Dividends paid to Canon Inc. stockholders				(1,636,345)			(1,636,345)		(1,636,345)
Dividends paid to noncontrolling interests								(40,138)	(40,138)
Transfer to legal reserve			30,563	(30,563)			—		—
Comprehensive income:									
Net income				2,581,195			2,581,195	90,587	2,671,782
Other comprehensive income (loss), net of tax (Note 15):									
Foreign currency translation adjustments					1,525,333		1,525,333	11,851	1,537,184
Net unrealized gains and losses on securities					36,184		36,184	1,345	37,529
Net gains and losses on derivative instruments					(56,115)		(56,115)	23	(56,092)
Pension liability adjustments					(167,586)		(167,586)	20,608	(146,978)
Total comprehensive income							3,919,011	124,414	4,043,425
Repurchase of treasury stock, net		(103)		(196)		(1,723,471)	(1,723,770)		(1,723,770)
Balance at December 31, 2012	$2,008,759	$4,615,483	$708,770	$36,080,184	$(4,221,253)	$(9,329,575)	$29,862,368	$1,796,276	$31,658,644

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Canon Inc. and Subsidiaries
Years ended December 31, 2012, 2011 and 2010

	Millions of yen			*Thousands of U.S. dollars (Note 2)*
	2012	2011	2010	**2012**
Cash flows from operating activities:				
Consolidated net income	**¥232,445**	¥254,109	¥252,703	**$ 2,671,782**
Adjustments to reconcile consolidated net income to net cash provided by operating activities:				
Depreciation and amortization	**258,133**	261,343	276,193	**2,967,046**
Loss on disposal of fixed assets	**11,242**	8,937	21,120	**129,218**
Impairment loss of fixed assets	**7**	598	1,288	**80**
Impairment loss of investments	**1,527**	8,130	23,330	**17,552**
Equity in (earnings) losses of affiliated companies	**(610)**	7,368	(10,471)	**(7,011)**
Deferred income taxes	**7,487**	29,129	29,381	**86,057**
(Increase) decrease in trade receivables	**5,030**	9,991	(6,671)	**57,816**
Increase in inventories	**(24,805)**	(109,983)	(17,532)	**(285,115)**
Increase (decrease) in trade payables	**(102,293)**	35,766	115,726	**(1,175,782)**
Increase (decrease) in accrued income taxes	**12,427**	(25,653)	25,228	**142,839**
Increase (decrease) in accrued expenses	**(30,089)**	8,938	77	**(345,851)**
Increase (decrease) in accrued (prepaid) pension and severance cost	**5,515**	(2,315)	4,147	**63,391**
Other, net	**8,061**	(16,796)	29,894	**92,656**
Net cash provided by operating activities	**384,077**	469,562	744,413	**4,414,678**
Cash flows from investing activities:				
Purchases of fixed assets (Note 6)	**(316,211)**	(238,129)	(199,152)	**(3,634,609)**
Proceeds from sale of fixed assets (Note 6)	**4,861**	3,273	3,303	**55,874**
Purchases of available-for-sale securities	**(417)**	(2,160)	(10,891)	**(4,793)**
Proceeds from sale and maturity of available-for-sale securities	**344**	1,934	3,910	**3,954**
(Increase) decrease in time deposits, net	**103,137**	(34,111)	(80,904)	**1,185,483**
Acquisitions of subsidiaries, net of cash acquired	**(704)**	29	(55,686)	**(8,092)**
Purchases of other investments	**(796)**	(373)	(1,955)	**(9,149)**
Other, net	**(2,954)**	12,994	(758)	**(33,955)**
Net cash used in investing activities	**(212,740)**	(256,543)	(342,133)	**(2,445,287)**
Cash flows from financing activities:				
Proceeds from issuance of long-term debt	**614**	725	5,902	**7,057**
Repayments of long-term debt	**(3,732)**	(4,670)	(5,739)	**(42,897)**
Increase (decrease) in short-term loans, net	**(5,055)**	2,466	(74,933)	**(58,103)**
Dividends paid	**(142,362)**	(152,784)	(136,103)	**(1,636,345)**
Repurchases of treasury stock, net	**(149,968)**	(99,766)	(61,196)	**(1,723,770)**
Other, net	**(19,236)**	(3,484)	(7,828)	**(221,103)**
Net cash used in financing activities	**(319,739)**	(257,513)	(279,897)	**(3,675,161)**
Effect of exchange rate changes on cash and cash equivalents	**41,853**	(22,858)	(76,838)	**481,069**
Net change in cash and cash equivalents	**(106,549)**	(67,352)	45,545	**(1,224,701)**
Cash and cash equivalents at beginning of year	**773,227**	840,579	795,034	**8,887,667**
Cash and cash equivalents at end of year	**¥666,678**	¥773,227	¥840,579	**$ 7,662,966**
Supplemental disclosure for cash flow information (Note 22):				
Cash paid during the year for:				
Interest	**¥ 1,084**	¥ 914	¥ 1,924	**$ 12,460**
Income taxes	**98,096**	120,696	80,212	**1,127,540**

See accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Canon Inc. and Subsidiaries

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

(a) Description of Business

Canon Inc. (the "Company") and subsidiaries (collectively "Canon") is one of the world's leading manufacturers in such fields as office products, imaging system products and industry and other products. Office products consist mainly of office multifunction devices ("MFDs"), office copying machines, laser printers and digital production printing systems. Imaging system products consist mainly of interchangeable-lens digital cameras, compact digital cameras, interchangeable lenses, digital camcorders, digital cinema cameras, inkjet printers, large-format inkjet printers, commercial photo printers, image scanners and broadcast equipment. Industry and other products consist mainly of semiconductor lithography equipment, flat-panel-display ("FPD") lithography equipment, digital radiography systems, vacuum thin-film deposition equipment and organic LED panel manufacturing equipment. Canon's consolidated net sales for the years ended December 31, 2012, 2011 and 2010 were distributed as follows: the Office Business Unit 50.5%, 53.9% and 53.6%, the Imaging System Business Unit 40.4%, 36.9% and 37.5%, the Industry and Others Business Unit 11.7%, 11.8% and 11.7%, and elimination between segments 2.6%, 2.6% and 2.8%, respectively. These percentages were computed by dividing segment net sales, including intersegment sales, by consolidated net sales, based on the segment operating results described in Note 23.

Sales are made principally under the Canon brand name, almost entirely through sales subsidiaries. These subsidiaries are responsible for marketing and distribution, and primarily sell to retail dealers in their geographic area. 79.3%, 80.5% and 81.2% of consolidated net sales for the years ended December 31, 2012, 2011 and 2010 were generated outside Japan, with 27.0%, 27.0% and 27.6% in the Americas, 29.1%, 31.3% and 31.6% in Europe, and 23.2%, 22.2% and 22.0% in Asia and Oceania, respectively.

Canon sells laser printers on an OEM basis to Hewlett-Packard Company; such sales constituted 17.0%, 19.3% and 20.1% of consolidated net sales for the years ended December 31, 2012, 2011 and 2010, respectively, and are included in the Office Business Unit.

Canon's manufacturing operations are conducted primarily at 28 plants in Japan and 17 overseas plants which are located in countries or regions such as the United States, Germany, France, the Netherlands, Taiwan, China, Malaysia, Thailand and Vietnam.

(b) Basis of Presentation

The Company and its domestic subsidiaries maintain their books of account in conformity with financial accounting standards of Japan. Foreign subsidiaries maintain their books of account in conformity with financial accounting standards of the countries of their domicile.

Certain adjustments and reclassifications have been incorporated in the accompanying consolidated financial statements to conform with U.S. generally accepted accounting principles ("GAAP"). These adjustments were not recorded in the statutory books of account.

(c) Principles of Consolidation

The consolidated financial statements include the accounts of the Company, its majority owned subsidiaries and those variable interest entities where the Company or its consolidated subsidiaries are the primary beneficiaries. All significant intercompany balances and transactions have been eliminated.

(d) Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Significant estimates and assumptions are reflected in valuation and disclosure of revenue recognition, allowance for doubtful receivables, valuation of inventories, impairment of long-lived assets, environmental liabilities, valuation of deferred tax assets, uncertain tax positions and employee retirement and severance benefit obligations. Actual results could differ materially from those estimates.

(e) Translation of Foreign Currencies

Assets and liabilities of the Company's subsidiaries located outside Japan with functional currencies other than Japanese yen are translated into Japanese yen at the rates of exchange in effect at the balance sheet date. Income and expense items are translated at the average exchange rates prevailing during the year. Gains and losses resulting from translation of financial statements are excluded from earnings and are reported in other comprehensive income (loss).

Gains and losses resulting from foreign currency transactions, including foreign exchange contracts, and translation of assets and liabilities denominated in foreign currencies are included in other income (deductions) in the consolidated statements of income. Foreign currency exchange gains and losses was a net gain of ¥9,130 million ($104,943 thousand) for the year ended December 31, 2012, a net loss of ¥3,287 million for the year ended December 31, 2011 and a net gain of ¥3,089 million for the year ended December 31, 2010, respectively.

(f) Cash Equivalents

All highly liquid investments acquired with original maturities of three months or less are considered to be cash equivalents. Certain debt securities with original maturities of less than three months, classified as available-for-sale securities of ¥141,729 million ($1,629,069 thousand) and ¥204,307 million at December 31, 2012 and 2011, respectively, are included in cash and cash equivalents in the consolidated balance sheets.

(g) Investments

Investments consist primarily of time deposits with original maturities of more than three months, debt and marketable equity securities, investments in affiliated companies and non-marketable equity securities. Canon reports investments with maturities of less than one year as short-term investments.

Canon classifies investments in debt and marketable equity securities as available-for-sale or held-to-maturity securities. Canon does not hold any trading securities, which are bought and held primarily for the purpose of sale in the near term.

Available-for-sale securities are recorded at fair value. Fair value is determined based on quoted market prices, projected discounted cash flows or other valuation techniques as appropriate. Unrealized holding gains and losses, net of the related tax effect, are reported as a separate component of other comprehensive income (loss) until realized. Held-to-maturity securities are recorded at amortized cost, adjusted for amortization of premiums and accretion of discounts.

Available-for-sale and held-to-maturity securities are regularly reviewed for other-than-temporary declines in the carrying amount based on criteria that include the length of time and the extent to which the market value has been less than cost, the financial condition and near-term prospects of the issuer and Canon's intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in market value. For debt securities for which the declines are deemed to be other-than-temporary and there is no intent to sell, impairments are separated into the amount related to credit loss, which is recognized in earnings, and the amount related to all other factors, which is recognized in other comprehensive income (loss). For debt securities for which the declines are deemed to be other-than-temporary and there is an intent to sell, impairments in their entirety are recognized in earnings. For equity securities for which the declines are deemed to be other-than-temporary, impairments in their entirety are recognized in earnings. Canon recognizes an impairment loss to the extent by which the cost basis of the investment exceeds the fair value of the investment.

Realized gains and losses are determined by the average cost method and reflected in earnings.

Investments in affiliated companies over which Canon has the ability to exercise significant influence, but does not hold a controlling financial interest, are accounted for by the equity method.

Non-marketable equity securities in companies over which Canon does not have the ability to exercise significant influence are stated at cost and reviewed periodically for impairment.

(h) Allowance for Doubtful Receivables

Allowance for doubtful trade and finance receivables is maintained for all customers based on a combination of factors, including aging analysis, macroeconomic conditions and historical experience. An additional reserve for individual accounts is recorded when Canon becomes aware of a customer's inability to meet its financial obligations, such as in the case of bankruptcy filings. If circumstances related to customers change, estimates of the recoverability of receivables would be further adjusted. When all collection options are exhausted including legal recourse, the accounts or portions thereof are deemed to be uncollectable and charged against the allowance.

(i) Inventories

Inventories are stated at the lower of cost or market value. Cost is determined by the average method for domestic inventories and principally by the first-in, first-out method for overseas inventories.

(j) Impairment of Long-Lived Assets

Long-lived assets, such as property, plant and equipment, and acquired intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of the asset and the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of the asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of by sale are reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

(k) Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is calculated principally by the declining-balance method, except for certain assets which are depreciated by the straight-line method over the estimated useful lives of the assets.

The depreciation period ranges from 3 years to 60 years for buildings and 1 year to 20 years for machinery and equipment.

Assets leased to others under operating leases are stated at cost and depreciated to the estimated residual value of the assets by the straight-line method over the lease term, generally from 2 years to 5 years.

(l) Goodwill and Other Intangible Assets

Goodwill and other intangible assets with indefinite useful lives are not amortized, but are instead tested for impairment annually in the fourth quarter of each year, or more frequently if indicators of potential impairment exist. Canon performs its impairment test of goodwill using the two-step approach at the reporting unit level, which is one level below the operating segment level. All goodwill is assigned to the reporting unit or units that benefit from the synergies arising from each business combination. If the carrying amount assigned to the reporting unit exceeds the fair value of the reporting unit, Canon performs the second step to measure an impairment charge in the amount by which the carrying amount of a reporting unit's goodwill exceeds its implied fair value. Intangible assets with finite useful lives consist primarily of software, license fees, patented technologies and customer relationships. Software and license fees are amortized using the straight-line method over the estimated useful lives, which range from 3 years to 5 years for software and 5 years to 10 years for license fees. Patented technologies are amortized using the straight-line method principally over the estimated useful life of 3 years. Customer relationships are amortized principally using the declining-balance method over the estimated useful life of 5 years. Certain costs incurred in connection with developing or obtaining internal-use software are capitalized. These costs consist primarily of payments made to third parties and the salaries of employees working on such software development. Costs incurred in connection with developing internal-use software are capitalized at the application development stage. In addition, Canon develops or obtains certain software to be sold where related costs are capitalized after establishment of technological feasibility.

(m) Environmental Liabilities

Liabilities for environmental remediation and other environmental costs are accrued when environmental assessments or remedial efforts are probable and the costs can be reasonably estimated. Such liabilities are adjusted as further information develops or circumstances change. Costs of future obligations are not discounted to their present values.

(n) Income Taxes

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Canon records a valuation allowance to reduce the deferred tax assets to the amount that is more likely than not realizable.

Canon recognizes the financial statement effects of tax positions when it is more likely than not, based on the technical merits, that the tax positions will be sustained upon examination by the tax authorities. Benefits from tax positions that meet the more-likely-than-not recognition threshold are measured at the largest amount of benefit that is greater than 50% likely of being realized upon settlement. Interest and penalties accrued related to unrecognized tax benefits are included in income taxes in the consolidated statements of income.

(o) Stock-Based Compensation

Canon measures stock-based compensation cost at the grant date, based on the fair value of the award, and recognizes the cost on a straight-line basis over the requisite service period, which is the vesting period.

(p) Net Income Attributable to Canon Inc. Stockholders per Share

Basic net income attributable to Canon Inc. stockholders per share is computed by dividing net income attributable to Canon Inc. by the weighted-average number of common shares outstanding during each year. Diluted net income attributable to Canon Inc. stockholders per share includes the effect from potential issuances of common stock based on the assumptions that all stock options were exercised.

(q) Revenue Recognition

Canon generates revenue principally through the sale of office and imaging system products, equipment, supplies, and related services under separate contractual arrangements. Canon recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred and title and risk of loss have been transferred to the customer or services have been rendered, the sales price is fixed or determinable, and collectibility is probable.

Revenue from sales of office products, such as office MFDs and laser printers, and imaging system products, such as digital cameras and inkjet printers, is recognized upon shipment or delivery, depending upon when title and risk of loss transfer to the customer.

Revenue from sales of optical equipment, such as semiconductor lithography equipment and FPD lithography equipment that are sold with customer acceptance provisions related to their functionality, is recognized when the equipment is installed at the customer site and the specific criteria of the equipment functionality are successfully tested and demonstrated by Canon. Service revenue is derived primarily from separately priced product maintenance contracts on equipment sold to customers and is measured at the stated amount of the contract and recognized as services are provided.

Canon also offers separately priced product maintenance contracts for most office products, for which the customer typically pays a stated base service fee plus a variable amount based on usage. Revenue from these service maintenance contracts is measured at the stated amount of the contract and recognized as services are provided and variable amounts are earned.

Revenue from the sale of equipment under sales-type leases is recognized at the inception of the lease. Income on sales-type leases and direct-financing leases is recognized over the life of each respective lease using the interest method. Leases not qualifying as sales-type leases or direct-financing leases are accounted for as operating leases and related revenue is recognized ratably over the lease term. When equipment leases are bundled with product maintenance contracts, revenue is first allocated considering the relative fair value of the lease and non-lease deliverables based upon the estimated relative fair values of each element. Lease deliverables generally include equipment, financing and executory costs, while non-lease deliverables generally consist of product maintenance contracts and supplies.

For all other arrangements with multiple elements, Canon allocates revenue to each element based on its relative selling price if such element meets the criteria for treatment as a separate unit of accounting. Otherwise, revenue is deferred until the undelivered elements are fulfilled and accounted for as a single unit of accounting.

Canon records estimated reductions to sales at the time of sale for sales incentive programs including product discounts, customer promotions and volume-based rebates. Estimated reductions to sales are based upon historical trends and other known factors at the time of sale. During the year ended December 31, 2012, Canon revised its estimates for sales incentive programs accrual. This change in estimate caused an increase in net income attributable to Canon Inc. by ¥10,785 million ($123,966 thousand), and an increase in basic and diluted net income attributable to Canon Inc. stockholders per share by ¥9.19 ($0.11) each. In addition, Canon provides price protection to certain resellers of its products, and records reductions to sales for the estimated impact of price protection obligations when announced.

Estimated product warranty costs are recorded at the time revenue is recognized and are included in selling, general and administrative expenses in the consolidated statements of income. Estimates for accrued product warranty costs are based on historical experience, and are affected by ongoing product failure rates, specific product class failures outside of the baseline experience, material usage and service delivery costs incurred in correcting a product failure.

Taxes collected from customers and remitted to governmental authorities are excluded from revenues in the consolidated statements of income.

(r) Research and Development Costs

Research and development costs are expensed as incurred.

(s) Advertising Costs

Advertising costs are expensed as incurred. Advertising expenses were ¥83,134 million ($955,563 thousand), ¥81,232 million and ¥94,794 million for the years ended December 31, 2012, 2011 and 2010, respectively.

(t) Shipping and Handling Costs

Shipping and handling costs totaled ¥38,499 million ($442,517 thousand), ¥43,308 million and ¥56,306 million for the years ended December 31, 2012, 2011 and 2010, respectively, and are included in selling, general and administrative expenses in the consolidated statements of income.

(u) Derivative Financial Instruments

All derivatives are recognized at fair value and are included in prepaid expenses and other current assets, or other current liabilities in the consolidated balance sheets.

Canon uses and designates certain derivatives as a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge). Canon formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedge transactions. Canon also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items. When it is determined that a derivative is not highly effective as a hedge or that it has ceased to be a highly effective hedge, Canon discontinues hedge accounting prospectively. Changes in the fair value of a derivative that is designated and qualifies as a cash flow hedge are recorded in other comprehensive income (loss), until earnings are affected by the variability in cash flows of the hedged item. Gains and losses from hedging ineffectiveness are included in other income (deductions). Gains and losses related to the components of hedging instruments excluded from the assessment of hedge effectiveness are included in other income (deductions).

Canon also uses certain derivative financial instruments which are not designated as hedges. The changes in fair values of these derivative financial instruments are immediately recorded in earnings.

Canon classifies cash flows from derivatives as cash flows from operating activities in the consolidated statements of cash flows.

(v) Guarantees

Canon recognizes, at the inception of a guarantee, a liability for the fair value of the obligation it has undertaken in issuing guarantees.

(w) Recently Issued Accounting Guidance

In June 2011, the Financial Accounting Standards Board ("FASB") issued an amendment which requires presentation of net income and other comprehensive income in one continuous statement or in two separate but consecutive statements, which is applied retrospectively for all periods presented. Canon adopted this amended guidance from the quarter beginning January 1, 2012. This adoption did not have a material impact on Canon's consolidated results of operations and financial condition.

In February 2013, the FASB issued an amendment which requires entities to provide information about the amounts reclassified out of accumulated other comprehensive income by component, and to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income. Canon will adopt this amended guidance from the quarter beginning January 1, 2013, and does not expect the adoption of this guidance to have a material impact on Canon's consolidated results of operations and financial condition.

2. BASIS OF FINANCIAL STATEMENT TRANSLATION

The consolidated financial statements presented herein are expressed in Japanese yen and, solely for the convenience of the reader, have been translated into United States dollars at the rate of ¥87 = U.S.$1, the approximate exchange rate prevailing on the Tokyo Foreign Exchange Market on December 28, 2012. This translation should not be construed as a representation that the amounts shown could be converted into United States dollars at such rate.

3. INVESTMENTS

The cost, gross unrealized holding gains, gross unrealized holding losses and fair value for available-for-sale securities included in short-term investments and investments by major security type at December 31, 2012 and 2011 were as follows:

December 31

Millions of yen	*Cost*	*Gross unrealized holding gains*	*Gross unrealized holding losses*	*Fair value*
2012: Current:				
Corporate bonds	**¥ 30**	**¥ —**	**¥ —**	**¥ 30**
Noncurrent:				
Government bonds	**¥ 181**	**¥ —**	**¥ —**	**¥ 181**
Corporate bonds	**590**	**—**	**30**	**560**
Fund trusts	**1,192**	**43**	**1**	**1,234**
Equity securities	**14,866**	**7,033**	**564**	**21,335**
	¥16,829	**¥7,076**	**¥595**	**¥23,310**

Millions of yen	*Cost*	*Gross unrealized holding gains*	*Gross unrealized holding losses*	*Fair value*
2011: Current:				
Corporate bonds	¥ 20	¥ —	¥ —	¥ 20
Noncurrent:				
Government bonds	¥ 172	¥ —	¥ 22	¥ 150
Corporate bonds	569	73	84	558
Fund trusts	1,867	2	43	1,826
Equity securities	15,911	3,200	1,387	17,724
	¥18,519	¥3,275	¥1,536	¥20,258

Thousands of U.S. dollars	*Cost*	*Gross unrealized holding gains*	*Gross unrealized holding losses*	*Fair value*
2012: Current:				
Corporate bonds	**$ 345**	**$ —**	**$ —**	**$ 345**
Noncurrent:				
Government bonds	**$ 2,080**	**$ —**	**$ —**	**$ 2,080**
Corporate bonds	**6,782**	**—**	**345**	**6,437**
Fund trusts	**13,701**	**494**	**11**	**14,184**
Equity securities	**170,874**	**80,839**	**6,483**	**245,230**
	$193,437	**$81,333**	**$6,839**	**$267,931**

Maturities of available-for-sale debt securities and fund trusts included in short-term investments and investments in the accompanying consolidated balance sheets were as follows at December 31, 2012:

December 31	*Millions of yen*		*Thousands of U.S. dollars*	
	Cost	*Fair value*	*Cost*	*Fair value*
Due within one year	¥ 30	¥ 30	$ 345	$ 345
Due after one year through five years	953	990	10,954	11,379
Due after five years through ten years	1,010	985	11,609	11,322
	¥1,993	¥2,005	$22,908	$23,046

Gross realized gains were ¥238 million ($2,736 thousand), ¥204 million and ¥641 million for the years ended December 31, 2012, 2011 and 2010, respectively. Gross realized losses, including write-downs for impairments that were other-than-temporary, were ¥1,545 million ($17,759 thousand), ¥4,281 million and ¥1,961 million for the years ended December 31, 2012, 2011 and 2010, respectively.

At December 31, 2012, substantially all of the available-for-sale securities with unrealized losses had been in a continuous unrealized loss position for less than twelve months.

Time deposits with original maturities of more than three months are ¥28,292 million ($325,195 thousand) and ¥125,497 million at December 31, 2012 and 2011, respectively, and are included in short-term investments in the accompanying consolidated balance sheets.

Aggregate cost of non-marketable equity securities accounted for under the cost method totaled ¥14,808 million ($170,207 thousand) and ¥14,583 million at December 31, 2012 and 2011, respectively. These investments were not evaluated for impairment at December 31, 2012 and 2011, respectively, because (a) Canon did not estimate the fair value of those investments as it was not practicable to estimate the fair value of the investments and (b) Canon did not identify any events or changes in circumstances that might have had significant adverse effects on the fair value of those investments.

Investments in affiliated companies accounted for by the equity method amounted to ¥17,345 million ($199,368 thousand) and ¥15,776 million at December 31, 2012 and 2011, respectively. Canon's share of the net earnings (losses) in affiliated companies accounted for by the equity method, included in other income (deductions), were earnings of ¥610 million ($7,011 thousand), losses of ¥7,368 million and earnings of ¥10,471 million for the years ended December 31, 2012, 2011 and 2010, respectively.

4. TRADE RECEIVABLES

Trade receivables are summarized as follows:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Notes	¥ 17,207	¥ 16,739	$ 197,782
Accounts	569,138	528,032	6,541,816
	586,345	544,771	6,739,598
Less allowance for doubtful receivables	(12,970)	(11,563)	(149,081)
	¥573,375	¥533,208	$6,590,517

5. INVENTORIES

Inventories are summarized as follows:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Finished goods	¥391,194	¥291,023	$4,496,483
Work in process	139,923	166,076	1,608,310
Raw materials	20,506	19,605	235,701
	¥551,623	¥476,704	$6,340,494

6. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost less accumulated depreciation and are summarized as follows:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Land	**¥ 272,233**	¥ 268,493	**$ 3,129,115**
Buildings	**1,447,838**	1,367,187	**16,641,816**
Machinery and equipment	**1,586,827**	1,499,331	**18,239,391**
Construction in progress	**112,919**	94,507	**1,297,919**
	3,419,817	3,229,518	**39,308,241**
Less accumulated depreciation	**(2,159,453)**	(2,038,682)	**(24,821,298)**
	¥1,260,364	¥1,190,836	**$14,486,943**

Depreciation expense for the years ended December 31, 2012, 2011 and 2010 was ¥211,973 million ($2,436,471 thousand), ¥210,179 million and ¥232,327 million, respectively.

Amounts due for purchases of property, plant and equipment were ¥38,893 million ($447,046 thousand) and ¥47,690 million at December 31, 2012 and 2011, respectively, and are included in other current liabilities in the accompanying consolidated balance sheets. Fixed assets presented in the consolidated statements of cash flows include property, plant and equipment and intangible assets.

7. FINANCE RECEIVABLES AND OPERATING LEASES

Finance receivables represent financing leases which consist of sales-type leases and direct-financing leases resulting from the sales of Canon's and complementary third-party products primarily in foreign countries. These receivables typically have terms ranging from 1 year to 8 years.

The components of the finance receivables, which are included in prepaid expenses and other current assets, and other assets in the accompanying consolidated balance sheets, are as follows:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Total minimum lease payments receivable	**¥231,221**	¥204,326	**$2,657,713**
Unguaranteed residual values	**8,863**	8,195	**101,873**
Executory costs	**(2,598)**	(2,275)	**(29,862)**
Unearned income	**(27,521)**	(24,955)	**(316,333)**
	209,965	185,291	**2,413,391**
Less allowance for credit losses	**(6,908)**	(7,039)	**(79,402)**
	203,057	178,252	**2,333,989**
Less current portion	**(74,168)**	(66,337)	**(852,506)**
	¥128,889	¥111,915	**$1,481,483**

The activity in the allowance for credit losses is as follows:

Years ended December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Balance at beginning of year	**¥7,039**	¥7,983	**$80,908**
Charge-offs	**(1,304)**	(1,937)	**(14,989)**
Provision	**1,922**	2,052	**22,092**
Other	**(749)**	(1,059)	**(8,609)**
Balance at end of year	**¥6,908**	¥7,039	**$79,402**

Canon has policies in place to ensure that its products are sold to customers with an appropriate credit history, and continuously monitors its customers' credit quality based on information including length of period in arrears, macroeconomic conditions, initiation of legal proceedings against customers and bankruptcy filings. The allowance for credit losses of finance receivables are evaluated collectively based on historical experience of credit losses. An additional reserve for individual accounts is recorded when Canon becomes aware of a customer's inability to meet its financial obligations, such as in the case of bankruptcy filings. Finance receivables which are past due or individually evaluated for impairment at December 31, 2012 and 2011 are not significant.

The cost of equipment leased to customers under operating leases included in property, plant and equipment, net at December 31, 2012 and 2011 was ¥80,186 million ($921,678 thousand) and ¥75,391 million, respectively. Accumulated depreciation on equipment under operating leases at December 31, 2012 and 2011 was ¥58,433 million ($671,644 thousand) and ¥54,791 million, respectively.

The following is a schedule by year of the future minimum lease payments to be received under financing leases and noncancelable operating leases at December 31, 2012.

Year ending December 31:	*Millions of yen*		*Thousands of U.S. dollars*	
	Financing leases	*Operating leases*	*Financing leases*	*Operating leases*
2013	¥ 89,794	¥ 7,073	$1,032,115	$ 81,299
2014	63,348	4,359	728,138	50,103
2015	38,983	3,038	448,080	34,920
2016	19,221	2,195	220,931	25,230
2017	19,472	1,671	223,816	19,207
Thereafter	403	4,084	4,633	46,942
	¥231,221	¥22,420	$2,657,713	$257,701

8. ACQUISITIONS

In March 2010, Canon acquired 45.2% of the total outstanding shares of Océ N.V. ("Océ"), which was listed on NYSE Euronext Amsterdam, principally through a fully self-funded public cash tender offer for consideration of ¥50,374 million, in addition to the 22.9% interest Canon held before the public cash tender offer. In addition, Canon acquired Océ's convertible cumulative financing preference shares representing 19.1% of the total outstanding shares of Océ for consideration of ¥8,027 million. As a result, Canon's aggregate interest represented 87.2% of the total outstanding shares of Océ at that time. The fair value of the 12.8% noncontrolling interest in Océ of ¥18,245 million was measured based on the quoted price of Océ's common stock on the acquisition date. Canon holds 99.4% of Océ's outstanding shares at December 31, 2012.

The acquisition was accounted for using the acquisition method. Prior to the March 2010 acquisition date, Canon accounted for its 22.9% interest in Océ using the equity method. The acquisition-date fair value of the previous equity interest of ¥25,508 million was remeasured using the quoted price of Océ's common stock on the acquisition date and included in the measurement of the total acquisition consideration. In connection with the acquisition, Canon repaid ¥55,378 million of Océ's existing bank debt and ¥22,936 million of Océ's existing United States Private Placement notes, which are included in decrease in short-term loans in the consolidated statement of cash flows.

Océ is engaged in research and development, manufacture and sale of document management systems, printing systems for professionals and high-speed, wide format digital printing systems. Canon and Océ have complementary technologies and products and would benefit from this strong business relationship. Amid the increasingly competitive printing industry, Canon is further strengthening its business foundation in order to solidify its position as one of the global leaders. Canon aims to provide diversified solutions to its customers in the printing industry by making Océ a consolidated subsidiary.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at acquisition date.

	Millions of yen
Current assets	¥122,248
Property, plant and equipment	51,156
Intangible assets	56,297
Goodwill	77,253
Other noncurrent assets	42,658
Non-current assets	227,364
Total acquired assets	349,612
Total assumed liabilities	247,458
Net assets acquired	¥102,154

Intangible assets acquired, which are subject to amortization, consist of customer relationships of ¥32,747 million, patented technologies of ¥11,316 million, and other intangible assets of ¥12,234 million. Canon has estimated the amortization period for the customer relationships and patented technologies to be 5 years and 3 years, respectively. The weighted average amortization period for all intangible assets is approximately 4.4 years.

Goodwill recognized, which is assigned to the Office Business Unit for impairment testing, is attributable primarily to expected synergies from combining operations of Océ and Canon. None of the goodwill is expected to be deductible for income tax purposes.

The amount of net sales of Océ included in Canon's consolidated statement of income from the acquisition date for the year ended December 31, 2010 was ¥246,518 million.

The unaudited pro forma net sales as if Océ had been included in Canon's consolidated statements of income from the beginning of the year ended December 31, 2010 was ¥3,772,425 million. Pro forma net income was not disclosed because the impact on Canon's consolidated statements of income was not material.

Canon acquired businesses other than this described above during the years ended December 31, 2012, 2011, and 2010. Such acquisitions were accounted for using the acquisition method but were not material to its consolidated financial statements.

9. GOODWILL AND OTHER INTANGIBLE ASSETS

Intangible assets subject to amortization acquired during the years ended December 31, 2012 and 2011 totaled ¥34,196 million ($393,057 thousand) and ¥35,994 million, which primarily consist of software of ¥33,985 million ($390,632 thousand) and ¥33,217 million, respectively. The weighted average amortization periods for intangible assets in total acquired during the years ended December 31, 2012 and 2011 are approximately 4 years and 5 years, respectively. The weighted average amortization periods for software acquired during the years ended December 31, 2012 and 2011 are approximately 4 years.

The components of intangible assets subject to amortization at December 31, 2012 and 2011 were as follows:

December 31	**2012**		2011	
Millions of yen	*Gross carrying amount*	*Accumulated amortization*	*Gross carrying amount*	*Accumulated amortization*
Software	**¥225,894**	**¥131,875**	¥205,235	¥115,131
Customer relationships	**39,615**	**26,938**	34,957	18,724
Patented technologies	**25,900**	**19,028**	24,342	13,317
License fees	**20,142**	**14,573**	20,425	12,867
Other	**22,776**	**9,382**	19,235	6,857
	¥334,327	**¥201,796**	¥304,194	¥166,896

December 31 Thousands of U.S. dollars	2012 Gross carrying amount	 Accumulated amortization
Software	**$2,596,483**	**$1,515,805**
Customer relationships	**455,345**	**309,632**
Patented technologies	**297,701**	**218,713**
License fees	**231,517**	**167,506**
Other	**261,793**	**107,838**
	$3,842,839	**$2,319,494**

Aggregate amortization expense for the years ended December 31, 2012, 2011 and 2010 was ¥46,160 million ($530,575 thousand), ¥51,164 million and ¥43,866 million, respectively. Estimated amortization expense for intangible assets currently held for the next five years ending December 31 is ¥44,409 million ($510,448 thousand) in 2013, ¥34,219 million ($393,322 thousand) in 2014, ¥20,576 million ($236,506 thousand) in 2015, ¥11,822 million ($135,885 thousand) in 2016, and ¥6,605 million ($75,920 thousand) in 2017.

Intangible assets not subject to amortization other than goodwill at December 31, 2012 and 2011 were not significant.

For management reporting purposes, goodwill is not allocated to the segments. Goodwill has been allocated to its respective segment for impairment testing.

The changes in the carrying amount of goodwill by segment, which is included in other assets in the consolidated balance sheets, for the years ended December 31, 2012 and 2011 were as follows:

Years ended December 31 Millions of yen	Office	Imaging System	Industry and Others	Total
2012: Balance at beginning of year	**¥102,060**	**¥12,088**	**¥4,873**	**¥119,021**
Goodwill acquired during the year	**—**	**—**	**961**	**961**
Translation adjustments and other	**9,288**	**586**	**987**	**10,861**
Balance at end of year	**¥111,348**	**¥12,674**	**¥6,821**	**¥130,843**

Millions of yen	Office	Imaging System	Industry and Others	Total
2011: Balance at beginning of year	¥107,301	¥12,386	¥5,502	¥125,189
Translation adjustments and other	(5,241)	(298)	(629)	(6,168)
Balance at end of year	¥102,060	¥12,088	¥4,873	¥119,021

Thousands of U.S. dollars	Office	Imaging System	Industry and Others	Total
2012: Balance at beginning of year	**$1,173,103**	**$138,943**	**$56,012**	**$1,368,058**
Goodwill acquired during the year	**—**	**—**	**11,046**	**11,046**
Translation adjustments and other	**106,759**	**6,735**	**11,345**	**124,839**
Balance at end of year	**$1,279,862**	**$145,678**	**$78,403**	**$1,503,943**

10. SHORT-TERM LOANS AND LONG-TERM DEBT

Short-term loans consisting of bank borrowings at December 31, 2012 and 2011 were ¥319 million ($3,666 thousand) and ¥4,641 million, respectively. The weighted average interest rates on short-term loans outstanding at December 31, 2012 and 2011 were 4.00% and 2.72%, respectively.

Long-term debt consisted of the following:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Loans, principally from banks, maturing in installments through 2020; bearing weighted average interest of 1.94% and 1.68% at December 31, 2012 and 2011, respectively	**¥ 132**	¥1,297	**$ 1,517**
0.75% Japanese yen notes, due 2012	**—**	1,020	**—**
0.84% Japanese yen notes, due 2013	**—**	156	**—**
Capital lease obligations	**3,532**	4,597	**40,598**
	3,664	7,070	**42,115**
Less current portion	**(1,547)**	(3,702)	**(17,782)**
	¥2,117	¥3,368	**$24,333**

The aggregate annual maturities of long-term debt outstanding at December 31, 2012 were as follows:

Year ending December 31:	*Millions of yen*	*Thousands of U.S. dollars*
2013	¥1,547	$17,782
2014	1,199	13,781
2015	611	7,023
2016	182	2,092
2017	91	1,046
Thereafter	34	391
	¥3,664	$42,115

Both short-term and long-term bank loans are made under general agreements which provide that security and guarantees for present and future indebtedness will be given upon request of the bank, and that the bank shall have the right to offset cash deposits against obligations that have become due or, in the event of default, against all obligations due to the bank.

11. TRADE PAYABLES

Trade payables are summarized as follows:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Notes	**¥ 11,971**	¥ 16,519	**$ 137,598**
Accounts	**313,264**	364,013	**3,600,735**
	¥325,235	¥380,532	**$3,738,333**

12. EMPLOYEE RETIREMENT AND SEVERANCE BENEFITS

The Company and certain of its subsidiaries have contributory and noncontributory defined benefit pension plans covering substantially all of their employees. Benefits payable under the plans are based on employee earnings and years of service. The Company and certain of its subsidiaries also have defined contribution pension plans covering substantially all of their employees.

The amounts of cost recognized for the defined contribution pension plans of the Company and certain of its subsidiaries for the years ended December 31, 2012, 2011 and 2010 were ¥13,021 million ($149,667 thousand), ¥12,511 million and ¥11,780 million, respectively.

Obligations and funded status

Reconciliations of beginning and ending balances of the benefit obligations and the fair value of the plan assets are as follows:

Years ended December 31	*Japanese plans*			*Foreign plans*		
	Millions of yen		*Thousands of U.S. dollars*	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**	**2012**	2011	**2012**
Change in benefit obligations:						
Benefit obligations at beginning of year	**¥ 626,924**	¥ 593,274	**$ 7,206,023**	**¥262,130**	¥261,130	**$ 3,012,989**
Service cost	**25,738**	25,875	**295,839**	**5,884**	5,756	**67,632**
Interest cost	**11,788**	12,354	**135,494**	**13,176**	12,748	**151,448**
Plan participants' contributions	**—**	—	**—**	**2,315**	2,680	**26,609**
Amendments	**—**	(1,913)	**—**	**—**	—	**—**
Actuarial loss	**6,049**	14,845	**69,529**	**45,145**	3,872	**518,908**
Benefits paid	**(18,979)**	(17,511)	**(218,149)**	**(10,407)**	(8,234)	**(119,621)**
Foreign currency exchange rate changes	**—**	—	**—**	**46,366**	(15,822)	**532,943**
Benefit obligations at end of year	**651,520**	626,924	**7,488,736**	**364,609**	262,130	**4,190,908**
Change in plan assets:						
Fair value of plan assets at beginning of year	**448,736**	460,090	**5,157,885**	**192,033**	197,835	**2,207,276**
Actual return on plan assets	**41,593**	(17,285)	**478,080**	**25,290**	2,335	**290,690**
Employer contributions	**22,589**	22,282	**259,644**	**7,832**	8,228	**90,023**
Plan participants' contributions	**—**	—	**—**	**2,315**	2,680	**26,609**
Benefits paid	**(17,466)**	(16,351)	**(200,758)**	**(9,825)**	(8,201)	**(112,931)**
Foreign currency exchange rate changes	**—**	—	**—**	**31,889**	(10,844)	**366,540**
Fair value of plan assets at end of year	**495,452**	448,736	**5,694,851**	**249,534**	192,033	**2,868,207**
Funded status at end of year	**¥(156,068)**	¥(178,188)	**$(1,793,885)**	**¥(115,075)**	¥(70,097)	**$(1,322,701)**

Amounts recognized in the consolidated balance sheets at December 31, 2012 and 2011 are as follows:

December 31	*Japanese plans*			*Foreign plans*		
	Millions of yen		*Thousands of U.S. dollars*	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**	**2012**	2011	**2012**
Other assets	**¥ —**	¥ 54	**$ —**	**¥ 1,371**	¥ 1,397	**$ 15,759**
Accrued expenses	**—**	—	**—**	**(383)**	(132)	**(4,402)**
Accrued pension and severance cost	**(156,068)**	(178,242)	**(1,793,885)**	**(116,063)**	(71,362)	**(1,334,058)**
	¥(156,068)	¥(178,188)	**$(1,793,885)**	**¥(115,075)**	¥(70,097)	**$(1,322,701)**

Amounts recognized in accumulated other comprehensive income (loss) at December 31, 2012 and 2011 before the effect of income taxes are as follows:

December 31	*Japanese plans*			*Foreign plans*		
	Millions of yen		*Thousands of U.S. dollars*	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**	**2012**	2011	**2012**
Actuarial loss	**¥253,748**	¥291,778	**$2,916,643**	**¥50,417**	¥16,095	**$579,506**
Prior service credit	**(117,633)**	(130,712)	**(1,352,103)**	**(261)**	(345)	**(3,000)**
	¥136,115	¥161,066	**$1,564,540**	**¥50,156**	¥15,750	**$576,506**

The accumulated benefit obligation for all defined benefit plans was as follows:

December 31	*Japanese plans*			*Foreign plans*		
	Millions of yen		*Thousands of U.S. dollars*	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**	**2012**	2011	**2012**
Accumulated benefit obligation	**¥620,589**	¥595,689	**$7,133,207**	**¥328,736**	¥238,675	**$3,778,575**

The projected benefit obligations and the fair value of plan assets for the pension plans with projected benefit obligations in excess of plan assets, and the accumulated benefit obligations and the fair value of plan assets for the pension plans with accumulated benefit obligations in excess of plan assets are as follows:

December 31	*Japanese plans*			*Foreign plans*		
	Millions of yen		*Thousands of U.S. dollars*	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**	**2012**	2011	**2012**
Plans with projected benefit obligations in excess of plan assets:						
Projected benefit obligations	**¥651,520**	¥622,645	**$7,488,736**	**¥360,742**	¥259,517	**$4,146,460**
Fair value of plan assets	**495,452**	444,403	**5,694,851**	**244,296**	188,023	**2,808,000**
Plans with accumulated benefit obligations in excess of plan assets:						
Accumulated benefit obligations	**¥615,551**	¥591,830	**$7,075,299**	**¥324,869**	¥160,941	**$3,734,126**
Fair value of plan assets	**489,929**	444,403	**5,631,368**	**244,296**	111,527	**2,808,000**

Components of net periodic benefit cost and other amounts recognized in other comprehensive income (loss)

Net periodic benefit cost for Canon's employee retirement and severance defined benefit plans for the years ended December 31, 2012, 2011 and 2010 consisted of the following components:

Years ended December 31	*Japanese plans*				*Foreign plans*			
	Millions of yen			*Thousands of U.S. dollars*	*Millions of yen*			*Thousands of U.S. dollars*
	2012	2011	2010	**2012**	**2012**	2011	2010	**2012**
Service cost	**¥25,738**	¥25,875	¥23,331	**$295,839**	**¥ 5,884**	¥ 5,756	¥ 5,660	**$ 67,632**
Interest cost	**11,788**	12,354	12,636	**135,494**	**13,176**	12,748	11,792	**151,448**
Expected return on plan assets	**(13,791)**	(16,485)	(16,591)	**(158,516)**	**(11,806)**	(12,112)	(10,540)	**(135,702)**
Amortization of net transition obligation	**—**	722	722	**—**	**—**	—	—	**—**
Amortization of prior service credit	**(13,079)**	(13,674)	(13,878)	**(150,334)**	**(116)**	(93)	(116)	**(1,333)**
Amortization of actuarial loss	**16,277**	14,462	14,545	**187,092**	**1,351**	621	1,050	**15,529**
	¥26,933	¥23,254	¥20,765	**$309,575**	**¥ 8,489**	¥ 6,920	¥ 7,846	**$ 97,574**

Other changes in plan assets and benefit obligations recognized in other comprehensive income (loss) for the years ended December 31, 2012, 2011 and 2010 are summarized as follows:

Years ended December 31	*Japanese plans*				*Foreign plans*			
	Millions of yen			*Thousands of U.S. dollars*	*Millions of yen*			*Thousands of U.S. dollars*
	2012	2011	2010	**2012**	**2012**	2011	2010	**2012**
Current year actuarial (gain) loss	**¥(21,753)**	¥48,615	¥34,348	**$ (250,035)**	**¥31,661**	¥13,649	¥(14,713)	**$363,920**
Amortization of actuarial loss	**(16,277)**	(14,462)	(14,545)	**(187,092)**	**(1,351)**	(621)	(1,050)	**(15,529)**
Prior service credit due to amendments	**—**	(1,913)	(423)	**—**	**—**	—	(149)	**—**
Amortization of prior service credit	**13,079**	13,674	13,878	**150,334**	**116**	93	116	**1,333**
Amortization of net transition obligation	**—**	(722)	(722)	**—**	**—**	—	—	**—**
	¥(24,951)	¥45,192	¥32,536	**$ (286,793)**	**¥30,426**	¥13,121	¥(15,796)	**$349,724**

The estimated prior service credit and actuarial loss for the defined benefit pension plans that will be amortized from accumulated other comprehensive income (loss) into net periodic benefit cost over the next year are summarized as follows:

	Japanese plans		*Foreign plans*	
	Millions of yen	*Thousands of U.S. dollars*	*Millions of yen*	*Thousands of U.S. dollars*
Prior service credit	¥(13,070)	$(150,230)	¥ (124)	$ (1,425)
Actuarial loss	14,414	165,678	1,413	16,241

Assumptions

Weighted-average assumptions used to determine benefit obligations are as follows:

December 31	*Japanese plans*		*Foreign plans*	
	2012	2011	**2012**	2011
Discount rate	**1.8%**	1.9%	**3.6%**	4.6%
Assumed rate of increase in future compensation levels	**3.0%**	3.0%	**2.2%**	2.4%

Weighted-average assumptions used to determine net periodic benefit cost are as follows:

Years ended December 31	*Japanese plans*			*Foreign plans*		
	2012	2011	2010	**2012**	2011	2010
Discount rate	**1.9%**	2.1%	2.3%	**4.6%**	4.9%	4.9%
Assumed rate of increase in future compensation levels	**3.0%**	3.0%	3.0%	**2.4%**	2.9%	2.8%
Expected long-term rate of return on plan assets	**3.1%**	3.6%	3.6%	**5.4%**	5.7%	6.1%

Canon determines the expected long-term rate of return based on the expected long-term return of the various asset categories in which it invests. Canon considers the current expectations for future returns and the actual historical returns of each plan asset category.

Plan assets

Canon's investment policies are designed to ensure adequate plan assets are available to provide future payments of pension benefits to eligible participants. Taking into account the expected long-term rate of return on plan assets, Canon formulates a “model” portfolio comprised of the optimal combination of equity securities and debt securities. Plan assets are invested in individual equity and debt securities using the guidelines of the “model” portfolio in order to produce a total return that will match the expected return on a mid-term to long-term basis. Canon evaluates the gap between expected return and actual return of invested plan assets on an annual basis to determine if such differences necessitate a revision in the formulation of the “model” portfolio. Canon revises the “model” portfolio when and to the extent considered necessary to achieve the expected long-term rate of return on plan assets.

Canon’s model portfolio for Japanese plans consists of three major components: approximately 30% is invested in equity securities, approximately 50% is invested in debt securities, and approximately 20% is invested in other investment vehicles, primarily consisting of investments in life insurance company general accounts.

Outside Japan, investment policies vary by country, but the long-term investment objectives and strategies remain consistent. Canon’s model portfolio for foreign plans has been developed as follows: approximately 40% is invested in equity securities, approximately 55% is invested in debt securities, and approximately 5% is invested in other investment vehicles, primarily consisting of investments in real estate assets.

The equity securities are selected primarily from stocks that are listed on the securities exchanges. Prior to investing, Canon has investigated the business condition of the investee companies, and appropriately diversified investments by type of industry and other relevant factors. The debt securities are selected primarily from government bonds, public debt instruments, and corporate bonds. Prior to investing, Canon has investigated the quality of the issue, including rating, interest rate, and repayment dates, and has appropriately diversified the investments. Pooled funds are selected using strategies consistent with the equity and debt securities described above. As for investments in life insurance company general accounts, the contracts with the insurance companies include a guaranteed interest rate and return of capital. With respect to investments in foreign investment vehicles, Canon has investigated the stability of the underlying governments and economies, the market characteristics such as settlement systems and the taxation systems. For each such investment, Canon has selected the appropriate investment country and currency.

The three levels of input used to measure fair value are more fully described in Note 21. The fair values of Canon’s pension plan assets at December 31, 2012 and 2011, by asset category, are as follows:

December 31, 2012	*Millions of yen*							
	Japanese plans				*Foreign plans*			
	Level 1	*Level 2*	*Level 3*	*Total*	*Level 1*	*Level 2*	*Level 3*	*Total*
Equity securities:								
Japanese companies (a)	¥34,387	¥ —	¥ —	¥ 34,387	¥ —	¥ —	¥—	¥ —
Foreign companies	6,560	—	—	6,560	13,149	—	—	13,149
Pooled funds (b)	—	99,631	—	99,631	—	60,142	—	60,142
Debt securities:								
Government bonds (c)	20,301	—	—	20,301	4,345	—	—	4,345
Municipal bonds	—	1,064	—	1,064	—	21	—	21
Corporate bonds	—	8,425	—	8,425	—	—	—	—
Pooled funds (d)	—	192,386	—	192,386	—	128,647	—	128,647
Mortgage backed securities (and other asset backed securities)	—	8,400	—	8,400	—	236	—	236
Life insurance company general accounts	—	113,179	—	113,179	—	1,857	—	1,857
Other assets	—	9,813	1,306	11,119	—	41,137	—	41,137
	¥61,248	¥432,898	¥1,306	¥495,452	¥17,494	¥232,040	¥—	¥249,534

December 31, 2011	Millions of yen							
	Japanese plans				Foreign plans			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Equity securities:								
Japanese companies (e)	¥37,875	¥ —	¥ —	¥ 37,875	¥ —	¥ —	¥ —	¥ —
Foreign companies	4,804	—	—	4,804	3,779	—	—	3,779
Pooled funds (f)	—	82,380	—	82,380	—	47,779	—	47,779
Debt securities:								
Government bonds (g)	17,951	—	—	17,951	2,326	—	—	2,326
Municipal bonds	—	864	—	864	—	19	—	19
Corporate bonds	—	8,170	—	8,170	—	—	—	—
Pooled funds (h)	—	190,832	—	190,832	—	92,653	—	92,653
Mortgage backed securities (and other asset backed securities)	—	4,842	—	4,842	—	2,726	—	2,726
Life insurance company general accounts	—	92,700	—	92,700	—	—	—	—
Other assets	—	7,171	1,147	8,318	—	42,751	—	42,751
	¥60,630	¥386,959	¥1,147	¥448,736	¥6,105	¥185,928	¥ —	¥192,033

December 31, 2012	Thousands of U.S. dollars							
	Japanese plans				Foreign plans			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Equity securities:								
Japanese companies (a)	$395,253	$ —	$ —	$ 395,253	$ —	$ —	$ —	$ —
Foreign companies	75,402	—	—	75,402	151,138	—	—	151,138
Pooled funds (b)	—	1,145,184	—	1,145,184	—	691,287	—	691,287
Debt securities:								
Government bonds (c)	233,345	—	—	233,345	49,943	—	—	49,943
Municipal bonds	—	12,230	—	12,230	—	241	—	241
Corporate bonds	—	96,839	—	96,839	—	—	—	—
Pooled funds (d)	—	2,211,333	—	2,211,333	—	1,478,701	—	1,478,701
Mortgage backed securities (and other asset backed securities)	—	96,552	—	96,552	—	2,713	—	2,713
Life insurance company general accounts	—	1,300,908	—	1,300,908	—	21,345	—	21,345
Other assets	—	112,793	15,012	127,805	—	472,839	—	472,839
	$704,000	$4,975,839	$15,012	$5,694,851	$201,081	$2,667,126	$ —	$2,868,207

(a) The plan's equity securities include common stock of the Company and certain of its subsidiaries in the amounts of ¥565 million ($6,494 thousand).

(b) These funds invest in listed equity securities consisting of approximately 20% Japanese companies and 80% foreign companies for Japanese plans, and mainly foreign companies for foreign plans.

(c) This class includes approximately 30% Japanese government bonds and 70% foreign government bonds for Japanese plans, and mainly foreign government bonds for foreign plans.

(d) These funds invest in approximately 65% Japanese government bonds, 25% foreign government bonds, 5% Japanese municipal bonds, and 5% corporate bonds for Japanese plans. These funds invest in approximately 30% foreign government bonds and 70% corporate bonds for foreign plans.

(e) The plan's equity securities include common stock of the Company and certain of its subsidiaries in the amounts of ¥1,129 million.

(f) These funds invest in listed equity securities consisting of approximately 50% Japanese companies and 50% foreign companies for Japanese plans, and mainly foreign companies for foreign plans.
(g) This class includes approximately 30% Japanese government bonds and 70% foreign government bonds for Japanese plans, and mainly foreign government bonds for foreign plans.
(h) These funds invest in approximately 75% Japanese government bonds, 15% foreign government bonds, 5% Japanese municipal bonds, and 5% corporate bonds for Japanese plans. These funds invest in approximately 40% foreign government bonds and 60% corporate bonds for foreign plans.

Each level into which assets are categorized is based on inputs used to measure the fair value of the assets, and does not necessarily indicate the risks or ratings of the assets.

Level 1 assets are comprised principally of equity securities and government bonds, which are valued using unadjusted quoted market prices in active markets with sufficient volume and frequency of transactions. Level 2 assets are comprised principally of pooled funds that invest in equity and debt securities, corporate bonds and investments in life insurance company general accounts. Pooled funds are valued at their net asset values that are calculated by the sponsor of the fund and have daily liquidity. Corporate bonds are valued using quoted prices for identical assets in markets that are not active. Investments in life insurance company general accounts are valued at conversion value.

The fair value of Level 3 assets, consisting of hedge funds, was ¥1,306 million ($15,012 thousand) and ¥1,147 million at December 31, 2012 and 2011, respectively. Amounts of actual returns on, and purchases and sales of, these assets during the years ended December 31, 2012 and 2011 were not significant.

Contributions

Canon expects to contribute ¥18,610 million ($213,908 thousand) to its Japanese defined benefit pension plans and ¥21,454 million ($246,598 thousand) to its foreign defined benefit pension plans for the year ending December 31, 2013.

Estimated future benefit payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

Year ending December 31:	*Japanese plans*		*Foreign plans*	
	Millions of yen	*Thousands of U.S. dollars*	*Millions of yen*	*Thousands of U.S. dollars*
2013	¥ 15,961	$ 183,460	¥ 8,954	$102,920
2014	16,947	194,793	8,876	102,023
2015	18,765	215,690	9,094	104,529
2016	20,524	235,908	9,792	112,552
2017	21,970	252,529	10,467	120,310
2018-2022	141,232	1,623,356	61,438	706,184

13. INCOME TAXES

Domestic and foreign components of income before income taxes and the current and deferred income tax expense (benefit) attributable to such income are summarized as follows:

Years ended December 31	*Millions of yen*		
	Japanese	*Foreign*	*Total*
2012: Income before income taxes	**¥257,640**	**¥84,917**	**¥342,557**
Income taxes:			
Current	**¥ 73,573**	**¥29,052**	**¥102,625**
Deferred	**13,900**	**(6,413)**	**7,487**
	¥ 87,473	**¥22,639**	**¥110,112**
2011: Income before income taxes	¥287,592	¥86,932	¥374,524
Income taxes:			
Current	¥ 67,671	¥23,615	¥ 91,286
Deferred	21,047	8,082	29,129
	¥ 88,718	¥31,697	¥120,415
2010: Income before income taxes	¥302,965	¥89,898	¥392,863
Income taxes:			
Current	¥ 78,359	¥32,420	¥110,779
Deferred	35,496	(6,115)	29,381
	¥113,855	¥26,305	¥140,160

	Thousands of U.S. dollars		
	Japanese	*Foreign*	*Total*
2012: Income before income taxes	**$2,961,379**	**$976,058**	**$3,937,437**
Income taxes:			
Current	**$ 845,667**	**$333,931**	**$1,179,598**
Deferred	**159,770**	**(73,713)**	**86,057**
	$1,005,437	**$260,218**	**$1,265,655**

The Company and its domestic subsidiaries are subject to a number of income taxes, which, in the aggregate, represent a statutory income tax rate of approximately 40% for the years ended December 31, 2012, 2011 and 2010.

Amendments to the Japanese tax regulations were enacted into law on November 30, 2011. As a result of these amendments, the statutory income tax rate will be reduced from approximately 40% to 38% effective from the year beginning January 1, 2013, and to approximately 35% effective from the year beginning January 1, 2016 thereafter. Consequently, the statutory income tax rate utilized for deferred tax assets and liabilities expected to be settled or realized in the period from January 1, 2013 to December 31, 2015 is approximately 38% and for periods subsequent to December 31, 2015 the rate is approximately 35%. The adjustments of deferred tax assets and liabilities for this change in the tax rate amounted to ¥6,599 million and have been reflected in income taxes in the consolidated statement of income for the year ended December 31, 2011.

A reconciliation of the Japanese statutory income tax rate and the effective income tax rate as a percentage of income before income taxes is as follows:

Years ended December 31	**2012**	2011	2010
Japanese statutory income tax rate	**40.0%**	40.0%	40.0%
Increase (reduction) in income taxes resulting from:			
Expenses not deductible for tax purposes	**0.8**	0.6	0.8
Income of foreign subsidiaries taxed at lower than Japanese statutory tax rate	**(4.3)**	(4.3)	(3.5)
Tax credit for research and development expenses	**(5.7)**	(3.9)	(5.1)
Change in valuation allowance	**(1.7)**	(0.5)	2.8
Effect of enacted changes in tax laws and rates on Japanese tax	**—**	1.8	—
Other	**3.0**	(1.5)	0.7
Effective income tax rate	**32.1%**	32.2%	35.7%

Net deferred income tax assets and liabilities are included in the accompanying consolidated balance sheets under the following captions:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Prepaid expenses and other current assets	**¥ 62,358**	¥ 61,961	**$ 716,759**
Other assets	**121,934**	130,582	**1,401,540**
Other current liabilities	**(2,662)**	(1,735)	**(30,598)**
Other noncurrent liabilities	**(44,712)**	(43,542)	**(513,931)**
	¥136,918	¥147,266	**$1,573,770**

The tax effects of temporary differences that give rise to the deferred tax assets and deferred tax liabilities at December 31, 2012 and 2011 are presented below:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Deferred tax assets:			
Inventories	**¥ 13,040**	¥ 18,885	**$ 149,885**
Accrued business tax	**4,754**	3,227	**54,644**
Accrued pension and severance cost	**86,442**	90,025	**993,586**
Research and development – costs capitalized for tax purposes	**12,658**	12,898	**145,494**
Property, plant and equipment	**28,780**	31,624	**330,805**
Accrued expenses	**36,528**	37,992	**419,862**
Net operating losses carried forward	**32,494**	31,967	**373,494**
Other	**41,366**	38,220	**475,471**
	256,062	264,838	**2,943,241**
Less valuation allowance	**(32,167)**	(33,788)	**(369,735)**
Total deferred tax assets	**223,895**	231,050	**2,573,506**
Deferred tax liabilities:			
Undistributed earnings of foreign subsidiaries	**(8,235)**	(6,783)	**(94,655)**
Net unrealized gains on securities	**(2,437)**	(1,180)	**(28,011)**
Tax deductible reserve	**(6,417)**	(6,385)	**(73,759)**
Financing lease revenue	**(41,417)**	(40,878)	**(476,057)**
Prepaid pension and severance cost	**(1,073)**	(2,224)	**(12,333)**
Other	**(27,398)**	(26,334)	**(314,921)**
Total deferred tax liabilities	**(86,977)**	(83,784)	**(999,736)**
Net deferred tax assets	**¥136,918**	¥147,266	**$1,573,770**

The net changes in the total valuation allowance were a decrease of ¥1,621 million ($18,632 thousand) for the year ended December 31, 2012, a decrease of ¥1,519 million and an increase of ¥13,119 million for the years ended December 31, 2011 and 2010, respectively.

Based upon the level of historical taxable income and projections for future taxable income over the periods which the net deductible temporary differences are expected to reverse, management believes it is more likely than not that Canon will realize the benefits of these deferred tax assets, net of the existing valuation allowance, at December 31, 2012.

At December 31, 2012, Canon had net operating losses which can be carried forward for income tax purposes of ¥122,850 million ($1,412,069 thousand) to reduce future taxable income.

Periods available to reduce future taxable income vary in each tax jurisdiction and generally range from one year to twenty years as follows:

	Millions of yen	*Thousands of U.S. dollars*
Within one year	¥ 2,583	$ 29,690
After one year through five years	28,470	327,241
After five years through ten years	15,803	181,644
After ten years through twenty years	44,533	511,874
Indefinite period	31,461	361,620
Total	¥122,850	$1,412,069

Income taxes have not been accrued on undistributed earnings of domestic subsidiaries as the tax law provides a means by which the dividends from a domestic subsidiary can be received tax free.

Canon has not recognized deferred tax liabilities of ¥22,604 million ($259,816 thousand) for a portion of undistributed earnings of foreign subsidiaries that arose for the year ended December 31, 2012 and prior years because Canon currently does not expect to have such amounts distributed or paid as dividends to the Company in the foreseeable future. Deferred tax liabilities will be recognized when Canon expects that it will realize those undistributed earnings in a taxable manner, such as through receipt of dividends or sale of the investments. At December 31, 2012, such undistributed earnings of these subsidiaries were ¥894,850 million ($10,285,632 thousand).

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

Years ended December 31	*Millions of yen*			*Thousands of U.S. dollars*
	2012	2011	2010	**2012**
Balance at beginning of year	**¥2,933**	¥6,035	¥13,235	**$33,713**
Additions for tax positions of the current year	**869**	149	73	**9,989**
Additions for tax positions of prior years	**4,903**	431	805	**56,356**
Reductions for tax positions of prior years	**(1,546)**	(2,139)	(8,354)	**(17,770)**
Settlements with tax authorities	**(41)**	(1,264)	(2,471)	**(471)**
Additions from acquisitions	**—**	—	4,066	**—**
Other	**593**	(279)	(1,319)	**6,815**
Balance at end of year	**¥7,711**	¥2,933	¥ 6,035	**$88,632**

The total amounts of unrecognized tax benefits that would reduce the effective tax rate, if recognized, are ¥7,711 million ($88,632 thousand) and ¥2,809 million at December 31, 2012 and 2011, respectively.

Although Canon believes its estimates and assumptions of unrecognized tax benefits are reasonable, uncertainty regarding the final determination of tax audit settlements and any related litigation could affect the effective tax rate in the future period. Based on each of the items of which Canon is aware at December 31, 2012, no significant changes to the unrecognized tax benefits are expected within the next twelve months.

Canon recognizes interest and penalties accrued related to unrecognized tax benefits in income taxes. Both interest and penalties accrued at December 31, 2012 and 2011, and interest and penalties included in income taxes for the years ended December 31, 2012, 2011 and 2010 are not material.

Canon files income tax returns in Japan and various foreign tax jurisdictions. In Japan, Canon is no longer subject to regular income tax examinations by the tax authority for years before 2012. While there has been no specific indication by the tax authority that Canon will be subject to a transfer pricing examination in the near future, the tax authority could conduct a transfer pricing examination for years after 2003. In other major foreign tax jurisdictions, including the United States and the Netherlands, Canon is no longer subject to income tax examinations by tax authorities for years before 2006 with few exceptions. The tax authorities are currently conducting income tax examinations of Canon's income tax returns for years after 2005 in major foreign tax jurisdictions.

14. LEGAL RESERVE AND RETAINED EARNINGS

The Corporation Law of Japan provides that an amount equal to 10% of distributions from retained earnings paid by the Company and its Japanese subsidiaries be appropriated as a legal reserve. No further appropriations are required when the total amount of the additional paid-in capital and the legal reserve equals 25% of their respective stated capital. The Corporation Law of Japan also provides that additional paid-in capital and legal reserve are available for appropriations by the resolution of the stockholders. Certain foreign subsidiaries are also required to appropriate their earnings to legal reserves under the laws of the respective countries.

Cash dividends and appropriations to the legal reserve charged to retained earnings for the years ended December 31, 2012, 2011 and 2010 represent dividends paid out during those years and the related appropriations to the legal reserve. Retained earnings at December 31, 2012 did not reflect current year-end dividends in the amount of ¥80,695 million ($927,529 thousand) which were approved by the stockholders in March 2013.

The amount available for dividends under the Corporation Law of Japan is based on the amount recorded in the Company's nonconsolidated books of account in accordance with generally accepted accounting standards of Japan. Such amount was ¥1,090,834 million ($12,538,322 thousand) at December 31, 2012.

Retained earnings at December 31, 2012 included Canon's equity in undistributed earnings of affiliated companies accounted for by the equity method in the amount of ¥17,094 million ($196,483 thousand).

15. OTHER COMPREHENSIVE INCOME (LOSS)

Changes in accumulated other comprehensive income (loss) are as follows:

Years ended December 31	*Millions of yen*			*Thousands of U.S. dollars*
	2012	2011	2010	**2012**
Foreign currency translation adjustments:				
Balance at beginning of year	**¥(378,863)**	¥(325,612)	¥(202,628)	**$(4,354,747)**
Adjustments for the year	**131,129**	(53,251)	(122,984)	**1,507,230**
Balance at end of year	**(247,734)**	(378,863)	(325,612)	**(2,847,517)**
Net unrealized gains and losses on securities:				
Balance at beginning of year	**1,003**	3,020	3,285	**11,529**
Adjustments for the year	**3,143**	(2,017)	(265)	**36,126**
Balance at end of year	**4,146**	1,003	3,020	**47,655**
Net gains and losses on derivative instruments:				
Balance at beginning of year	**455**	917	71	**5,230**
Adjustments for the year	**(4,917)**	(462)	846	**(56,517)**
Balance at end of year	**(4,462)**	455	917	**(51,287)**
Pension liability adjustments:				
Balance at beginning of year	**(104,368)**	(68,784)	(61,546)	**(1,199,633)**
Adjustments for the year	**(14,831)**	(35,584)	(7,238)	**(170,471)**
Balance at end of year	**(119,199)**	(104,368)	(68,784)	**(1,370,104)**
Total accumulated other comprehensive income (loss):				
Balance at beginning of year	**(481,773)**	(390,459)	(260,818)	**(5,537,621)**
Adjustments for the year	**114,524**	(91,314)	(129,641)	**1,316,368**
Balance at end of year	**¥(367,249)**	¥(481,773)	¥(390,459)	**$(4,221,253)**

Tax effects allocated to each component of other comprehensive income (loss) and reclassification adjustments, including amounts attributable to noncontrolling interests, are as follows:

Years ended December 31	*Millions of yen*		
	Before-tax amount	*Tax (expense) or benefit*	*Net-of-tax amount*
2012:			
Foreign currency translation adjustments	**¥ 134,930**	**¥ (1,195)**	**¥ 133,735**
Net unrealized gains and losses on securities:			
Amount arising during the year	**3,418**	**(1,004)**	**2,414**
Reclassification adjustments for gains and losses realized in net income	**1,307**	**(456)**	**851**
Net change during the year	**4,725**	**(1,460)**	**3,265**
Net gains and losses on derivative instruments:			
Amount arising during the year	**(10,647)**	**4,041**	**(6,606)**
Reclassification adjustments for gains and losses realized in net income	**2,440**	**(714)**	**1,726**
Net change during the year	**(8,207)**	**3,327**	**(4,880)**
Pension liability adjustments:			
Amount arising during the year	**(13,888)**	**(1,738)**	**(15,626)**
Reclassification adjustments for gains and losses realized in net income	**4,433**	**(1,594)**	**2,839**
Net change during the year	**(9,455)**	**(3,332)**	**(12,787)**
Other comprehensive income (loss)	**¥ 121,993**	**¥ (2,660)**	**¥ 119,333**
2011:			
Foreign currency translation adjustments	¥ (53,839)	¥ (247)	¥ (54,086)
Net unrealized gains and losses on securities:			
Amount arising during the year	(7,571)	3,010	(4,561)
Reclassification adjustments for gains and losses realized in net income	4,077	(1,632)	2,445
Net change during the year	(3,494)	1,378	(2,116)
Net gains and losses on derivative instruments:			
Amount arising during the year	4,221	(1,708)	2,513
Reclassification adjustments for gains and losses realized in net income	(5,006)	2,044	(2,962)
Net change during the year	(785)	336	(449)
Pension liability adjustments:			
Amount arising during the year	(59,928)	20,252	(39,676)
Reclassification adjustments for gains and losses realized in net income	2,038	(739)	1,299
Net change during the year	(57,890)	19,513	(38,377)
Other comprehensive income (loss)	¥(116,008)	¥20,980	¥ (95,028)
2010:			
Foreign currency translation adjustments	¥(128,271)	¥ 1,353	¥(126,918)
Net unrealized gains and losses on securities:			
Amount arising during the year	(2,179)	671	(1,508)
Reclassification adjustments for gains and losses realized in net income	1,320	42	1,362
Net change during the year	(859)	713	(146)
Net gains and losses on derivative instruments:			
Amount arising during the year	8,409	(3,573)	4,836
Reclassification adjustments for gains and losses realized in net income	(6,990)	2,921	(4,069)
Net change during the year	1,419	(652)	767
Pension liability adjustments:			
Amount arising during the year	(19,170)	8,314	(10,856)
Reclassification adjustments for gains and losses realized in net income	2,323	(794)	1,529
Net change during the year	(16,847)	7,520	(9,327)
Other comprehensive income (loss)	¥(144,558)	¥ 8,934	¥(135,624)

Years ended December 31	*Thousands of U.S. dollars*		
	Before-tax amount	*Tax (expense) or benefit*	*Net-of-tax amount*
2012:			
Foreign currency translation adjustments	**$1,550,920**	**$(13,736)**	**$1,537,184**
Net unrealized gains and losses on securities:			
Amount arising during the year	**39,287**	**(11,540)**	**27,747**
Reclassification adjustments for gains and losses realized in net income	**15,023**	**(5,241)**	**9,782**
Net change during the year	**54,310**	**(16,781)**	**37,529**
Net gains and losses on derivative instruments:			
Amount arising during the year	**(122,379)**	**46,448**	**(75,931)**
Reclassification adjustments for gains and losses realized in net income	**28,046**	**(8,207)**	**19,839**
Net change during the year	**(94,333)**	**38,241**	**(56,092)**
Pension liability adjustments:			
Amount arising during the year	**(159,633)**	**(19,977)**	**(179,610)**
Reclassification adjustments for gains and losses realized in net income	**50,954**	**(18,322)**	**32,632**
Net change during the year	**(108,679)**	**(38,299)**	**(146,978)**
Other comprehensive income (loss)	**$1,402,218**	**$(30,575)**	**$1,371,643**

16. STOCK-BASED COMPENSATION

On May 1, 2011, based on the approval of the stockholders, the Company granted stock options to its directors, executive officers and certain employees to acquire 912,000 shares of common stock. These option awards vest after two years of continued service beginning on the grant date and have a four year contractual term. The grant-date fair value per share of the stock options granted during the year ended December 31, 2011 was ¥772.

On May 1, 2010, based on the approval of the stockholders, the Company granted stock options to its directors, executive officers and certain employees to acquire 890,000 shares of common stock. These option awards vest after two years of continued service beginning on the grant date and have a four year contractual term. The grant-date fair value per share of the stock options granted during the year ended December 31, 2010 was ¥988.

On May 1, 2009, based on the approval of the stockholders, the Company granted stock options to its directors, executive officers and certain employees to acquire 954,000 shares of common stock. These option awards vest after two years of continued service beginning on the grant date and have a four year contractual term. The grant-date fair value per share of the stock options granted during the year ended December 31, 2009 was ¥699.

On May 1, 2008, based on the approval of the stockholders, the Company granted stock options to its directors, executive officers and certain employees to acquire 592,000 shares of common stock. These option awards vest after two years of continued service beginning on the grant date and have a four year contractual term. The grant-date fair value per share of the stock options granted during the year ended December 31, 2008 was ¥1,247.

The compensation cost recognized for these stock options for the years ended December 31, 2012, 2011 and 2010 was ¥364 million ($4,184 thousand), ¥748 million and ¥643 million, respectively, and is included in selling, general and administrative expenses in the consolidated statements of income.

The fair value of each option award was estimated on the date of grant using the Black-Scholes option pricing model that incorporates the assumptions presented below:

Years ended December 31	2011	2010
Expected term of option (in years)	4.0	4.0
Expected volatility	36.44%	38.00%
Dividend yield	3.16%	2.53%
Risk-free interest rate	0.44%	0.45%

A summary of option activity under the stock option plans as of and for the years ended December 31, 2012, 2011 and 2010 is presented below:

	Shares	Weighted-average exercise price		Weighted-average remaining contractual term	Aggregate intrinsic value	
		Yen	U.S. dollars	Year	Millions of yen	Thousands of U.S. dollars
Outstanding at January 1, 2010	1,512,000	¥4,119		3.0	¥588	
Granted	890,000	4,573				
Forfeited	(182,000)	3,479				
Outstanding at December 31, 2010	2,220,000	4,354		2.5	722	
Granted	912,000	3,990				
Exercised	(65,800)	3,287				
Forfeited	(24,000)	4,282				
Outstanding at December 31, 2011	3,042,200	4,268		2.0	88	
Exercised	**(10,800)**	**3,287**	**$42.14**			
Forfeited	**(305,000)**	**4,493**	**54.90**			
Outstanding at December 31, 2012	**2,726,400**	**¥4,247**	**$54.72**	**1.6**	**¥ 37**	**$425**
Exercisable at December 31, 2012	**1,988,400**	**¥4,342**	**$54.58**	**1.1**	**¥ 37**	**$425**

At December 31, 2012, all outstanding option awards were vested or expected to be vested.

A summary of the status of the Company's nonvested shares at December 31, 2012, and changes during the year ended December 31, 2012, is presented below:

Year ended December 31, 2012	Shares	Weighted-average grant-date fair value	
		Yen	U.S. dollars
Nonvested at January 1, 2012	**1,768,000**	**¥878**	**$10.09**
Vested	**(848,000)**	**988**	**11.36**
Forfeited	**(182,000)**	**796**	**9.15**
Nonvested at December 31, 2012	**738,000**	**772**	**8.87**

At December 31, 2012, there was ¥95 million ($1,092 thousand) of total unrecognized compensation cost related to nonvested stock options. That cost is expected to be recognized over a period of 0.33 year. The total fair value of shares vested during the years ended December 31, 2012, 2011 and 2010 was ¥848 million ($9,747 thousand), ¥547 million and ¥696 million, respectively. Cash received from the exercise of stock options for the year ended December 31, 2012 and 2011 was ¥35 million ($402 thousand) and ¥216 million, respectively.

17. NET INCOME ATTRIBUTABLE TO CANON INC. STOCKHOLDERS PER SHARE

A reconciliation of the numerators and denominators of basic and diluted net income attributable to Canon Inc. stockholders per share computations is as follows:

Years ended December 31	*Millions of yen*			*Thousands of U.S. dollars*
	2012	2011	2010	**2012**
Net income attributable to Canon Inc.	**¥224,564**	¥248,630	¥246,603	**$2,581,195**
	Number of shares			
Average common shares outstanding	**1,173,647,835**	1,215,832,419	1,234,817,434	
Effect of dilutive securities:				
Stock options	**20,574**	60,552	50,603	
Diluted common shares outstanding	**1,173,668,409**	1,215,892,971	1,234,868,037	
	Yen			*U.S. dollars*
Net income attributable to Canon Inc. stockholders per share:				
Basic	**¥191.34**	¥204.49	¥199.71	**$2.20**
Diluted	**191.34**	204.48	199.70	**2.20**

The computation of diluted net income attributable to Canon Inc. stockholders per share for the years ended December 31, 2012, 2011 and 2010 excludes certain outstanding stock options because the effect would be anti-dilutive.

18. DERIVATIVES AND HEDGING ACTIVITIES

Risk management policy

Canon operates internationally, exposing it to the risk of changes in foreign currency exchange rates. Derivative financial instruments are comprised principally of foreign exchange contracts utilized by the Company and certain of its subsidiaries to reduce the risk. Canon assesses foreign currency exchange rate risk by continually monitoring changes in the exposures and by evaluating hedging opportunities. Canon does not hold or issue derivative financial instruments for trading purposes. Canon is also exposed to credit-related losses in the event of non-performance by counterparties to derivative financial instruments, but it is not expected that any counterparties will fail to meet their obligations. Most of the counterparties are internationally recognized financial institutions and selected by Canon taking into account their financial condition, and contracts are diversified across a number of major financial institutions.

Foreign currency exchange rate risk management

Canon's international operations expose Canon to the risk of changes in foreign currency exchange rates. Canon uses foreign exchange contracts to manage certain foreign currency exchange exposures principally from the exchange of U.S. dollars and euros into Japanese yen. These contracts are primarily used to hedge the foreign currency exposure of forecasted intercompany sales and intercompany trade receivables that are denominated in foreign currencies. In accordance with Canon's policy, a specific portion of foreign currency exposure resulting from forecasted intercompany sales are hedged using foreign exchange contracts which principally mature within three months.

Cash flow hedge

Changes in the fair value of derivative financial instruments designated as cash flow hedges, including foreign exchange contracts associated with forecasted intercompany sales, are reported in accumulated other comprehensive income (loss). These amounts are subsequently reclassified into earnings through other income (deductions) in the same period as the hedged items affect earnings. Substantially all amounts recorded in accumulated other comprehensive income (loss) at year-end are expected to be recognized in earnings over the next twelve months. Canon excludes the time value component from the assessment of hedge effectiveness. Changes in the fair value of a foreign exchange contract for the period between the date that the forecasted intercompany sales occur and its maturity date are recognized in earnings and not considered hedge ineffectiveness.

Derivatives not designated as hedges

Canon has entered into certain foreign exchange contracts to primarily offset the earnings impact related to fluctuations in foreign currency exchange rates associated with certain assets denominated in foreign currencies. Although these foreign exchange contracts have not been designated as hedges as required in order to apply hedge accounting, the contracts are effective from an economic perspective. The changes in the fair value of these contracts are recorded in earnings immediately.

Contract amounts of foreign exchange contracts at December 31, 2012 and 2011 are set forth below:

December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
To sell foreign currencies	**¥420,272**	¥391,455	**$4,830,713**
To buy foreign currencies	**66,563**	75,016	**765,092**

Fair value of derivative instruments in the consolidated balance sheets

The following tables present Canon's derivative instruments measured at gross fair value as reflected in the consolidated balance sheets at December 31, 2012 and 2011.

Derivatives designated as hedging instruments

December 31		*Fair value*		
		Millions of yen		*Thousands of U.S. dollars*
	Balance sheet location	**2012**	2011	**2012**
Assets:				
Foreign exchange contracts	Prepaid expenses and other current assets	**¥ 443**	¥1,325	**$ 5,092**
Liabilities:				
Foreign exchange contracts	Other current liabilities	**4,472**	1,270	**51,402**

Derivatives not designated as hedging instruments

December 31		*Fair value*		
		Millions of yen		*Thousands of U.S. dollars*
	Balance sheet location	**2012**	2011	**2012**
Assets:				
Foreign exchange contracts	Prepaid expenses and other current assets	**¥ 388**	¥3,393	**$ 4,460**
Liabilities:				
Foreign exchange contracts	Other current liabilities	**21,021**	1,340	**241,621**

Effect of derivative instruments in the consolidated statements of income

The following tables present the effect of Canon's derivative instruments in the consolidated statements of income for the years ended December 31, 2012, 2011 and 2010.

Derivatives in cash flow hedging relationships

Years ended December 31	*Gain (loss) recognized in OCI (effective portion)*	*Gain (loss) reclassified from accumulated OCI into income (effective portion)*		*Gain (loss) recognized in income (ineffective portion and amount excluded from effectiveness testing)*	
Millions of yen	*Amount*	*Location*	*Amount*	*Location*	*Amount*
2012: Foreign exchange contracts	**¥(8,207)**	Other, net	**¥(2,440)**	Other, net	**¥(221)**
2011: Foreign exchange contracts	(785)	Other, net	5,006	Other, net	(457)
2010: Foreign exchange contracts	1,419	Other, net	6,990	Other, net	(302)
Thousands of U.S. dollars					
2012: Foreign exchange contracts	**$(94,333)**	Other, net	**$(28,046)**	Other, net	**$(2,540)**

Derivatives not designated as hedging instruments

Years ended December 31		*Gain (loss) recognized in income on derivative*			
		Millions of yen			*Thousands of U.S. dollars*
	Location	**2012**	2011	2010	**2012**
Foreign exchange contracts	Other, net	**¥(30,602)**	¥11,168	¥50,794	**$(351,747)**

19. COMMITMENTS AND CONTINGENT LIABILITIES

Commitments

At December 31, 2012, commitments outstanding for the purchase of property, plant and equipment approximated ¥39,520 million ($454,253 thousand), and commitments outstanding for the purchase of parts and raw materials approximated ¥65,311 million ($750,701 thousand).

Canon occupies sales offices and other facilities under lease arrangements accounted for as operating leases. Deposits made under such arrangements aggregated ¥13,313 million ($153,023 thousand) and ¥14,171 million at December 31, 2012 and 2011, respectively, and are included in noncurrent receivables in the accompanying consolidated balance sheets. Rental expenses under such operating lease arrangements amounted to ¥40,273 million ($462,908 thousand), ¥38,167 million and ¥40,396 million for the years ended December 31, 2012, 2011 and 2010, respectively.

Future minimum lease payments required under noncancelable operating leases that have initial or remaining lease terms in excess of one year at December 31, 2012 are as follows:

Year ending December 31:	*Millions of yen*	*Thousands of U.S. dollars*
2013	¥25,101	$288,517
2014	16,512	189,793
2015	11,296	129,839
2016	7,529	86,540
2017	5,623	64,632
Thereafter	9,746	112,024
Total future minimum lease payments	¥75,807	$871,345

Guarantees

Canon provides guarantees for bank loans of its employees, affiliates and other companies. The guarantees for the employees are principally made for their housing loans. The guarantees of loans of its affiliates and other companies are made to ensure that those companies operate with less financial risk.

For each guarantee provided, Canon would have to perform under a guarantee if the borrower defaults on a payment within the contract periods of 1 year to 30 years, in the case of employees with housing loans, and of 1 year to 10 years, in the case of affiliates and other companies. The maximum amount of undiscounted payments Canon would have had to make in the event of default is ¥13,333 million ($153,253 thousand) at December 31, 2012. The carrying amounts of the liabilities recognized for Canon's obligations as a guarantor under those guarantees at December 31, 2012 were not significant.

Canon also issues contractual product warranties under which it generally guarantees the performance of products delivered and services rendered for a certain period or term.

Changes in accrued product warranty cost for the years ended December 31, 2012 and 2011 are summarized as follows:

Years ended December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Balance at beginning of year	**¥11,691**	¥13,343	**$134,379**
Addition	**13,553**	14,296	**155,782**
Utilization	**(12,503)**	(14,649)	**(143,713)**
Other	**(578)**	(1,299)	**(6,643)**
Balance at end of year	**¥12,163**	¥11,691	**$139,805**

Legal proceedings

Canon is involved in various claims and legal actions arising in the ordinary course of business. Canon has recorded provisions for liabilities when it is probable that liabilities have been incurred and the amount of loss can be reasonably estimated. Canon reviews these provisions at least quarterly and adjusts these provisions to reflect the impact of the negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case. Based on its experience, although litigation is inherently unpredictable, Canon believes that any damage amounts claimed in outstanding matters are not a meaningful indicator of Canon's potential liability. In the opinion of management, any reasonably possible range of losses from outstanding matters would not have a material adverse effect on Canon's consolidated financial position, results of operations, or cash flows.

20. DISCLOSURES ABOUT THE FAIR VALUE OF FINANCIAL INSTRUMENTS AND CONCENTRATIONS OF CREDIT RISK

Fair value of financial instruments

The estimated fair values of Canon's financial instruments at December 31, 2012 and 2011 are set forth below. The following summary excludes cash and cash equivalents, trade receivables, finance receivables, noncurrent receivables, short-term loans, trade payables and accrued expenses for which fair values approximate their carrying amounts. The summary also excludes investments which are disclosed in Note 3.

December 31	*Millions of yen*				*Thousands of U.S. dollars*	
	2012		2011		**2012**	
	Carrying amount	*Estimated fair value*	*Carrying amount*	*Estimated fair value*	*Carrying amount*	*Estimated fair value*
Long-term debt, including current installments	**¥ (3,664)**	**¥ (3,654)**	¥(7,070)	¥(7,053)	**$ (42,115)**	**$ (42,000)**
Foreign exchange contracts:						
Assets	**831**	**831**	4,718	4,718	**9,552**	**9,552**
Liabilities	**(25,493)**	**(25,493)**	(2,610)	(2,610)	**(293,023)**	**(293,023)**

The following methods and assumptions are used to estimate the fair value in the above table.

Long-term debt

Canon's long-term debt instruments are classified as Level 2 instruments and valued based on the present value of future cash flows associated with each instrument discounted using current market borrowing rates for similar debt instruments of comparable maturity. The levels are more fully described in Note 21.

Foreign exchange contracts

The fair values of foreign exchange contracts are measured based on the market price obtained from financial institutions.

Limitations of fair value estimates

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instruments. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Concentrations of credit risk

At December 31, 2012 and 2011, one customer accounted for approximately 18% and 17% of consolidated trade receivables, respectively. Although Canon does not expect that the customer will fail to meet its obligations, Canon is potentially exposed to concentrations of credit risk if the customer failed to perform according to the terms of the contracts.

21. FAIR VALUE MEASUREMENTS

Fair value is the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. A three-level fair value hierarchy that prioritizes the inputs used to measure fair value is as follows:

Level 1— Inputs are quoted prices in active markets for identical assets or liabilities.

Level 2— Inputs are quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable, and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3— Inputs are derived from valuation techniques in which one or more significant inputs or value drivers are unobservable, which reflect the reporting entity's own assumptions about the assumptions that market participants would use in establishing a price.

Assets and liabilities measured at fair value on a recurring basis

The following tables present Canon's assets and liabilities that are measured at fair value on a recurring basis consistent with the fair value hierarchy at December 31, 2012 and 2011.

December 31 *Millions of yen*	*Level 1*	*Level 2*	*Level 3*	*Total*
2012: Assets:				
Cash and cash equivalents	**¥ —**	**¥141,729**	**¥ —**	**¥141,729**
Available-for-sale (current):				
Corporate bonds	**30**	**—**	**—**	**30**
Available-for-sale (noncurrent):				
Government bonds	**181**	**—**	**—**	**181**
Corporate bonds	**—**	**116**	**444**	**560**
Fund trusts	**159**	**1,075**	**—**	**1,234**
Equity securities	**21,335**	**—**	**—**	**21,335**
Derivatives	**—**	**831**	**—**	**831**
Total assets	**¥21,705**	**¥143,751**	**¥444**	**¥165,900**
Liabilities:				
Derivatives	**¥ —**	**¥ 25,493**	**¥ —**	**¥ 25,493**
Total liabilities	**¥ —**	**¥ 25,493**	**¥ —**	**¥ 25,493**

Millions of yen	*Level 1*	*Level 2*	*Level 3*	*Total*
2011: Assets:				
Cash and cash equivalents	¥ —	¥204,307	¥ —	¥204,307
Available-for-sale (current):				
Corporate bonds	20	—	—	20
Available-for-sale (noncurrent):				
Government bonds	150	—	—	150
Corporate bonds	—	104	454	558
Fund trusts	151	1,675	—	1,826
Equity securities	17,724	—	—	17,724
Derivatives	—	4,718	—	4,718
Total assets	¥18,045	¥210,804	¥454	¥229,303
Liabilities:				
Derivatives	¥ —	¥ 2,610	¥ —	¥ 2,610
Total liabilities	¥ —	¥ 2,610	¥ —	¥ 2,610

December 31 *Thousands of U.S. dollars*		*Level 1*	*Level 2*	*Level 3*	*Total*
2012:	Assets:				
	Cash and cash equivalents	**$ —**	**$1,629,069**	**$ —**	**$1,629,069**
	Available-for-sale (current):				
	Corporate bonds	**345**	**—**	**—**	**345**
	Available-for-sale (noncurrent):				
	Government bonds	**2,080**	**—**	**—**	**2,080**
	Corporate bonds	**—**	**1,334**	**5,103**	**6,437**
	Fund trusts	**1,828**	**12,356**	**—**	**14,184**
	Equity securities	**245,230**	**—**	**—**	**245,230**
	Derivatives	**—**	**9,552**	**—**	**9,552**
	Total assets	**$249,483**	**$1,652,311**	**$5,103**	**$1,906,897**
	Liabilities:				
	Derivatives	**$ —**	**$ 293,023**	**$ —**	**$ 293,023**
	Total liabilities	**$ —**	**$ 293,023**	**$ —**	**$ 293,023**

Level 1 investments are comprised principally of Japanese equity securities, which are valued using an unadjusted quoted market price in active markets with sufficient volume and frequency of transactions. Level 2 cash and cash equivalents are valued based on market approach, using quoted prices for identical assets in markets that are not active. Level 3 investments are mainly comprised of corporate bonds, which are valued based on cost approach, using unobservable inputs as the market for the assets was not active at the measurement date.

Derivative financial instruments are comprised of foreign exchange contracts. Level 2 derivatives are valued using quotes obtained from counterparties or third parties, which are periodically validated by pricing models using observable market inputs, such as foreign currency exchange rates and interest rates, based on market approach.

The following table presents the changes in Level 3 assets measured on a recurring basis, consisting primarily of corporate bonds, for the years ended December 31, 2012 and 2011.

Years ended December 31	*Millions of yen*		*Thousands of U.S. dollars*
	2012	2011	**2012**
Balance at beginning of year	**¥454**	¥ 1,950	**$5,218**
Total gains or losses (realized or unrealized):			
Included in earnings	**3**	(2)	**34**
Included in other comprehensive income (loss)	**2**	(12)	**23**
Purchases, issuances, and settlements	**(15)**	(1,482)	**(172)**
Balance at end of year	**¥444**	¥ 454	**$5,103**

Gains and losses included in earnings are mainly related to corporate bonds still held at December 31, 2012 and 2011, and are reported in “Other, net” in the consolidated statements of income.

Assets and liabilities measured at fair value on a nonrecurring basis

During the year ended December 31, 2012, there were no circumstances that required any significant assets or liabilities to be measured at fair value on a nonrecurring basis.

During the year ended December 31, 2011, equity securities accounted for by the equity method with a carrying amount of ¥3,577 million were written down to their fair value of zero, resulting in an other-than-temporary impairment charge of ¥3,577 million, which was included in earnings. Equity securities accounted for by the equity method were classified as Level 3 instruments and valued based on an income approach using unobservable inputs such as projected income of the investment.

22. SUPPLEMENTAL CASH FLOW INFORMATION

During the year ended December 31, 2010, the Company executed three separate share exchanges under which the Company made its three listed subsidiaries, Canon Finetech Inc., Canon Machinery Inc. and Tokki Corporation, its wholly owned subsidiaries. The Company issued no new shares, as it issued 10,000,853 shares of treasury stock for these transactions in total.

As a result of the share exchanges, the carrying amount of the Company's noncontrolling interest in Canon Finetech Inc., Canon Machinery Inc. and Tokki Corporation was decreased from ¥38,644 million to zero.

23. SEGMENT INFORMATION

Canon operates its business in three segments: the Office Business Unit, the Imaging System Business Unit, and the Industry and Others Business Unit, which are based on the organizational structure and information reviewed by Canon's management to evaluate results and allocate resources.

The primary products included in each segment are as follows:

Office Business Unit:
Office MFDs / Office copying machines/ Personal-use copying machines / Laser MFDs / Laser printers / Digital production printing systems / High speed continuous feed printers / Wide-format printers / Document solution

Imaging System Business Unit*:
Interchangeable-lens digital cameras / Compact digital cameras / Digital camcorders / Digital cinema cameras / Interchangeable lenses / Inkjet printers / Large-format inkjet printers / Commercial photo printers / Image scanners / Broadcast equipment / Calculators

Industry and Others Business Unit:
Semiconductor lithography equipment / FPD lithography equipment / Digital radiography systems / Ophthalmic equipment / Vacuum thin-film deposition equipment / Organic LED panel manufacturing equipment / Micromotors / Computers / Handy terminals / Document scanners

* The "Consumer Business Unit" has been renamed the "Imaging System Business Unit" to be more consistent with its strategy to expand the business. This change in segment description has no impact on any financial information of this segment.

The accounting policies of the segments are substantially the same as those described in the significant accounting policies in Note 1. Canon evaluates performance of, and allocates resources to, each segment based on operating profit.

Information about operating results and assets for each segment as of and for the years ended December 31, 2012, 2011 and 2010 is as follows:

Millions of yen	*Office*	*Imaging System*	*Industry and Others*	*Corporate and eliminations*	*Consolidated*
2012: Net sales:					
External customers	**¥1,751,960**	**¥1,404,394**	**¥323,434**	**¥ —**	**¥3,479,788**
Intersegment	**5,615**	**1,577**	**84,406**	**(91,598)**	**—**
Total	**1,757,575**	**1,405,971**	**407,840**	**(91,598)**	**3,479,788**
Operating cost and expenses	**1,553,997**	**1,195,653**	**401,930**	**4,352**	**3,155,932**
Operating profit	**¥ 203,578**	**¥ 210,318**	**¥ 5,910**	**¥ (95,950)**	**¥ 323,856**
Total assets	**¥ 828,222**	**¥ 614,328**	**¥337,899**	**¥2,175,054**	**¥3,955,503**
Depreciation and amortization	**77,660**	**53,664**	**34,264**	**92,545**	**258,133**
Capital expenditures	**58,402**	**58,142**	**44,086**	**146,031**	**306,661**
2011: Net sales:					
External customers	¥1,912,112	¥1,311,023	¥334,298	¥ —	¥3,557,433
Intersegment	5,831	1,021	86,565	(93,417)	—
Total	1,917,943	1,312,044	420,863	(93,417)	3,557,433
Operating cost and expenses	1,658,678	1,100,750	396,563	23,371	3,179,362
Operating profit (loss)	¥ 259,265	¥ 211,294	¥ 24,300	¥ (116,788)	¥ 378,071
Total assets	¥ 821,782	¥ 452,809	¥362,638	¥2,293,498	¥3,930,727
Depreciation and amortization	93,196	45,609	29,685	92,853	261,343
Capital expenditures	53,888	48,192	37,648	122,753	262,481
2010: Net sales:					
External customers	¥1,978,945	¥1,389,622	¥338,334	¥ —	¥3,706,901
Intersegment	8,324	1,705	94,624	(104,653)	—
Total	1,987,269	1,391,327	432,958	(104,653)	3,706,901
Operating cost and expenses	1,693,947	1,153,262	442,789	29,351	3,319,349
Operating profit (loss)	¥ 293,322	¥ 238,065	¥ (9,831)	¥ (134,004)	¥ 387,552
Total assets	¥ 855,893	¥ 414,022	¥307,029	¥2,406,876	¥3,983,820
Depreciation and amortization	103,548	41,665	37,387	93,593	276,193
Capital expenditures	53,115	36,266	27,105	77,061	193,547

Thousands of U.S. dollars	*Office*	*Imaging System*	*Industry and Others*	*Corporate and eliminations*	*Consolidated*
2012: Net sales:					
External customers	**$20,137,471**	**$16,142,460**	**$3,717,632**	**$ —**	**$39,997,563**
Intersegment	**64,540**	**18,126**	**970,184**	**(1,052,850)**	**—**
Total	**20,202,011**	**16,160,586**	**4,687,816**	**(1,052,850)**	**39,997,563**
Operating cost and expenses	**17,862,034**	**13,743,138**	**4,619,885**	**50,023**	**36,275,080**
Operating profit	**$ 2,339,977**	**$ 2,417,448**	**$ 67,931**	**$ (1,102,873)**	**$ 3,722,483**
Total assets	**$ 9,519,793**	**$ 7,061,241**	**$3,883,897**	**$25,000,621**	**$45,465,552**
Depreciation and amortization	**892,644**	**616,828**	**393,839**	**1,063,735**	**2,967,046**
Capital expenditures	**671,287**	**668,299**	**506,736**	**1,678,517**	**3,524,839**

Intersegment sales are recorded at the same prices used in transactions with third parties. Expenses not directly associated with specific segments are allocated based on the most reasonable measures applicable. Corporate expenses include certain corporate research and development expenses. Segment assets are based on those directly associated with each segment. Corporate assets primarily consist of cash and cash equivalents, finance receivables, investments, deferred tax assets, goodwill and corporate properties. Capital expenditures represent the additions to property, plant and equipment and intangible assets measured on an accrual basis.

Information by major geographic area as of and for the years ended December 31, 2012, 2011 and 2010 is as follows:

	Millions of yen			*Thousands of U.S. dollars*
	2012	2011	2010	**2012**
Net sales:				
Japan	**¥ 720,286**	¥ 694,450	¥ 695,749	**$ 8,279,149**
Americas	**939,873**	961,955	1,023,299	**10,803,138**
Europe	**1,014,038**	1,113,065	1,172,474	**11,655,609**
Asia and Oceania	**805,591**	787,963	815,379	**9,259,667**
Total	**¥3,479,788**	¥3,557,433	¥3,706,901	**$39,997,563**
Long-lived assets:				
Japan	**¥1,032,598**	¥1,070,412	¥1,104,949	**$11,868,943**
Americas	**112,163**	85,824	69,034	**1,289,230**
Europe	**91,904**	83,296	108,160	**1,056,368**
Asia and Oceania	**159,435**	89,334	72,846	**1,832,586**
Total	**¥1,396,100**	¥1,328,866	¥1,354,989	**$16,047,127**

Net sales are attributed to areas based on the location where the product is shipped to the customers. Other than in Japan and the United States, Canon does not conduct business in any individual country in which its sales in that country exceed 10% of consolidated net sales. Net sales in the United States are ¥763,870 million ($8,780,115 thousand), ¥779,652 million and ¥836,645 million for the years ended December 31, 2012, 2011 and 2010, respectively.

Long-lived assets represent property, plant and equipment and intangible assets for each geographic area.

The following information is based on the location of the Company and its subsidiaries as of and for the years ended December 31, 2012, 2011 and 2010. In addition to the disclosure requirements under U.S. GAAP, Canon discloses this information in order to provide financial statements users with useful information.

Millions of yen	*Japan*	*Americas*	*Europe*	*Asia and Oceania*	*Corporate and eliminations*	*Consolidated*
2012: Net sales:						
External customers	**¥ 834,406**	**¥ 932,987**	**¥ 1,010,922**	**¥ 701,473**	**¥ —**	**¥ 3,479,788**
Intersegment	**1,829,834**	**23,767**	**5,650**	**781,836**	**(2,641,087)**	**—**
Total	**2,664,240**	**956,754**	**1,016,572**	**1,483,309**	**(2,641,087)**	**3,479,788**
Operating cost and expenses	**2,336,536**	**937,111**	**972,585**	**1,437,527**	**(2,527,827)**	**3,155,932**
Operating profit	**¥ 327,704**	**¥ 19,643**	**¥ 43,987**	**¥ 45,782**	**¥ (113,260)**	**¥ 323,856**
Total assets	**¥ 1,206,702**	**¥ 339,918**	**¥ 457,592**	**¥ 548,583**	**¥ 1,402,708**	**¥ 3,955,503**
2011: Net sales:						
External customers	¥ 807,883	¥ 952,833	¥1,109,256	¥ 687,461	¥ —	¥3,557,433
Intersegment	1,873,157	16,217	4,681	744,179	(2,638,234)	—
Total	2,681,040	969,050	1,113,937	1,431,640	(2,638,234)	3,557,433
Operating cost and expenses	2,273,336	948,593	1,069,489	1,388,580	(2,500,636)	3,179,362
Operating profit	¥ 407,704	¥ 20,457	¥ 44,448	¥ 43,060	¥ (137,598)	¥ 378,071
Total assets	¥1,236,468	¥ 250,131	¥ 427,030	¥ 442,263	¥ 1,574,835	¥3,930,727
2010: Net sales:						
External customers	¥ 854,208	¥1,008,200	¥1,163,452	¥ 681,041	¥ —	¥3,706,901
Intersegment	1,974,591	7,975	3,489	723,423	(2,709,478)	—
Total	2,828,799	1,016,175	1,166,941	1,404,464	(2,709,478)	3,706,901
Operating cost and expenses	2,398,439	993,310	1,126,521	1,357,663	(2,556,584)	3,319,349
Operating profit	¥ 430,360	¥ 22,865	¥ 40,420	¥ 46,801	¥ (152,894)	¥ 387,552
Total assets	¥1,321,572	¥ 251,587	¥ 472,785	¥ 421,250	¥ 1,516,626	¥3,983,820

Thousands of U.S. dollars	*Japan*	*Americas*	*Europe*	*Asia and Oceania*	*Corporate and eliminations*	*Consolidated*
2012: Net sales:						
External customers	**$ 9,590,874**	**$10,723,989**	**$11,619,793**	**$ 8,062,907**	**$ —**	**$39,997,563**
Intersegment	**21,032,574**	**273,183**	**64,943**	**8,986,622**	**(30,357,322)**	**—**
Total	**30,623,448**	**10,997,172**	**11,684,736**	**17,049,529**	**(30,357,322)**	**39,997,563**
Operating cost and expenses	**26,856,735**	**10,771,390**	**11,179,138**	**16,523,299**	**(29,055,482)**	**36,275,080**
Operating profit	**$ 3,766,713**	**$ 225,782**	**$ 505,598**	**$ 526,230**	**$ (1,301,840)**	**$ 3,722,483**
Total assets	**$13,870,138**	**$ 3,907,103**	**$ 5,259,678**	**$ 6,305,552**	**$16,123,081**	**$45,465,552**

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Canon is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) promulgated under the Securities Exchange Act of 1934, as amended, as a process designed by, or under the supervision of, the company's principal executive and principal financial officers and effected by the company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Canon's management assessed the effectiveness of internal control over financial reporting as of December 31, 2012. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework (the "COSO criteria").

Based on its assessment, management concluded that, as of December 31, 2012, Canon's internal control over financial reporting was effective based on the COSO criteria.

Canon's independent registered public accounting firm, Ernst & Young ShinNihon LLC, has issued an audit report on the effectiveness of Canon's internal control over financial reporting.

Fujio Mitarai
Chairman & CEO

Toshizo Tanaka
Executive Vice President & CFO

March 28, 2013

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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2-2-3 Uchisaiwai-cho
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The Board of Directors and Stockholders of
Canon Inc.

We have audited the accompanying consolidated balance sheets of Canon Inc. and subsidiaries as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2012, all expressed in Japanese yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Canon Inc. and subsidiaries at December 31, 2012 and 2011, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2012, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Canon Inc. and subsidiaries' internal control over financial reporting as of December 31, 2012, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 28, 2013 expressed an unqualified opinion thereon.

We have also recomputed the translation of the consolidated financial statements as of and for the year ended December 31, 2012 into United States dollars. In our opinion, the consolidated financial statements expressed in Japanese yen have been translated into United States dollars on the basis described in Note 2.

Ernst & Young ShinNihon LLC

March 28, 2013

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

ERNST & YOUNG

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Tel: +81 3 3503 1191
Fax: +81 3 3503 1277

The Board of Directors and Stockholders of
Canon Inc.

We have audited Canon Inc. and subsidiaries' internal control over financial reporting as of December 31, 2012, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Canon Inc. and subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Canon Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Canon Inc. and subsidiaries as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2012, all expressed in Japanese yen, and our report dated March 28, 2013 expressed an unqualified opinion thereon.

Ernst & Young ShinNihon LLC

March 28, 2013

TRANSFER AND REGISTRAR'S OFFICE

Canon Inc.

30-2, Shimomaruko 3-chome, Ohta-ku, Tokyo 146-8501, Japan

Manager of the Register of Stockholders

Mizuho Trust & Banking Co., Ltd.
2-1, Yaesu 1-chome, Chuo-ku, Tokyo 103-8670, Japan

Depositary and Agent with Respect to American Depositary Receipts for Common Shares

JPMorgan Chase Bank, N.A.
1 Chase Manhattan Plaza, Floor 58, New York, N.Y. 10005-1401, U.S.A.

STOCKHOLDER INFORMATION

Stock Exchange Listings:

Tokyo, Osaka, Nagoya, Fukuoka, Sapporo and New York stock exchanges

American Depositary Receipts are traded on the New York Stock Exchange (CAJ).

Ordinary General Meeting of Shareholders:

March 28, 2013, in Tokyo

Further Information:

For publications or information, please contact the Public Affairs Headquarters, Canon Inc., Tokyo, or access Canon's Website at
www.canon.com

MAJOR CONSOLIDATED SUBSIDIARIES

(As of December 31, 2012)

Manufacturing

Canon Precision Inc.
Fukushima Canon Inc.
Canon Chemicals Inc.
Canon Components, Inc.
Canon Electronics Inc.
Canon Finetech Inc.
Nisca Corporation
Canon Tokki Corporation
Canon ANELVA Corporation
Nagahama Canon Inc.
Canon Machinery Inc.
Oita Canon Materials Inc.
Oita Canon Inc.
Nagasaki Canon Inc.
Canon Virginia, Inc.
Canon Bretagne S.A.S.
Océ-Technologies B.V.
OPTOPOL Technology S.A.
Canon Dalian Business Machines, Inc.
Canon (Suzhou) Inc.
Canon Zhongshan Business Machines Co., Ltd.
Canon Zhuhai, Inc.
Canon Inc., Taiwan
Canon Vietnam Co., Ltd.
Canon Hi-Tech (Thailand) Ltd.
Canon Opto (Malaysia) Sdn. Bhd.

Research & Development

Canon Research Centre France S.A.S.
Canon Information Systems Research Australia Pty. Ltd.

Marketing & Other

Canon Marketing Japan Inc.
Canon System and Support Inc.
Canon Software Inc.
Canon IT Solutions Inc.
Canon U.S.A., Inc.
Canon Canada Inc.
Canon Business Solutions, Inc.
Canon Latin America, Inc.
Canon Europa N.V.
Canon Europe Ltd.
Canon Ru LLC
Canon (UK) Ltd.
Canon Deutschland GmbH
Canon (Schweiz) AG
Canon Nederland N.V.
Canon France S.A.S.
Canon Middle East FZ-LLC
Canon (China) Co., Ltd.
Canon Hongkong Co., Ltd.
Canon Singapore Pte. Ltd.
Canon Australia Pty. Ltd.

* Canon Business Solutions, Inc. changed its name to "Canon Solutions America, Inc." effective January 1, 2013.

CANON INC. 30-2, Shimomaruko 3-chome, Ohta-ku, Tokyo 146-8501, Japan

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