CANON ANNUAL REPORT 2021

Fiscal Year Ended December 31, 2021

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Cover Photo:

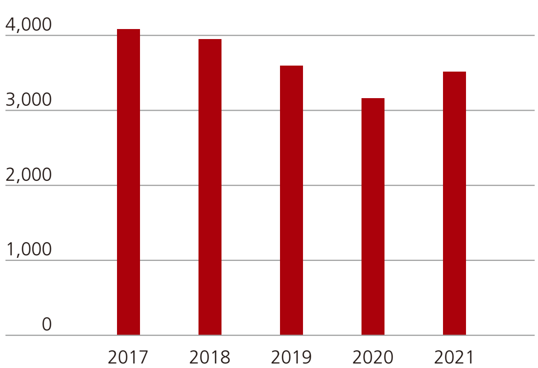
Fujita Health University Hospital —which boasts the largest number of hospital beds in Japan —currently uses Canon's computed tomography ("CT") systems equipped with the Precise IQ Engine (PIQE) so that high-definition cardiac testing can be carried out with the latest AI-driven image reconstruction technology.

FINANCIAL HIGHLIGHTS

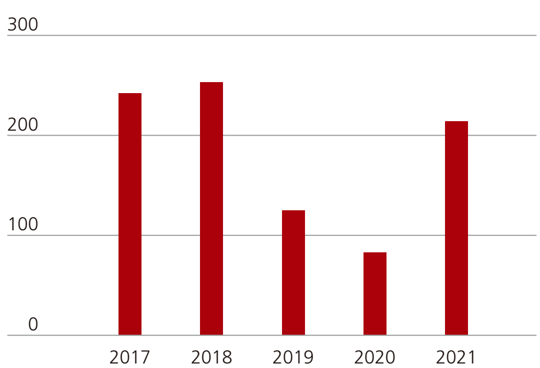
	Millions of yen (except per share amounts)			Thousands of U.S. dollars (except per share amounts)
	2021	2020	**Change (%)**	**2021**
Net sales	**¥ 3,513,357**	¥ 3,160,243	**+11.2**	**$ 30,550,930**
Operating profit	**281,918**	110,547	**+155.0**	**2,451,461**
Income before income taxes	**302,706**	130,280	**+132.4**	**2,632,226**
Net income attributable to Canon Inc.	**214,718**	83,318	**+157.7**	**1,867,113**
Net income attributable to Canon Inc. shareholders per share:				
—Basic	**¥ 205.35**	¥ 79.37	**+158.7**	**$ 1.79**
—Diluted	**205.29**	79.35	**+158.7**	**1.79**
Total assets	**¥ 4,750,888**	¥ 4,625,614	**+2.7**	**$ 41,312,070**
Canon Inc. shareholders' equity	**¥ 2,873,773**	¥ 2,575,031	**+11.6**	**$ 24,989,330**

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 JPY115=U.S.$1, the approximate exchange rate on the Tokyo Foreign Exchange Market as of December 30, 2021, solely for the convenience of the reader.

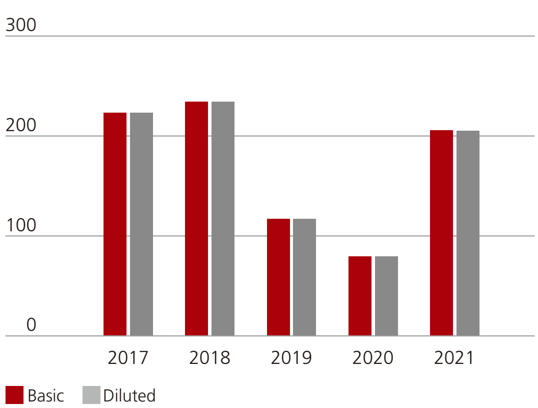
Net Sales (Billions of yen)



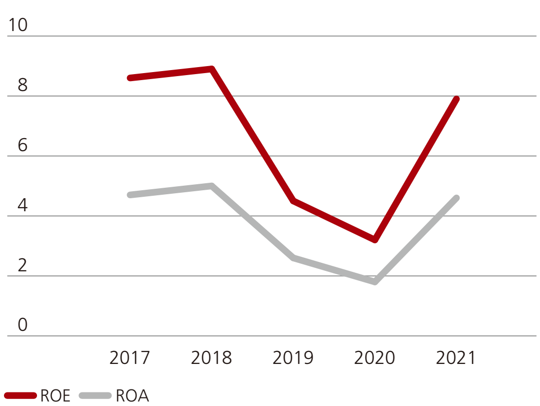
Net Income Attributable to Canon Inc. (Billions of yen)



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



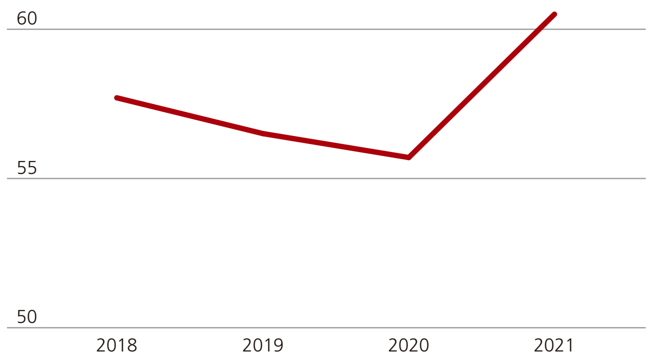
ROE/ROA (%)



Canon will further promote a grand strategic transformation by accelerating reform activities.

FUJIO MITARAI
Chairman & CEO
Canon Inc.

Canon Inc. shareholders' equity ratio (%)



Performance in 2021

Following on from 2020, the COVID-19 pandemic continued to affect many aspects of our lives in 2021. Even though the pandemic necessitated numerous restrictions, we began to see economic activity pick up again as the vaccination rollout gained traction and the world adjusted to the reality of having to coexist with the virus. However, in the second half of the term, demand grew sharply on the back of the resumption of economic activity. This resulted in disrupted distribution networks mainly due to semiconductor and labor shortages, and it even precipitated an inflationary economy on a global scale by driving up the prices of energy resources and commodities.

In this environment, Canon launched a new five-year management plan, Phase VI of the "Excellent Global Corporation Plan," to enhance competitiveness through company-wide organizational realignment and to improve group-wide productivity through extensive reinforcement of Canon's global headquarter functions under the basic policy of "accelerating our corporate portfolio transformation by improving productivity and creating new businesses."

With office occupancy rates recovering, we saw signs of a recovery in sales of office multifunction devices (MFDs), while sales of inkjet and laser printers increased thanks to the implementation of remote work and home studying. Sales of commercial printers rose, thanks to their capacity to produce high-quality images whilst boosting productivity. Sales of full-frame mirrorless cameras were strong partly thanks to a recovery in the digital interchangeable-lens digital camera market. Sales of network cameras were also buoyed by the resumption of investments in public facilities and the like after grinding to a halt during the COVID-19 pandemic, while sales of video management systems and video content analytics software were also solid thanks to heightened demand for mainly remote monitoring systems. Stronger demand for medical equipment during the pandemic underpinned firm sales, primarily for CT systems and diagnostic ultrasound systems. In addition, production of semiconductor manufacturing equipment continued at maximum capacity due to aggressive investment in equipment by chip makers to meet growing demand and address supply shortages. Furthermore, sales of flat panel display (FPD) lithography equipment were strong, reflecting solid demand for televisions, laptop computers, and other devices.

As a result, consolidated net sales for this term increased by 11.2% year on year to 3,513.4 billion yen, consolidated income before income taxes increased by 132.4% year on year to 302.7 billion yen, and consolidated net income attributable to Canon Inc. increased by 157.7% year on year to 214.7 billion yen.

Phase I
1996–2000

Canon transformed its mindset to focus more on total (not partial) optimization and profitability (not sales) and also engaged in thorough cash flow management. We introduced various business innovations, including the selection and consolidation of business areas, and reform activities in such areas as production and development.

Phase II
2001–2005

Aiming to become No. 1 in all major business areas, Canon focused on strengthening its competitiveness by stepping up efforts to digitalize its products in line with the changing times. We also reformed how we undertake procurement activities mainly by setting up a new Procurement Headquarters, and we took steps to reform in-house systems, such as our personnel system, with the aim of balancing lifetime employment with merit-based principles.

Phase III
2006–2010

Canon pushed ahead with new growth strategies, including the enhancement of existing businesses and expansion of new business areas, and also implemented supply chain management and IT reforms in order to achieve real-time management that can readily adapt to changes.

Phase IV
2011–2015

Canon revised its management policy from a strategy targeting expansion of scale to a strategy aimed at strengthening its financial structure. While actively pursuing M&As, we pushed ahead with the rebuilding of our business foundation to serve as a new driver of future growth with a view to making a foray into industries that can become new growth engines in step with changes in the times.

Phase V
2016–2020

Canon endeavored to reconsolidate its traditional core businesses, which include cameras and office equipment, and completed the first stage of its grand strategic transformation by working to expand and strengthen the following four new businesses that underpin Canon’s future: commercial printing, network cameras, medical, and industrial equipment.

Excellent Global Corporation Plan

Phase I to Phase V (1996–2020)

Canon launched the Excellent Global Corporation Plan in 1996, and has since strengthened its management base through each of the plan’s five-year stages, from Phase I through Phase V.

During Phase I, we stressed thorough cash flow management and significantly boosted productivity through the introduction of our cell production system, along with other measures. In Phase II, we stepped up efforts to digitalize our copying machines and camera offerings, endeavored to strengthen the competitiveness of our products, and established a strong earnings structure. In Phase III, we rode the globalization and digitization wave to drive sales and profit higher. In 2007, we achieved record-high sales of 4,481.3 billion yen and recorded net profit of 488.3 billion yen. Also during that period, we turned our attention to OLED displays and welcomed Canon Tokki (formerly Tokki) and Netherlands-based printer manufacturer Canon Production Printing (formerly Océ) into the Canon Group.

During Phase IV, we promoted diversification via the lateral expansion of our existing businesses into such new businesses as the Cinema EOS System, while also accelerating our M&A strategy in pursuit of new growth. In this manner, we set out a clear direction for shifting our focus for growth from B2C to B2B. At that time, we turned Milestone Systems (“Milestone”) and Axis Communications (“Axis”) into subsidiaries in order to reinforce and expand our rapidly growing network camera business. Additionally, Canon Nanotechnologies (formerly Molecular Imprints) became a subsidiary, and we furthered the development of next-generation semiconductor manufacturing equipment that uses nanoimprint lithography, a technology that enables miniaturization and cost reductions for semiconductor devices.

In Phase V, we welcomed Canon Medical Systems Corporation (“Canon Medical”; formerly Toshiba Medical Systems) into the Canon Group to complete our current business setup in line with the basic policy of “embracing the challenge of new growth through a grand strategic transformation.” As a manufacturer, we strove unceasingly to achieve production reforms and thorough cost reductions. At the same time, we accomplished the grand transformation of our business portfolio by establishing new growth platforms in commercial printing, network cameras, medical equipment, and industrial equipment.

Phase VI basic policy and key strategies

Building on our achievements thus far, in Phase VI, which commenced in 2021, we aim to surpass our record-high sales figure achieved in 2007 with at least 4,500 billion yen in sales in 2025, the final year of Phase VI. We plan to achieve this by "thoroughly enhancing competitiveness through company-wide realignment into a new industry-oriented business group structure" and "improving group-wide productivity through extensive reinforcement of Canon's global headquarter functions." These efforts will be guided by our basic policy of "accelerating our corporate portfolio transformation by improving productivity and creating new businesses." We are also targeting an operating profit ratio of at least 12%, a net profit ratio of 8% or higher, and a shareholder equity ratio of 60% or greater.

Strategy 1

Thoroughly enhancing competitiveness through company-wide realignment into a new industry-oriented business group structure

In April 2021, with the objective of fully maximizing our wide array of businesses and technologies, we reorganized our business divisions into the following four groups according to their affinity with each other: printing, imaging, medical, and industrial. People-to-people exchange within these groups has already led to synergies, and going forward, we will make every effort to reinforce organizations by reviewing technological capabilities and business domains from the perspective of each group. Also, we will aim to accelerate the pace of R&D to create and quickly expand new businesses more efficiently by aggressively and boldly pursuing M&A deals and realizing synergies with Canon's existing businesses.

In addition, to coincide with the business shift to the B2B domain, we intend to restructure the roles and positioning of business headquarters and sales companies and focus on developing a first-rate sales engineer team that accurately reflects the needs of customers in product development. Meanwhile, the frontier business will be upgraded to a business headquarters (the Frontier Business Promotion Headquarters) so it can accelerate the commercialization of solutions mainly for the materials business, production technology, and component sales to outside businesses.

Strategy 1

PRINTING GROUP

The continuous-feed press ProStream 1000 series

The Printing Group mainly consists of multifunction devices, inkjet printers, laser printers, and commercial and industrial printers. The primary objective for this group—the largest of all the industry-oriented business groups—is to cement a dominant position in new fields, including commercial and industrial printing, and expand sales. By combining Canon's printing technology with the exceptional productivity and stability techniques hitherto honed by Canon Production Printing, we will look to further deepen collaboration and expand into new commercial and industrial printing domains. In commercial printing, we will provide products that deliver even greater image quality and a high level of productivity, whilst also targeting steady growth, mainly by improving workflow and strengthening the added value of printed material. In industrial printing, armed with printheads that leverage our in-house developed technology, we will strive to expand our business in such fields as printing of labels and other packagings.

With the digital transformation (DX) of society gaining considerable momentum among corporations, we will work on improving our lineup of multifunction devices in the office equipment business. At the same time, because a hybrid working style that combines office-based work with remote work has now become well entrenched at companies, we will expand our range of products and services that can offer a printing environment free from the constraints of physical working location, whether it be at home or in the office. In this field in particular, we intend to reinforce our development of hardware and software with the aim of providing cloud-based digital services and find an optimal balance between lineup expansion and cost reductions with the use of platform-based product development.

Strategy 1

IMAGING GROUP

The EOS R5 full-frame mirrorless camera

The Imaging Group comprises cameras and lenses, broadcast equipment, professional video cameras, network cameras, automotive cameras, and similar products.

In this group, the first goal is to seize the number one spot in the global interchangeable-lens camera market. As the world's leading camera manufacturer, we aim to achieve this objective by expanding our lineup of camera models and lenses.

The second goal is to establish a solid position in network cameras, for which industrial and societal demand is growing rapidly. With demand rising in manufacturing and marketing fields—for such applications as process management at production sites or the retail customer analyses—we will support the development activities of Axis, further deepen collaboration with Group companies that develop software, and reinforce our suite of total solutions, including video management and video analytics, that only Canon is capable of delivering.

The third goal is to develop new businesses in such areas as XR (VR/AR/MR), remote camera systems, and free viewpoint video. Finally, the fourth objective of this group is to strengthen the key component business in new fields of imaging. In particular, in the dynamically evolving mobility market, in anticipation of a future age of unmanned vehicles, we will push ahead with strategic development in such businesses as vehicle on-board camera and transportation infrastructure based on Canon's optical and network technologies.

MEDICAL GROUP

Canon's CT System

The most important objective of the Medical Group is to capture the biggest share of the global CT market. Through an acquisition completed in September 2021, we welcomed Canada-based Redlen Technologies into the Canon Group. This company boasts world-leading technology in semiconductor detector modules, a key device in next-generation CT systems. By collaborating with Redlen Technologies, we can now greatly accelerate the development of Photon Counting CT technology (PCCT), which is expected to be the next-generation CT technology. We are also bolstering our product competitiveness in the areas of MRI and diagnostic ultrasound systems by ensuring high-quality images and lowering costs. Also, in the field of healthcare IT, we expect to see growth in demand for AI-driven solutions such as radiology interpretation and diagnostic support for future personalized medical services. These are the kind of opportunities we intend to pursue in order to achieve steady growth.

Boosting sales overseas is another priority. We will focus primarily on the U.S. market and seek to expand our share in other overseas markets by hastening the expansion of sales bases and sales personnel.

INDUSTRIAL GROUP

Flat Panel Display (FPD) lithography equipment

The Industrial Group handles semiconductor and flat panel display (FPD) lithography systems, Canon Tokki's OLED panel manufacturing systems, Canon Anelva's sputtering equipment, Canon Machinery's die bonders, and similar product lines. In this group we will endeavor to scale up and augment business operations by combining the group's collective strengths to meet the massive demand for semiconductors and display panels.

In the area of semiconductor lithography systems, we will aim to maintain the dominant position of our i-line systems and capitalize upon favorable market conditions to expand our market share of KrF systems. We are also taking up the challenge of expanding the use of our nanoimprint lithography technology. Moreover, in terms of economic security in developed countries and regions, there is a tendency for chips to be produced domestically or within the region. In light of this we intend to focus our efforts on expanding sales of semiconductor lithography equipment not only in Asia, but also in Western markets.

As for display panel manufacturing equipment, we will strive to further increase our market share by offering increasingly higher resolution in LCDs and improving manufacturing productivity. For the production of OLEDs we are working to reduce the costs associated with the current deposition technique and we are also accelerating the development of equipment for new techniques and the in-house production of materials. For sputtering equipment and die bonders, the industrial group will work together to leverage its distinctive technology and expand business operations.

FRONTIER BUSINESS

The Frontier Business Promotion Headquarters, which was upgraded to a business headquarters in 2021, draws upon the wealth of technologies Canon has cultivated thus far to explore commercial potential in the three fields of life sciences, materials, and solutions. Going forward, it will work closely with Canon HQ's R&D department and each business headquarters to engage in a process of selection and concentration to clearly identify the areas targeted for commercialization and someday establish our fifth and even the sixth industry-oriented business groups.

Complex ceramic lattice structure in hollow shapes

Strategy 2

Improving group-wide productivity through extensive reinforcement of Canon's global headquarter functions

Another key strategy of Phase VI will be the extensive reinforcement of Canon's global headquarter functions in order to achieve a total optimization across the aforementioned industry-oriented business groups. There are four points of focus in this strategy.

The first is "thorough cash flow management." As we needed to borrow funds to facilitate the grand transformation of our business portfolio through M&As, we plan on repaying these debts in full during the period of Phase VI so as to prepare for the next major investment or economic crisis. We will also aim to rectify the flow of capital within the Group and obtain a high credit rating of AA or Aa1.

The second focus point is "establishing a more dynamic and merit-based HR management system." We will improve the link between performance and salary while switching to a system that better reflects the abilities of employees. At the same time, we intend to strengthen HR development and encourage career transitions within the Company in line with the transformation of our business portfolio. We will also push ahead with the nurturing of a digital-savvy workforce and the utilization of IT tools as we endeavor to boost productivity amid the digital transformation (DX).

The third point is "promoting cost reduction initiatives across the whole Group." We will aim to lower the cost-of-sales ratio by 50% through the seamless automation of design, production engineering, and manufacturing floor processes, as well as the in-house production of manufacturing equipment. On top of this, we will build a resilient supply network for minimizing the impacts of unexpected events on production, procurement, and distribution.

The fourth point is "focusing on innovations that advance new product development and responding to the rapidly changing business environment." This involves the anticipation of exit points three to five years from now and furthering the development of technologies and devices that will be indispensable in the future. And on a company-wide level, we will take steps to tackle various issues pertaining to decarbonization, the adoption of renewable energy, and changes in world affairs.

In conclusion

Given that COVID-19 vaccinations continue to be administered worldwide and the development and use of therapeutic drugs has also begun, we expect economic activity to gradually normalize and the balance of supply and demand for semiconductors and other components and products to stabilize. This will likely drive a full-fledged recovery in employment, income, and consumption. Amid this environment, the Canon Group is pushing ahead with the Group-wide business portfolio transformation, as we believe that change is progress and transformation is advancement. The world has been shaken to the core by the COVID-19 pandemic, forcing people to reassess their values and lifestyles, but Canon will stay a step ahead of changes in society and keep reinventing itself as an excellent company not only in terms of scale, but also quality. We look forward to your continued support and understanding.

Fujio Mitarai
Chairman & CEO
Canon Inc.

BUSINESS STRATEGY

Tapping demand from a hybrid working style and targeting growth in the digital commercial printing field

The varioPRINT iX series of high-speed cut-sheet inkjet printers combines image quality and productivity at a high level.

The imageRUNNER ADVANCE DX series of office MFDs by connecting to cloud services is contributing to improved productivity.

Canon's inkjet printers that are suited for remote work and learning from home.

In commercial and industrial printing and other new fields, we will aim to cement a dominant position in the market by enhancing the competitiveness of our products. We will also push ahead with the development of products and services to capture new lifestyle and work-style demand from offices and prosumers, strengthen our DX-capable products and services, and find a balance between product line expansions and cost reductions.

2021 Performance

In the office equipment business, we endeavored to find a balance between development efficiency enhancements and production cost reductions and launched a new product that was favorably received, the imageRUNNER ADVANCE DX C5800 series, which offers enhanced essential features, such as low power consumption and quiet operation. Sales of consumables are also recovering as the ratio of people who have gone back to the office gradually returns to normal.

In the prosumer business, sales of both inkjet and laser printers, as well as consumables, were strong following the launch of new products designed for teleworking and home learning.

In the production business, we boosted our competitiveness with the launch of a new high-speed imagePRESS printer and through the launch of new accessories that can automatically inspect and adjust images. In the large-format printer category, we launched the TZ series, our fastest imagePROGRAF printers to date. We also expanded our imagePROGRAF lineup with the introduction of the new GP series, the industry's first model equipped with fluorescent ink to enhance poster printing. And, in addition to the ColorStream and ProStream series, which are the mainstream products of continuous feed presses, thanks to exceptional image quality and level of productivity, sales of the varioPRINT iX series of high-speed cut-sheet inkjet printers were boosted by favorable market assessment since going on sale in 2020. Moreover, we successfully expanded the number of dealers selling the new Colorado 1630 large-format printer for graphic arts printing as it supports a wide range of media.

Toward further growth

In this era of digital transformation (DX), the shift towards paperless offices—in the sense of decreasing printing volume—will continue to gather momentum in the coming future, but we still anticipate firm demand for printing in terms of sharing thoughts and work results. A hybrid working style that combines office-based work with teleworking has gained traction among companies due to the spread of COVID-19 infections, which means we must now provide printing environments and services that are impervious to the constraints of physical working location by, for example, taking advantage of the cloud. Canon will draw upon its strengths—namely, the two digital printing technologies of electrophotography and inkjet, as well as a worldwide sales and service network—to focus on providing solutions attuned to the era of DX and aim to be the global leader in the office and prosumer market categories. Additionally, in the commercial printing field, which includes the printing of books, catalogues and direct mailings, as well as in the industrial printing field, which includes the printing of labels and other packaging, we expect the shift from analogue to digital to progress even further, which is why we will look to establish a solid position in the market by successively launching new competitive products that conserve energy and add greater value.

Maintain the world's No.1 brand by securing absolute market share and establish solid position in network cameras

Canon's high-resolution network cameras watch over the safety of elementary school to university students at Seikei Gakuen. (Tokyo, Japan)

The EOS R5 features a more advanced function to detect subjects through deep-learning technology.

Canon's volumetric video technology can produce videos from any viewpoint and angle.

In interchangeable-lens cameras, we aim to secure sustainable profit, maintaining the world's No.1 brand by securing absolute market share. In the network camera field, we aim to establish a solid position in the market by capturing a broad spectrum of demand. We will also cultivate new businesses in the field of 3D imaging application such as free viewpoint video and XR fields including virtual reality.

2021 Performance

The digital camera market overall held firm buoyed by solid demand for high-quality image expression. Sales of the EOS R5 and EOS R6 that were released in 2020 remained brisk and sales of RF lenses —the lineup of which has now been expanded to 26—also grew significantly thanks to synergies with EOS R series camera bodies. Moreover, we launched a new virtual reality (VR) imaging production system (EOS VR SYSTEM) with a view to expanding into new business fields. We also offered new ways of enjoying image content; for example, we launched a new product in the MREAL series of mixed reality (MR) head-mount displays (HMDs), as well as a new camera that captures images automatically.

In addition, sales of not only network cameras, but also video management software and video content analytics software applications were strong, reflecting heightened demand for, among others, production site automation and remote monitoring systems during the COVID-19 pandemic.

In the business for video production, which includes broadcast equipment, we launched a remote camera system that allows users to control multiple cameras over a network. We also worked on strengthening and expanding into new fields such as capturing actual images at the Volumetric Video Studio – Kawasaki, a studio leveraging our Free Viewpoint Video System technology.

Toward further growth

Demand for high-quality visual expression remains firm largely as a result of more people using their extra free time to enjoy taking pictures at home and sharing them online. We will look to further bolster our offerings of EOS R system cameras and RF-series interchangeable lenses and gain a bigger market share by launching products in a timely manner that give users more options. Furthermore, in broadcasting and video production fields, we will strengthen our lineup of high-image-quality remote camera systems. We also intend to leverage the technologies of the imaging group, such as optical technology and image processing technology, in order to help drive growth in image capturing, from still images and movies to VR videos.

In the network camera area, we will enhance our presence in the security field with the combined strengths across Group companies: Axis, a network camera leader with partners all over the world; Milestone, a leading video management software company; BriefCam, a video content analytics software company; and Arcules, a cloud services company. We also intend to go beyond the conventional objectives of security and deploy products and services that can handle various operations; for example, inspecting finished products at production sites or detecting congestion levels in stores or exhibition halls.

In autonomous driving and other mobility fields in which innovative changes are progressing at a blistering pace, we will look to contribute to the proliferation of mobility services, such as driver assistance systems, by leveraging our long-honed expertise in optical and network technologies to enter the automotive camera as well as the transportation infrastructure business.

Aiming to scale up business operations by strengthening product competitiveness and sales structures

Canon's MRI scanners offer high-image quality and other high-performance features in a compact and more energy efficient design.

Canon's diagnostic ultrasound systems provide high-definition images that are clear with little noise.

Canon Medical has introduced antigen qualitative test kit for COVID-19, which is used at Yokohama City University Hospital.

In order to respond to the growing sophistication of medical treatment, we aim to contribute to healthcare around the world by expanding our business field to healthcare IT and in-vitro diagnostics, with diagnostic imaging at its core.

We will strengthen the competitiveness of our CT, MRI, and diagnostic ultrasound systems and gain the largest share of the global CT market. We will also bolster our sales structure in overseas markets, particularly in priority areas like the United States.

2021 Performance

In the Japanese market in 2021, sales of mainly CT systems and diagnostic ultrasound systems for COVID-19 testing were strong partly thanks to the government providing support for medical institutions. In the US, where we have continued to strengthen our sales structure, orders and sales grew as we expanded business operations whilst flexibly contending with the negative impacts of the pandemic. We have been also engaged in joint research with the National Cancer Center Japan with a view to commercial viability at the earliest possible time for Photon Counting CT (PCCT), which is increasingly touted as the next-generation of CT technology. In September 2021 through an M&A deal we welcomed Canada-based Redlen Technologies into the Canon Group. This company possesses world-leading technology to develop and manufacture semiconductor detector modules that are used as the key device for PCCT.

Toward further growth

In the diagnostic imaging business, having brought Redlen Technologies into the Canon Group in 2021, we can now push forward with the technological development and early practical application of PCCT, a technology with the potential to deliver unprecedented diagnostic functionality and greatly reduce radiation exposure. And to complement our proprietary technologies, such as RF coil technology (the fundamental technology in MRI), we will look to develop next-generation high performance MRI with the use of AI-driven image processing technology. As for our diagnostic ultrasound systems, we will take steps to reduce costs with the use of Canon's production engineering by realizing the in-house production and standardization of platforms. Also, by strengthening our sales network mainly in the US, we will aim to secure the leading global market share in CT and establish ourselves as one of the world's leading manufacturers of diagnostic imaging equipment.

In the field of healthcare IT, we will aim to provide high-quality diagnostic support and efficient medical care by integrating image and non-image data collected from clinical settings and using AI and other types of technology to analyze and process those data before offering them to medical institutions worldwide. Moreover, in the field of in-vitro diagnostics, we will work on expanding our portfolio and business into the field of peripheral testing systems, such as test reagents for COVID-19.

In the medical component business, not only will we grow the existing business mainly by gaining new customers and consolidating sales functions, but with a view to M&A-driven growth, we will also look to provide solutions to B2B customers on multiple levels, including end products, modules, processes, and services. By doing so, we will aim to further expand this business, whose sales account for more than 10% of the entire Medical Systems and Components Operations.

INDUSTRIAL AND OTHERS GROUP

Meeting robust demand for semiconductors and flat panel displays in a bid to expand market share

Canon's semiconductor lithography equipment used in the production of memory and image sensors.

Production of OLED panel manufacturing equipment with overwhelming competitiveness at Canon Tokki.

Mass production verification of nanoimprint manufacturing equipment is underway at Kioxia's Yokkaichi plant. (Japan)

For semiconductor lithography equipment and flat panel display (FPD) lithography equipment, we will develop and provide functions and performance, such as throughput and overlay accuracy, in a timely manner so as to contribute to productivity improvements for customers. We will also leverage IoT, AI, and other digital technologies to deliver services and support with a high level of customer satisfaction. In addition, for Canon Tokki's OLED panel manufacturing equipment, we will endeavor to enhance the function and performance of equipment that use the current deposition technique and will also accelerate the development of new manufacturing processes and materials.

2021 Performance

Despite the impact of COVID-19 casting a shadow over the timing of a long-term economic recovery, as well as concerns about how semiconductor shortages and mounting US-China trade friction might affect investments, there was only a slight impact from these factors and capital investment demand from mainly memory and logic chip manufacturers for semiconductor lithography equipment remained firm in all sectors. Demand for FPD lithography equipment was also solid thanks to the ongoing installation of equipment that had been pushed out to 2021 from 2020 due to COVID-19 travel restrictions, as well as the increased demand for devices such as TVs, laptop computers, and tablets owing to stay-at-home demand. Also, the adoption of OLED displays for mainly mobile devices continued, driving solid demand for Canon Tokki's vacuum deposition equipment.

Toward further growth

Owing to the proliferation of the 5G telecommunications network standard and cloud computing, demand for ICs, memory devices, and other types of semiconductors is expected to expand going forward. We also anticipate solid demand for LCD and OLED panels driven mainly by online video streaming, home learning, and increasingly higher image resolution. Considering that we continue to produce our semiconductor lithography equipment, FPD lithography equipment, and OLED panel manufacturing equipment at nearly full capacity, swiftly meeting increased demand in the near term will prove challenging. This is why we will look to harness the collective strength of the Industrial Group and augment our production system.

Over the medium-to-long term, we will work to enhance our product capabilities and increase our market share by adding functions and improving performance in order to contribute to customer productivity.

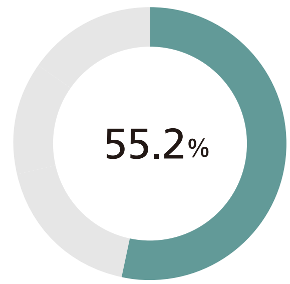
As for nanoimprint lithography, because the main capabilities of this technology have now reached mass production levels, we will aim to quickly achieve commercialization and step up the pace of efforts to expand the scope of application. We will also focus our resources on establishing production technology for next-generation OLED displays.

In addition to ultra-precision positioning and highly accurate fabrication in lithography equipment and vacuum deposition systems for deposition equipment, the industrial group possesses a whole host of core technologies, including Canon Anelva's sputtering technology essential to the production of hard disks and DRAMs, and Canon Machinery's thin die handling technology used to attach semiconductor chips to a substrate. By fusing together the group's core technologies to create products and services that deliver new value to customers we aim to expand our business sphere as well as establish a strong earnings base.

AT A GLANCE

PRINTING GROUP

Composition of Sales (%)



Office multifunction devices (MFDs)

Laser multifunction printers (MFPs)

Digital sheet-fed presses (Electrophotographic)

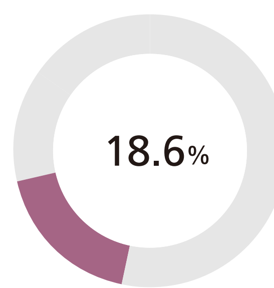
Large format printers (Inkjet)

Main Products

- Office multifunction devices (MFDs)
- Document solutions
- Laser multifunction printers (MFPs)
- Laser printers
- Inkjet printers
- Image scanners
- Calculators
- Digital continuous feed presses
- Digital sheet-fed presses
- Large format printers

IMAGING GROUP

Composition of Sales (%)



Interchangeable-lens digital cameras
—Mirrorless cameras

Interchangeable-lens digital cameras
—Digital SLR cameras

Interchangeable lenses

Network cameras

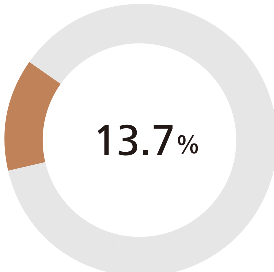
Main Products

- Interchangeable-lens digital cameras
- Interchangeable lenses
- Digital compact cameras
- Compact photo printers
- Network cameras
- Video management software
- Video content analytics software
- Digital camcorders
- Digital cinema cameras
- Broadcast equipment
- Multimedia projectors

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

MEDICAL GROUP

Composition of Sales (%)



Main Products

- Computed tomography (CT) systems
- Diagnostic ultrasound systems
- Diagnostic X-ray systems
- Magnetic resonance imaging (MRI) systems
- Clinical chemistry analyzers
- Digital radiography systems
- Ophthalmic equipment

Computed tomography (CT) systems

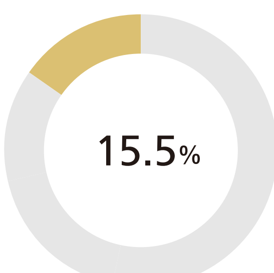
Diagnostic X-ray systems

Diagnostic ultrasound systems

Digital radiography systems

INDUSTRIAL AND OTHERS GROUP

Composition of Sales (%)



Main Products

- Semiconductor lithography equipment
- FPD (Flat panel display) lithography equipment
- OLED Display Manufacturing Equipment
- Vacuum thin-film deposition equipment
- Die bonders
- Handy terminals
- Document scanners

Semiconductor lithography equipment

FPD (Flat panel display) lithography equipment

Organic LED (OLED) panel manufacturing equipment

Die bonders

Development of SPAD image sensor that is expected to be used in a wide range of fields such as self-driving vehicles and medical care.

Canon is perpetually strengthening R&D as a company possessing a corporate DNA that places high importance on technology to differentiate itself from competitors.

R&D Expenses and Patents

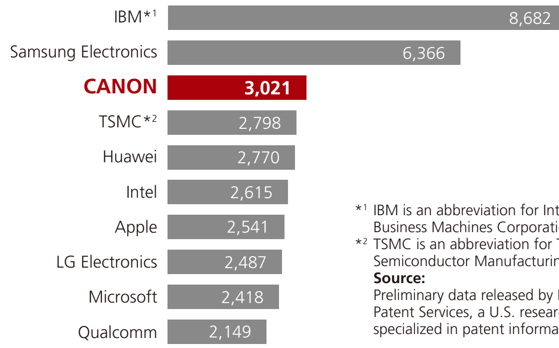
From the time of Canon's founding, we have continued to diversify our business operations by practicing a style of core competency management that combines fundamental technologies and core competency technologies in a variety of ways.

On a global scale, technology is in the midst of significant change and a so-called paradigm shift is occurring in R&D whereby companies are adding innovation-focused R&D for solving social issues to their existing invention-focused R&D portfolios. Canon's invention-focused R&D revolves around industry-academia collaboration and open innovation, while in the innovation-focused R&D space, to complement the modification of our proprietary technologies, we are accelerating our efforts to generate innovation to accurately meet societal needs through alliances with other companies, M&A deals, and other endeavors.

In 2021, R&D expenses amounted to ¥287.3 billion, and the ratio of R&D expenses to net sales was 8.2%. This focus on R&D activities has also cemented Canon's leading position in the

Highly accurate facial recognition with Canon's proprietary facial recognition engine and large-sized database of facial images.

2021 Top Ten U.S. Patent Holders by Company



*1 IBM is an abbreviation for International Business Machines Corporation.
*2 TSMC is an abbreviation for Taiwan Semiconductor Manufacturing Co Ltd.
Source:
Preliminary data released by IFI CLAIMS Patent Services, a U.S. research company specialized in patent information

intellectual property field. Canon was granted 3,021 patents in the United States in 2021, ranking it third among all companies. At the same time that we have maintained first place among Japanese companies for the 17th consecutive year.

Initiatives to Establish New Businesses

Guided by a long-term perspective, Canon is focused on discovering new technologies for the future.

Development of the world's first 3.2-megapixel SPAD image sensor

Owing to Canon's proprietary pixel architecture that efficiently captures and greatly multiplies faint particles of light, we have successfully developed an ultra-small SPAD sensor capable of capturing the world's highest*1 resolution of 3.2-megapixel color images—a higher resolution than Full HD (approximately 2.07 megapixels), even in low-light environments. The newly developed SPAD sensor greatly enhances sensitivity, including light on the near-infrared spectrum, and is capable of capturing color video at a resolution of 3.2 megapixels under low-light conditions of 0.002 lux*2, which is darker than a starless night sky. In addition, the SPAD sensor is capable of extremely high information processing speeds on the level of 100 picoseconds (one trillionth of a second). By taking advantage of its high sensitivity and rapid response functionality, the SPAD sensor has the potential to be utilized in a wide range of applications, including self-driving vehicles, medical diagnostic imaging devices, and scientific precision measuring instruments.

*1 Among SPAD sensors. As of December 14, 2021. Based on Canon research.
*2 Light from stars estimated at 0.02 lux. Ambient light in starless night environment estimated at 0.007 lux.

Improving the technology of facial recognition systems

Powered by Canon's proprietary facial recognition engine, we have successfully developed a highly accurate facial recognition technology. It combines a large database of various facial images with Canon's deep learning AI design techniques making it possible to recognize a person's face with a high degree of accuracy and speed even in network camera images captured from a top-down angle—which conventional technology has struggled to interpret—and also in blurry low-resolution images. In 2021 we demonstrated world-class accuracy in four categories for assessing the accuracy of a person retrieval in the Face Recognition Vendor Test (FRVT), a global evaluation benchmark organized by the National Institute of Standards and Technology (NIST) in the United States.

Detecting defects in infrastructure

In response to the progressive deterioration of public infrastructure around the world, Canon is developing solutions that use imaging to inspect the integrity of bridges, tunnels, and other concrete structures. With the use of deep-learning AI, cracks as fine as 0.2 mm in width, rebar exposures, water leaks, and other defects can be detected from high-resolution images, thus improving the efficiency and quality of inspection reports. Also, because hairline cracks will go unnoticed in images that are even slightly out of focus or blurry, in 2021 we announced the development of a tool for verifying the quality of inspection images. This tool automatically and rapidly judges whether an image is out of focus or blurry, and by extension, helps improve the quality of images taken at inspection sites.

Automatic production line for interchangeable lens (Utsunomiya Plant).

Canon is a corporation that has constantly pursued ultimate perfection in manufacturing. While striving to further improve production-engineering technology such as automation of assembly lines, we also focus on developing human resources armed with outstanding technical skills.

Globally Optimized Production

Canon employs a globally optimized production system through which we comprehensively determine the most rational locations to produce our products. This decision hinges on changes in social and economic circumstances and takes into account country or region-specific factors such as costs, tax systems, logistics, ease of procuring parts, and labor. In Japan we are endeavoring to reduce costs by establishing mother factories that integrate development, procurement, production, and manufacturing processes. Meanwhile, in emerging countries and regions we aim to boost productivity by further honing the skills of employees. Canon leverages regional


Product evaluation test at a plant. (Oita Canon)


Young engineers raise their techniques by participating in a competition.

characteristics and manufactures products utilizing an agile and flexible system that spans the globe.

Automation and In-house Production

Canon endeavors to create original products by actively pursuing the in-house production of not only CMOS sensors and other key devices and components, but also production equipment like automatic assembly machines and high-precision processing machines, as well as molding dies. To produce high-quality products at low cost, we aim to establish highly reliable automated production lines. We have rolled out fully automated production lines with zero human intervention for toner cartridges and we seek to do the same for the manufacturing of cameras in the future. In 2021 Canon Mold, which heads up the Group's mold manufacturing business, consolidated its six plants in Kasama City in Ibaraki Prefecture into a single location and is currently endeavoring to ramp up production capacity and enhance distribution efficiency.

Development of Human Resources

To further enhance its manufacturing capabilities, Canon is focused on nurturing its most skilled technicians, known as Master Craftsmen, and those who contribute to the advancement of manufacturing with their wide-ranging skills and knowledge of mainly assembly and component processing, known as Meisters. These technicians contribute to the improvement of Canon's production technology and play an active role at the front line of production by passing on the skills they have honed over the years to the next generation.

Initiatives for Environmentally Conscious Manufacturing and Enhanced Product Quality

Canon has worked to reduce energy consumption by undertaking a thorough-going review of operating conditions at production sites, for instance by cutting out excess use of pressurized air and cooling water and adjusting air conditioner settings. At the Kiyohara Industrial Park located in Utsunomiya City, Tochigi Prefecture, we launched a smart energy project (a multi-plant integrated energy-saving project) in partnership with Tokyo Gas Co., Ltd. and three other enterprises. By sharing electric power and heat (steam and hot water) between a number of business sites with differing levels of energy demand, we were able to realize major energy savings not possible at a single business site operating in isolation. This project was awarded the METI Minister's Award in the 2021 Energy Conservation Grand Prize hosted by the Energy Conservation Center, Japan.

In addition, guided by our mission to guarantee the high quality of our products, "no claims, no trouble," we have drawn up our own rules in the form of a quality management system that we adhere to exhaustively. This guarantees that our products are safe and provide satisfaction to our customers. Our unique quality standards not only comply with international quality management standards and relevant laws and regulations in each country or region, but they also take customer safety into account. Moreover, we endeavor to bring to market only the products that have satisfied our quality standards after putting them through a rigorous evaluation test at well-developed testing facilities and comprehensive checks in each manufacturing process.

The world premiere show "CP+2021" for cameras and photographic images as an online event.

Accelerating growth in commercial printing, network cameras, medical and industrial equipment as key drivers of Canon's next-generation business

Japan

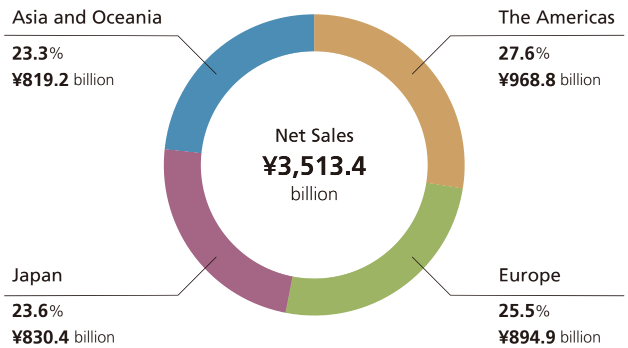
Sales in Japan amounted to ¥830.4 billion, or 23.6% of consolidated net sales.

Sales of mainstay business equipment such as office MFPs and laser printers declined due to the impact of product supply shortages caused primarily by a lack of semiconductors. On the other hand, sales increased for mid-range and high-end mirrorless cameras and RF mount interchangeable lenses, on which we have been concentrating our efforts. In addition, sales to major corporations in the System Integration (SI) services and data center businesses were boosted by active IT investment activity by corporations. Demand from SMEs to build teleworking environments remained strong and sales in the IT solutions business rose on the back of growth in security services and maintenance/operation services for IT equipment and the like.

In addition, we actively participated in webinars and online exhibitions, to promote the appeal of our products and

Canon Europe launched a virtual platform to help production print professionals.

Composition of Sales by Region



services.

The Americas

Sales in the Americas amounted to ¥968.8 billion, or 27.6% of consolidated net sales.

Canon U.S.A. handles marketing operations for North, Central, and South America. Its high-quality service framework for office equipment and commercial printers covering all U.S. states has been rated highly by customers. To meet growing demand for printing in hybrid working environments, Canon U.S.A. took steps to realign its organization and strengthen sales. It also expanded sales of mainly the EOS R5 and R6 cameras and sharply boosted sales of mainly the Cinema EOS System by capturing strong video streaming demand. Also, Canon's technological innovations mainly in its unique new businesses were widely promoted during CES 2021, the world's largest consumer electronics showcase event that was held online for the very first time.

Europe (Europe, Middle East, Africa)

Sales in Europe amounted to ¥ 894.9 billion, or 25.5% of consolidated net sales.

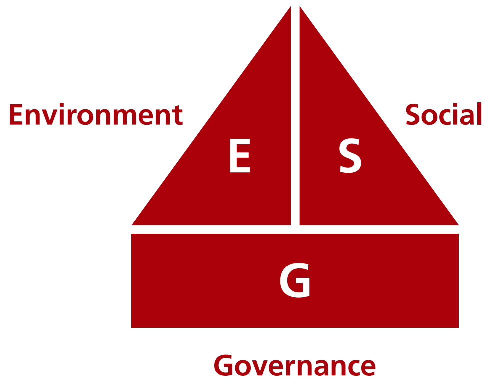
Canon Europe oversees business in the EMEA region - Europe, the Middle East and Africa. Operating in approximately 120 markets. In 2021, we launched a virtual platform to help production print professionals shape a positive business future, with practical advice, demonstrations and the latest market insights. We also continued to support partners and customers through virtual events.

Canon Europe is the official printing and imaging provider of Expo 2020 Dubai, which provides an exciting opportunity to demonstrate innovative technologies, products and services.

Asia and Oceania

Sales in Asia and Oceania region amounted to ¥819.2 billion, or 23.3% of consolidated net sales.

In order to swiftly and accurately respond to the characteristics and changes of the rapidly expanding Chinese market, in 2021 we split the Canon Asia Marketing Group (hitherto responsible for the entire Asian region) into two organizations: Canon China and Canon Asia Marketing. This has enabled us to engage in more market-oriented business activities than in the past. We announced a commemorative copy machine model ahead of the 25th anniversary of Canon China's founding which we will celebrate in 2022. Through such activities we hope to express our appreciation to our customers and continue to undertake sales activities whilst shortening the distance to market based on the slogan "Closer to Customer."



Environment:

Canon's Approach

In order to leave a rich earth for the next generation, Canon works together with its stakeholders to implement initiatives that help reduce environmental burdens with a focus on the entire product lifecycle.

Key Initiatives

- Contributing to a Carbon-Free Future
- Contributing to a Circular Economy
- Eliminating Hazardous Substances and Preventing Pollution
- Contributing to a Society in Harmony with Nature

Social:

Canon's Approach

As a good corporate citizen, Canon works to resolve social issues with technology and through business activities mainly by respecting human rights, ensuring responsible procurement as well as through sociocultural support activities.

Key Initiatives

- Respecting Human Rights
- Responsible Procurement in the Supply Chain
- Sociocultural Support Activities

Governance:

Canon's Approach

Canon maintains sound corporate governance as part of its efforts to maximize profits for shareholders and become a truly excellent global corporation.

Key Initiatives

- Board of Directors, Audit & Supervisory Board, Non-statutory Committees
- Constructive Dialogue with Shareholders

For more information, please refer to the Canon Sustainability Report. **https://global.canon/en/csr/report/index.html**

Since 1988, Canon has been striving to uphold our corporate philosophy of *kyosei* (living and working together for the common good) in order to contribute to worldwide prosperity and happiness, to endeavor to make contributions not only through products and services, but also in the areas of environmental protection, sociocultural support, and compliance. In May 2021, with the objective of further enhancing these initiatives, we established the Sustainability Headquarters at our corporate headquarters. We expressed our approach to sustainability and how we are committed to creating new value through the power of technology and innovation, providing world-first technologies and world-leading products and services while also contributing to solutions for the problems our society faces. Going forward, we will undertake numerous activities around the world as we work towards achieving the Sustainable Development Goals (SDGs).

Apart from this, in pursuing a corporate management focused on total optimization, we launched our own Consolidated Performance Evaluation System in 1997. During the period of more than 20 years since it was introduced, it has served as a marker of improvement for each of our business operations and Group companies. The evaluation items are reviewed annually in accordance with our management policy and in line with current trends. Under the system, we evaluate business operations and Group companies not only from their financial results, such as sales and profit, but also from non-financial aspects pertaining to sustainability, such as activities that support environmental and sociocultural initiatives. Through encouraging them to improve their operations, Canon aims to facilitate the sustained development of the Group as a whole and contribute to society.

An activity of Canon Bird Branch Project at the lush green site of our global headquarters.

Environment

In addition to its own business activities, such as development, production, and sales, Canon monitors the CO_2 Emission and other environmental impact at each stage of the product lifecycle, including those of suppliers and customers, and works to reduce them.

We support the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) and we constantly disclose climate-related information in our sustainability reports and on our website.

Contributing to a Carbon-Free Future

We are furthering environmental activities on a Group-wide basis with the goal of achieving an average annual improvement of 3% in lifecycle CO_2 emissions improvement index per product as a yardstick for reducing our environmental footprint across entire product lifecycles. Continuously achieving this target means we will be on track for an improvement of about 50% in 2030 compared to 2008. As of 2021 we have realized a 42% improvement versus 2008.

By working closely with society and implementing a number of initiatives across the entire lifecycle of our products, we aim to achieve net-zero CO_2 emissions by 2050.

Contributing to a Circular Economy

To ensure more efficient use of limited resources and reduce waste, Canon is making products smaller and lighter, and reusing and recycling used products as much as possible. In particular, we are pursuing product-to-product recycling—in other words, recycling used products into new ones, including the remanufacturing of office multifunction devices and the closed-loop recycling of toner cartridges.

Canon currently has five recycling centers in four regions around the world. The Canon Eco Technology Park, which opened in 2018, strives to realize state-of-the-art resource recycling as a front-runner in the creation of a circular economy.

For example, we have achieved a parts reuse rate (mass ratio) of more than 90% for every imageRUNNER ADVANCE C3330F-RG in our Refreshed series of office multifunction devices.

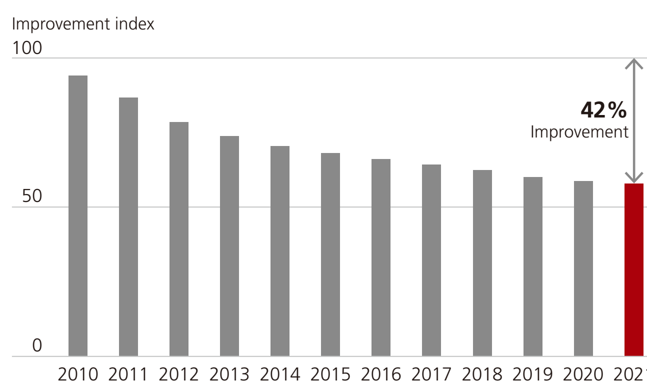
Eliminating Hazardous Substances and Preventing Pollution

Canon comprehensively manages chemical substances in products and those used in manufacturing processes to prevent pollution of the global environment and adverse effects on people's health. Particularly for chemical substances in products, we have built a Group-wide environmental assurance system, and we develop products in conformity with standards established in-house that are in line with the most stringent regulations in the world.

Contributing to a Society in Harmony with Nature

Canon engages in various activities worldwide based on our Biodiversity Policy. As part of these activities, we globally run the Canon Bird Branch Project in an effort to engage in biodiversity conservation across the Canon Group.

Lifecycle CO_2 Emissions Improvement Index per Product



*Indexed to 2008=100

High-resolution facsimile of the "Waves at Matsushima," painted by Tawaraya Sotatsu in the collection of the Freer Gallery of Art, was donated to Shoun-ji Temple, which is said to have owned the original.*

Social

Respecting Human Rights

In 2021, we expressed the Canon Group Human Rights Policy in accordance with the United Nations' Guiding Principles on Business and Human Rights. Guided by this policy, we engaged in a human rights due diligence process to identify significant human rights risks in the Canon Group. We also put in place a grievance mechanism, raised awareness about human rights, and addressed human rights risks in supply chains.

Promoting Diversity

Under our corporate philosophy of *kyosei*, Canon respects global diversity and actively encourages the fair hiring and promotion of employees, regardless of gender, age, or disability. We make every effort to promote the advancement of female employees, and we support the intentions of male employees to participate in child rearing, help employees balance work and nursing care duties, and encourage the active participation of sexual minorities, including those in the LGBT community, as well as employees with disabilities. In 2021, to coincide with International Women's Day, Canon Group companies in the Middle East and Africa launched the "Women who Empower" program, an internal campaign designed to support female empowerment in the workplace.

Responsible Procurement in Supply Chain

Canon is committed to fulfilling socially responsible procurement in cooperation with its business partners. In 2019, we joined the Responsible Business Alliance (RBA). And in 2021, we conducted self-assessments at 54 manufacturing sites and 326 major suppliers using the RBA Self-Assessment Questionnaire (SAQ), and found no major risks.

We also file an annual conflict minerals report with third-party assurance and submit it to the U.S. Securities and Exchange Commission.

Social Contributions

Canon established The Canon Institute for Global Studies and The Canon Foundation in 2008 to commemorate Canon's 70th anniversary.

The Canon Institute for Global Studies analyzes the status quo in terms of how the Japanese economy fits into the broader global economy and what kind of role Japan ought to play in today's world. The Institute facilitates the undertaking of global activities and the exchange of knowledge between various researchers hailing from industrial, government, and academic circles. In addition, the Canon Foundation provides grants to assist a broad range of science and technological research. Starting with grant applications in 2019, the Canon Foundation's activities are now based on the concept of assisting research studies in cutting-edge science and technology fields with the aim of creating new value for society.

Furthermore, as a company that contributes to the development of visual culture, since 2007, Canon and Kyoto Culture Association (NPO) have been working on the Tsuzuri Project (officially named the Cultural Heritage Inheritance Project) with the aim of preserving original cultural assets and utilizing high-resolution facsimiles. By combining Canon's advanced digital technologies, ranging from input to image processing and output, with the traditional craftsmanship of Kyoto, we have produced high-resolution facsimiles of important Japanese cultural assets, including folding screens, *fusuma* (Japanese sliding doors), and handscrolls. These facsimiles have been donated to temples and shrines, local municipalities, or museums that have a special connection with them.

* Facsimiles of works in the collection of the Freer Gallery of Art, Smithsonian Institution, Washington, D.C.: Gift of Charles Lang Freer, F1906.231, F1906.232.

For all company executive officers, the CEO provides updates on earnings progress and important matters to be implemented in the future both in person and online as a way to share crucial information.

Governance

Fundamental Policy

In order to establish a sound corporate governance structure and continuously raise corporate value, the Company believes that it is essential to improve management transparency and strengthen management supervising functions.

Governance Structure

Board of Directors

While the focus of the organizational structure of the Board of Directors is on Representative Directors that oversee company-wide business strategies or execution such as the CEO, COO, CFO, CTO, and Representative Directors or Executive Directors that oversee multiple business fields or headquarters functions, in order to secure sound management, at least one-third and at least two or more Independent Outside Directors are appointed. The Board of Directors, in accordance with laws and regulations, makes important decisions and supervises the execution of duties by officers.

Except for the above, the CEO and other Representative Directors are active in decision making and execution, and under the command and supervision of the Representative Directors, Executive Officers that are elected through resolution of the Board of Directors make decisions and execute operations of each business field or function. Currently, the Board of Directors consists of five members, three Representative Directors from inside the Company and two Independent Outside Directors.

Additionally, there will be 42 Executive Officers, including two females and one non-Japanese as of April 1, 2022.

Audit & Supervisory Board

As a body which is in charge of the audit of operations, under the principles of autonomy, which is independent from the Board of Directors, the Company has full-time Audit & Supervisory Board Members that are familiar with the Company's businesses or its management structure, and Independent Outside Audit & Supervisory Board Members that have extensive knowledge in specialized areas such as law, finance and accounting, and internal control. The Audit & Supervisory Board, which is composed of these individuals, cooperates with the Company's accounting auditors and internal audit division, oversees the status of duty execution of operations and corporate assets to secure the soundness of management.

The Audit & Supervisory Board consists of five individuals, three of which are Independent Outside Audit & Supervisory Board Members.

Procedures in the Nomination of Directors etc.

The Company established the "Nomination and Remuneration Advisory Committee," a non-statutory committee, which consists of the CEO, two Independent Outside Directors, and one Independent Outside Audit & Supervisory Board Member. At the time Director and Audit & Supervisory Board Member candidates are nominated and Executive Officers are appointed (includes the selection of a successor for the chief executive officer position), the CEO recommends candidates thereof from among individuals that have been recognized as having met the prescribed requirements, and the Committee checks the fairness and validity of such recommendation prior to submission to and deliberation by the Board of Directors.

Additionally, as for Audit & Supervisory Board Member candidates, prior to deliberation of the Board of Directors, consent of the Audit & Supervisory Board shall be acquired.

Governance

Corporate Strategy Committee, Risk Management Committee, and Disclosure Committee

The Company established the Corporate Strategy Committee, consisting of Representative Directors and some Executive Officers. Among items to be decided by the CEO, the Committee undertakes prior deliberations on important matters pertaining to Canon Group strategies. Outside Directors and Audit & Supervisory Board members attend Corporate Strategy Committee meetings and are able to express their own opinions. Based on a resolution passed by the Board of Directors, Canon set up the Risk Management Committee, which formulates policy and action proposals regarding improvement of the Canon Group risk management system. The Risk Management Committee consists of three entities: the Financial Risk Management Subcommittee, which is tasked with improving systems to ensure reliability of financial reporting; the Compliance Subcommittee, which is tasked with promoting corporate ethics and improving legal compliance systems; and the Business Risk Management Subcommittee, which is charged with improving systems to manage overall business risks, including risks related to product quality and information leak. The Risk Management Committee verifies the risk management system's improvement and implementation and reports the status to the CEO and the Board of Directors.

In addition, the Disclosure Committee was established to undertake deliberations pertaining to information disclosure, including content and timing, to ensure important corporate information will be disclosed in a timely and accurate manner.

Internal Audit Division

The Company has established the Corporate Audit Center as its internal auditing division, which audits, evaluates, and makes recommendations on compliance and internal control systems etc. The Corporate Audit Center also conducts audits on topics such as quality, the environment, and information security. Audit results are reported not only to the CEO and CFO, but also to the Audit & Supervisory Board Members and the Audit & Supervisory Board. In addition, the Company has established a system in which reports are also regularly given to outside directors and those outside directors can request submission of proposals to the Board of Directors, as necessary.

Details of Canon Inc.'s corporate governance structure are available on the Company's website under "an overview of Corporate Governance at Canon Inc."
https://global.canon/en/ir/strategies/governance.html

FINANCIAL SECTION

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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 office multifunction devices ("MFDs"), laser printers, inkjet printers, cameras, medical equipment and 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 four segments: the Printing Business Unit, the Imaging Business Unit, the Medical Business Unit and the Industrial and Others Business Unit.

Economic environment

Looking back at 2021, the global economy continued to recover as movement restrictions were gradually eased and the rollout of vaccines worldwide encouraged resumption of economic activities. However, production activity stagnated due to a resurgence of coronavirus disease ("COVID-19") infections. In addition, the global shortage of semiconductor chips and the disruption in logistic and distribution channels due to high demand became a serious issue in the second half of the year. In the United States, economic recovery advanced as a result of the increased personal consumption and expansion of capital investment through economic measures. In Europe, restrictions on economic activities were eased in each country, with increasing personal consumption and expansion of capital investment leading to a steady economic recovery. In China, personal consumption and exports continued to grow steadily despite sluggish infrastructure investment. In other emerging countries, economic recovery was modest due to stagnant economic activity caused by the spread of COVID-19 infections, mainly in India and Southeast Asia. In Japan, economic recovery remained moderate due to the prolonged State of Emergency.

Market environment

Amid these conditions, in the markets in which Canon operates, demand for products remained solid, despite the impact of the shortage of semiconductor chips in the second half of the year. Demand for office MFDs continued to recover. For laser printers, demand remained at the same level as the previous year. For inkjet printers, demand in home use remained solid. For cameras, demand remained solid, mainly in mirrorless cameras. For medical equipment, despite delays in the installation of medical devices in some areas due to the resurgence of COVID-19 infections, recovery continued thanks to the return of routine examinations at medical institutions compared with the previous year, in which COVID-19 testing was prioritized. For lithography equipment, demand for semiconductor lithography equipment continued amid favorable market conditions and flat panel display ("FPD") lithography equipment remained solid.

The average value of the yen for the year was ¥109.93 against the U.S. dollar, a year-on-year depreciation of approximately ¥3, and ¥129.94 against the euro, a year-on-year depreciation of approximately ¥8.

Summary of operations

In 2021, unit sales of office MFDs were above those of the previous year, despite the shortage of semiconductor chips in the second half of the year. Sales of services and consumables moderately recovered due to the gradual increase in employees returning to the office and resulting demand for related services and consumables. As for the Prosumer consisting of laser printers and inkjet printers, unit sales were below those of the previous year due to the stagnation of production activity resulting from a resurgence of COVID-19 infections in Southeast Asia. However, unit of sales of laser printer consumables increased significantly compared with the previous year, during which demand had decreased. For interchangeable-lens digital cameras, unit sales remained at around the same level as the previous year due to the shortage of semiconductor chips, despite continued strong sales of full-frame mirrorless cameras. As for network cameras, which are being used in a growing range of applications, sales increased due to the strengthening of sales activities. For medical equipment, sales increased mainly in Japan and North America due to strong sales of computed tomography ("CT") systems and diagnostic ultrasound systems as a result of recovering demand in key markets and government's support for medical institutions. While unit sales for semiconductor lithography equipment remained solid, unit sales for FPD lithography equipment were significantly above those of the previous year, when equipment installation stagnated due to circumstances related to COVID-19. Under these conditions, net sales for the year increased by 11.2% year-on-year to ¥3,513,357 million. Gross profit to net sales ratio increased by 2.8 points to 46.3%, due to recovery of services and consumables, increase in prices, expansion of highly profitable products and currency exchange rate fluctuations, despite the increase of cost due to higher prices of semiconductor chips and resin materials. Gross profit for the year increased by 18.3% year-on-year to ¥1,627,792 million. Operating expenses increased by 6.4% year-on-year to ¥1,345,874 million, mainly due to the increase of payroll cost, advertising cost, forwarding cost and R&D cost as a result of a rebound from the previous year, when sales activities were severely restricted due to the spread of COVID-19 and currency exchange rate fluctuations. However, operating expense percentage improved significantly from 40.0% to

38.3% thanks to the results of structural reform and group-wide improvements in productivity. As a result, operating profit increased by 155.0% year-on-year to ¥281,918 million. Other income (deductions) increased by ¥1,055 million year-on-year to ¥20,788 million, due to such factors as valuation gain on securities, while income before income taxes increased by 132.4% year-on-year to ¥302,706 million and net income attributable to Canon Inc. increased by 157.7% year-on-year to ¥214,718 million. Basic net income attributable to Canon Inc. shareholders per share was ¥205.35 for the year, a year-on-year increase of ¥125.98.

Total assets increased by ¥125,274 million to ¥4,750,888 million at December 31, 2021, compared with the end of previous year, mainly due to an increase of inventories resulting from difficulty in procuring parts and recovery production to supplement product supply due to reduced operating rates at production sites, and an increase of goodwill due to the acquisition of Redlen which play an important role in PCCT development. In addition, under the new five-year management plan, Phase VI, of the "Excellent Global Corporation Plan" which started from 2021, Canon regards thorough cash flow management as one of its priority items, and is reinforcing its financial health. In 2021, under management plan, Canon is comprised of the refinancing and the repayment of loans which was provided for the acquisition of Toshiba Medical Systems Corporation (currently, Canon Medical Systems Corporation) resulting in the decrease of long-term loans by ¥170.0 billion. Under these conditions, total liabilities decreased by ¥189,114 million to ¥1,652,459 million at December 31, 2021, compared with the end of previous year, mainly due to a decrease of short-term loans and current portion of long-term debt. Total equity increased by ¥314,388 million to ¥3,098,429 million at December 31, 2021, compared with the end of previous year, mainly due to an increase in retained earnings resulting from a significant increase in profit and an increase in accumulated other comprehensive income due to the depreciation of the yen. Under these conditions, Canon Inc. shareholders' equity as a percentage of total assets increased by 4.8 points to 60.5%.

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 the next page.

Net sales and profit ratio

As Canon pursues the goal to become a truly excellent global corporation, 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 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 product to be important for the purpose of assessing Canon's sales performance in various products, taking into account recent market trends.

Gross profit to net sales ratio is another KPI for Canon. Under the basic policy of Phase VI, Canon has been consistently strengthening business competitiveness and striving to provide highly profitable products with price competitiveness. Furthermore, Canon promotes cost reduction initiatives across the Canon Group through in-house production and automation of assembly processes which integrate the three functions of design, production technology and manufacturing. Canon will continue to actively take these measures to improve Canon's gross profit to net sales ratio.

Operating profit to net sales ratio, income before income taxes to net sales ratio, 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 adequate spending in core technology to sustain Canon's leading position in its current business areas and to exploit opportunities 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 relating to cash flow management that Canon's management believes to be important.

Inventory turnover measured in days is a KPI because it measures the efficiency 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.

The debt to total assets ratio is also one of the KPIs. For a manufacturing company like Canon, it generally takes considerable time to realize profit from a business due to lead times required for R&D, manufacturing and sales. Therefore, management believes that it is important to have sufficient financial strength. Canon will continue to reduce its dependency on external funds for capital investments in favor of generating the necessary funds from its own operations.

Canon Inc. shareholders' equity to total assets ratio is another KPI for Canon. Canon believes that its shareholders' equity to total assets ratio measures its long-term sustainability. Canon also believes that achieving a high or rising shareholders' 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's management believes a high shareholders' equity ratio will enable Canon 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 shareholders' equity to total assets ratio.

KEY PERFORMANCE INDICATORS

	2021	2020	2019	2018	2017
Net sales (Millions of yen)	**3,513,357**	3,160,243	3,593,299	3,951,937	4,080,015
Gross profit to net sales ratio	**46.3%**	43.5%	44.8%	46.4%	48.8%
R&D expense to net sales ratio	**8.2%**	8.6%	8.3%	8.0%	8.2%
Operating profit to net sales ratio	**8.0%**	3.5%	4.9%	8.7%	7.9%
Income before income taxes to net sales ratio	**8.6%**	4.1%	5.4%	9.2%	8.7%
Inventory turnover measured in days	**66 days**	60 days	59 days	56 days	49 days
Debt to total assets ratio	**6.8%**	10.9%	10.8%	8.2%	10.2%
Canon Inc. shareholders' equity to total assets ratio	**60.5%**	55.7%	56.3%	57.5%	55.1%

Notes:
1. Inventory turnover measured in days is determined by: Inventory divided by net sales for the previous six months, multiplied by 182.5.
2. The increase of the debt to total assets ratio in 2019 was primarily due to adopting Accounting Standards Update ("ASU") No. 2016-02, Leases (Topic 842) Section A. The company includes current operating lease liability and noncurrent operating lease liability as the debt since 2019. If this factor were excluded, the debt to total assets ratio in 2019 is 8.6%.
3. The decrease of the Canon Inc. shareholders' equity to total assets ratio in 2019 was primarily due to adopting ASU No. 2016-02, Leases (Topic 842) Section A. The company includes operating lease right-of-use assets in total assets since 2019. If this factor were excluded, Canon Inc. shareholders' equity to total assets ratio is 57.9%.
4. Canon adopted ASU No. 2017-07 from the quarter beginning January 1, 2018. The adoption of the new presentation requirement of the service cost component and the other components of net benefit cost resulted in reclassification from cost of sales, and selling, general and administrative expenses, and research and development expenses into other income (deductions) for the year ended December 31, 2017.
5. Certain figures for the fiscal years ended December 31, 2019, 2018 and 2017 presented in the table above have been revised from the versions previously disclosed. During the year ended December 31, 2020, Canon corrected an immaterial error in its previously issued consolidated financial statements related to accounting for the Company's and domestic subsidiaries' compensated absence carryforward as disclosed in the previous fiscal year. For further details, please refer to Note 1 (y) of the Notes to Consolidated Financial Statements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles ("U.S. 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. In addition, new waves of COVID-19 infections are being seen in some regions, and it is still difficult to predict when COVID-19 will be brought under control. However, each country and region continues to pursue infection control and accelerate economic activities. Actual results and outcomes may differ from management's estimates and assumptions due to risks and uncertainties, including uncertainty in the current economic environment triggered by COVID-19. 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 through the sale of products of the Printing Business Unit, the Imaging Business Unit, the Medical Business Unit and the Industrial and Others Unit, supplies and related services under separate contractual arrangements. Revenue is recognized when, or as, control of promised goods or services transfers to customers in an amount that reflects the consideration to which Canon expects to be entitled in exchange for transferring these goods or services.

Revenue from sales of products of the Printing Business Unit, such as office MFDs, laser printers and inkjet printers, and the Imaging Business Unit, such as digital cameras, is primarily recognized upon shipment or delivery, depending upon when the customer obtains controls of these products.

Revenue from sales of equipment of the Medical Business Unit and the Industrial and Others Business Unit that are sold with customer acceptance provisions related to their functionality including certain medical equipment such as CT systems and MRI systems, and lithography equipment such as semiconductor and FPD lithography equipment, is recognized when the equipment is installed at the customer site and the agreed-upon specifications are objectively satisfied and confirmed.

Most of Canon's service revenue is generated from maintenance service in the products of the Printing Business Unit and the Medical Business Unit which is recognized over time. For the service contracts of the products of the Printing Business Unit, the customer typically pays a variable amount based on usage, a stated fixed fee or a stated base fee plus a variable amount which frequently include the provision of consumables as well as break fix activities. The majority portion of service revenue from the products of the Printing Business Unit is recognized as billed since the invoiced amount directly correlates with the value to the customer of the underlying performance obligation to date. For the service contracts of the products of the Medical Business Unit, the customer typically pays a stated fixed fee for the stand ready maintenance service and revenue is recognized ratably over the contract period.

The majority of service arrangements for the products of the Printing Business Unit are executed in combination with related products. Transaction prices for products and services need to be allocated to each performance obligation on a relative standalone selling price basis where judgements are required. Canon estimates the standalone selling price using a range of prices that would meet the allocation objective based on all the information that is reasonably available including market conditions and other observable inputs. If transaction prices of the product or service contracts are not within the acceptable range, then the revenue is subject to allocation based on the estimated standalone selling prices. Canon recognizes the incremental costs of obtaining a contract as an expense when related products of the Printing Business Unit are sold.

Revenue from sales of certain industrial equipment which do not have alternative use and for which Canon has enforceable right to payment to the customers for the performance completed to date is recognized over time with progress towards completion measured using the cost based input method as the basis to recognize revenue and an estimated margin. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses become evident. Changes in job performance, job conditions, estimated margin and final contract settlements may result in revisions to projected costs and revenue and are recognized in the period in which the revisions to estimates are identified and the amounts can be reasonably estimated. Factors that may affect future project costs and margins include, production efficiencies, availability and costs of labor and materials. These factors can impact the accuracy of Canon's estimates and materially impact future reported revenue and cost of sales.

The transaction prices that Canon is entitled to receive in exchange for transferring goods or services to the customer include certain forms of variable consideration, including product discounts, customer promotions and volume-based rebates mainly for the products of the Imaging Business Unit, which are sold predominantly through distributors and retailers. Canon includes estimated amounts in the transaction price only to the extent it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is resolved. Variable considerations are estimated based upon historical trends and other known factors at the time of sale, and are subsequently adjusted in each period based on current information. In addition, Canon may provide a right of return on its products for a short time period after a sale. These rights are accounted for as variable consideration when determining the transaction price, and accordingly Canon recognizes revenue based on the estimated amount to which Canon expects to be entitled after considering expected returns.

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

Allowance for credit losses

Allowance for credit losses for trade and finance receivables is maintained for all customers based on ASC 326 “Financial Instruments – Credit Losses,” considering various 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.

Valuation of inventories

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

Lease

As for lessor accounting, Canon provides leasing arrangement to its customers primarily for the sale of office products. Revenue from the sale of these products under sales-type leases is recognized at the inception of the lease. Interest 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 product leases are bundled with maintenance contracts, revenue is allocated based upon the estimated standalone selling prices of the lease and non-lease components. Lease components generally include product and financing while non-lease components generally consist of maintenance contracts and supplies. Some of the contracts include options to extend or to terminate the lease. Canon takes such options into account to determine the lease term when it is reasonably certain that the customers will exercise these options. The majority of Canon's lease contracts do not contain bargain purchase options for their customers.

As for lessee accounting, Canon has operating and finance leases for various assets including office buildings, warehouses, employees' accommodations, and vehicles. Canon determines if an arrangement is a lease at the inception of each contract. Some of the contracts include options to extend or to terminate the lease. Canon takes such options into accounts to determine the lease term when it is reasonably certain that it will exercise these options. Canon's lease arrangements do not contain material residual value guarantees or material restrictive covenants. As a rate implicit in most of Canon's leases cannot be determined, Canon uses incremental borrowing rate based on the information available at commencement to determine the present values of lease payments. Canon has lease contracts with lease and non-lease components, which are accounted for separately. Canon allocates the consideration in the lease contract to the lease and non-lease components based upon the estimated standalone prices. Costs associated with operating lease assets are recognized on a straight-line basis over the term of the lease.

Business combinations

Acquisitions are accounted for using the acquisition method of accounting. The acquisition method of accounting requires the identification and measurement of all acquired tangible and intangible assets and assumed liabilities at their respective fair values, as of the acquisition date. The determination of the fair value of net assets acquired involves significant judgment and estimates, such as future cash flow projections, appropriate discount and capitalization rates and other estimates based on available market information. Estimates of future cash flows are based on a number of factors including operating results, known and anticipated trends, as well as market and economic conditions.

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. 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 recognizes an impairment charge in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. Fair value of a reporting unit is determined primarily based on the discounted cash flow analysis which involves estimates of projected future cash flows and discount rates. Estimates of projected future cash flows are primarily based on Canon's forecast of future growth rates. Estimates of discount rates are determined based on the weighted average cost of capital, which considers primarily market and industry data as well as specific risk factors. Canon has completed its impairment test in the fourth quarter of 2021 and determined that there were no reporting units that were at risk of failing the impairment test as the fair value of each reporting unit substantially exceeded its respective carrying amount. However, with regard to goodwill attributed to the Medical Reporting Unit, fair values in excess of reported carrying values as a percentage is lower than other reporting units. As a result, a future reduction in cash flows of the related business, could trigger an impairment. The goodwill related to this reporting unit as of December 31, 2021 is ¥537,183 million. Future cash flows for the Medical Reporting Unit were based on a mid-term management plan that considered the future market growth of medical equipment and growth in geographies where Canon operates its medical business. Intangible assets with finite useful lives consist primarily of software, trademarks, patents and developed technology, license fees and customer relationships, which are amortized using the straight-line method. The estimated useful lives of software are from 3 years to 8 years, trademarks are 15 years, patents and developed technology are from 5 years to 21 years, license fees are 8 years, and customer relationships are from 7 years to 15 years, respectively.

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 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 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 2021, Canon estimated a weighted-average discount rate used to determine benefit obligations of 0.5% for Japanese plans and 1.5% for foreign plans and a weighted-average expected long-term rate of return on plan assets of 3.0% for Japanese plans and 4.4% for foreign plans. In estimating the discount rate, Canon uses available information about rates of return on high-quality fixed-income government 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 2021, a decrease of 50 basis points in the discount rate increases the projected benefit obligation by approximately ¥96,008 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 2021, a decrease of 50 basis points in the expected long-term rate of return on plan assets would increase approximately ¥5,758 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 deferred amount 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 an accumulated other comprehensive income (loss), net of tax.

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, and are included in other noncurrent liabilities in the consolidated balance sheets. Such liabilities are adjusted as further information develops or circumstances change. Costs of future obligations are not discounted to their present values.

Recently Issued Accounting Guidance

Please refer to Note 1 of the Notes to Consolidated Financial Statements.

CONSOLIDATED RESULTS OF OPERATIONS

SUMMARY OF OPERATIONS

	Millions of yen				
	2021	change	2020	change	2019
Net sales	**3,513,357**	**+11.2%**	3,160,243	-12.1%	3,593,299
Products and Equipment	**2,804,680**	**+12.6%**	2,489,829	-12.2%	2,835,428
Services	**708,677**	**+5.7%**	670,414	-11.5%	757,871
Operating profit	**281,918**	**+155.0%**	110,547	-36.6%	174,420
Income before income taxes	**302,706**	**+132.4%**	130,280	-33.4%	195,493
Net income attributable to Canon Inc.	**214,718**	**+157.7%**	83,318	-33.3%	124,964

Note: See note to KEY PERFORMANCE INDICATORS

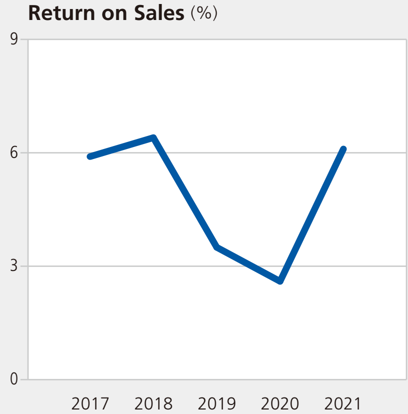
Sales

In the current business term, on a global basis, the economic recovery continued. In such an environment, although production activity stagnated due to a resurgence of COVID-19 infections and a shortage of semiconductor chips, Canon's consolidated net sales in 2021 totaled ¥3,513,357 million, an increase of 11.2% from the previous year largely due to a recovery of demand in each segment. Net sales of products and equipment totaled ¥2,804,680 million, a year-on-year increase of 12.6%, while net sales of services totaled ¥708,677 million, a year-on-year increase of 5.7%.

Overseas operations are significant to Canon's operating results and generated 76.4% of total net sales in 2021. Such sales are denominated in the applicable local currencies and are subject to fluctuations in the value of the yen relative 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 during the year was ¥109.93 against the U.S. dollar, a year-on-year depreciation of approximately ¥3, and ¥129.94 against the euro, a year-on-year depreciation of approximately ¥8. The effects of foreign exchange rate fluctuations positively affected net sales by approximately ¥110,830 million in 2021. This favorable impact consisted of approximately ¥38,624 million of favorable impact for the U.S. dollar denominated sales and favorable impact of ¥47,967 million for the euro denominated sales, and favorable impact of ¥24,239 million for other foreign currency denominated sales.

Return on 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. In 2021, Canon promoted cost reduction such as a common platform of office MFDs, although Canon was affected by rising prices of parts and materials, mainly semiconductor chips and resin materials, as well as by rising transportation costs due to the high demand for international freight transport. Under these conditions, the ratios of cost of sales to net sales for 2021 and 2020 were 53.7% and 56.5%, respectively. Cost of sales as a percentage of net sales decreased by 2.8 points.

Gross profit

Canon's gross profit in 2021 increased by 18.3% to ¥1,627,792 million from 2020. The gross profit to net sales ratio also increased by 2.8 points to 46.3%. The increase in the gross profit and gross profit to net sales ratio were mainly due to the cost reduction mentioned above, recovery of services and consumables due to a recovery in office occupancy rates, maintained levels of sales volumes and price levels for the EOS R5 and EOS R6 full-frame mirrorless cameras, expansion of the lineup to 26 lenses through the addition of 8 new products of RF-series interchangeable lenses which is a dedicated lens for full-frame mirrorless cameras and currency exchange rate fluctuations.

Operating expenses

The major components of operating expenses are payroll, R&D, advertising expenses and other marketing expenses. Operating expenses in 2021 increased by 6.4% year on year to ¥1,345,874 million, mainly due to a rebound from the previous year, when sales activities were severely restricted due to the spread of COVID-19 infections and currency exchange rate fluctuations. However, operating expenses as a percentage of net sales decreased by 1.7 points to 38.3% due to the promotion of structural reform of sales organizations, as well as reducing business trips through the use of video conferencing systems. As a result, Canon managed to appropriately control expenses in response to the growth in net sales and to control the growth of expenses.

Operating profit

Operating profit in 2021 increased by 155.0% from 2020 to a total of ¥281,918 million. The operating profit to net sales ratio increased by 4.5 points to 8.0% from 2020.

Other income (deductions)

Other income (deductions) for 2021 was ¥20,788 million, an increase of ¥1,055 million from 2020 mainly due to such factors as valuation gain on securities.

Income before income taxes

Income before income taxes in 2021 was ¥302,706 million, an increase of 132.4% from 2020, and constituted 8.6% of net sales.

Income taxes

Income taxes in 2021 increased by ¥37,529 million from 2020. The effective tax rate for 2021 was 23.7%, which was lower than the statutory tax rate in Japan. This resulted from a combination of factors such as the increase in tax credits of R&D expenses, the lower effective tax rates at foreign subsidiaries compared to the statutory tax rate in Japan and the reversal of the valuation allowances recognized by foreign subsidiaries owing to the improvement of the entities' profitability.

Net income attributable to Canon Inc.

As a result, net income attributable to Canon Inc. in 2021 increased by 157.7% to ¥214,718 million, which represents 6.1% of net sales. Net income attributable to Canon Inc. as a percentage of net sales increased by 2.6 points from 2019 before COVID-19 infections due to the structural reform and measures to improve profitability.

Segment information

Canon operates four segments: the Printing Business Unit, the Imaging Business Unit, the Medical Business Unit and the Industrial and Others Business Unit.

- **The Printing Business Unit** mainly includes Office MFDs / Document solutions / Laser MFPs / Laser printers / Inkjet printers / Image scanners / Calculators / Digital continuous feed presses / Digital sheet-fed presses / Large format printers
- **The Imaging Business Unit** mainly includes Interchangeable-lens digital cameras / Interchangeable lenses / Digital compact cameras / Compact photo printers / Network cameras / Video management software / Video content analytics software / Digital camcorders / Digital cinema cameras / Broadcast equipment / Multimedia projectors
- **The Medical Business Unit** mainly includes CT systems / Diagnostic ultrasound systems / Diagnostic X-ray systems / MRI systems / Clinical chemistry analyzers / Digital radiography systems / Ophthalmic equipment
- **The Industrial and Others Business Unit** mainly includes Semiconductor lithography equipment / FPD lithography equipment / OLED display manufacturing equipment / Vacuum thin-film deposition equipment / Die bonders / Handy terminals / Document scanners

Operating results by segment

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

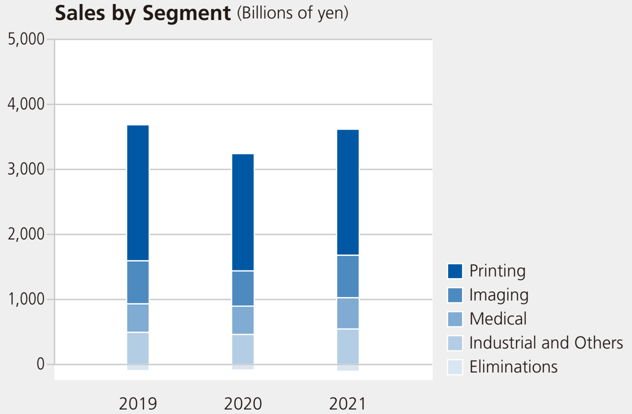
Within the Printing Business Unit, unit sales of office MFDs increased compared with the previous year as the imageRUNNER ADVANCE DX series saw solid demand and demand for MFDs continued to recover despite the shortage of semiconductor chips. Sales of services and consumables increased due to a recovery in office occupancy rates. For equipment in the production printing market, the varioPRINT iX series of high-speed sheet-fed color inkjet presses earned favorable reviews, and sales of services and consumables increased due to the recovery. As for laser printers, unit sales decreased compared with the previous year due to stagnation of production activity resulting from the resurgence of COVID-19 infections in Southeast Asia. However, sales of consumables increased significantly compared with the previous year, during which time demand had decreased. For inkjet printers, unit sales were below those of the previous year due to stagnation of production activity in Southeast Asia. However, unit sales of refillable ink tank printers were above those of the previous year due to solid global demand. Total sales were above those of the previous year due to a focus on higher-priced models. In addition, profitability improved due to a cost reduction as a result of common platformization and product mix as a result of increase of service profit due to a recovery in office occupancy rates, although operating costs increased due to a rebound from the previous year, when sales activities were severely restricted due to the spread of COVID-19. These factors resulted in total sales for the business unit of ¥1,938,847 million, a year-on-year increase of 7.4%, while income before income taxes increased by 53.1% year-on-year to ¥232,952 million.

As for the Imaging Business Unit, unit sales of interchangeable-lens digital cameras were the same level as the previous year, despite the shortage of semiconductor chips. The price level was maintained even after more than a year since the EOS R5 and EOS R6 full-frame mirrorless cameras were released. In addition, unit sales of RF-series interchangeable lenses increased significantly due to the synergistic effects with the cameras. As for network cameras, despite the continued impact of COVID-19, sales increased mainly as a result of strengthening sales activities for such diversified applications as monitoring of congested and confined spaces as well as conventional market needs including crime prevention and disaster monitoring tools. In addition, profitability improved due to the accelerated shift to highly profitable products such as EOS R system cameras and interchangeable lenses, although operating costs increased due to a rebound from the previous year, when sales activities were severely restricted due to the spread of COVID-19. These factors resulted in total sales for the business unit of ¥653,532 million, a year-on-year increase of 20.7%, while income before income taxes increased by 1,484.5% year-on-year to ¥78,462 million.

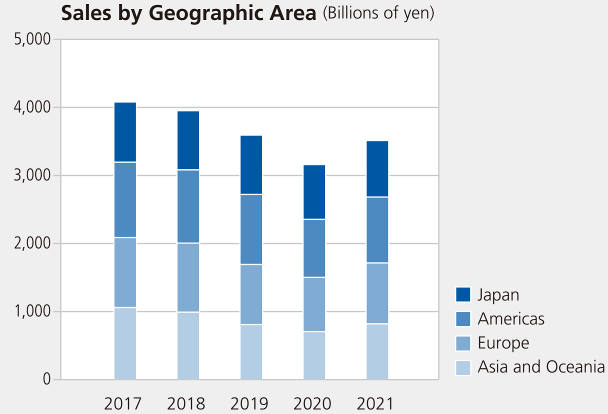
As for the Medical Business Unit, although the resurgence of COVID-19 infections and the shortage of semiconductor chips and shipping containers had an impact on production and installation, sales remained solid due to returning routine examinations at medical institutions. Sales of CT systems and diagnostic ultrasound systems increased mainly due to capitalizing on opportunities with medical institutions in Japan supported by the government and recovering demand in the North America. In addition, profitability improved due to a cost reduction as a result of volume discount based on business expansion. These factors resulted in total sales for the business unit of ¥480,362 million, a year-on-year increase of 10.2%, while income before income taxes increased by 34.3% year-on-year to ¥34,296 million, recording highs for both sales and income before income taxes for the Medical Business Unit.

As for the Industrial and Others Business Unit, regarding semiconductor lithography equipment, unit sales increased compared with the previous year due to strong demand in a wide range of products such as sensors and memory. For FPD lithography equipment, demand for panels used in devices including laptops, tablets and high-resolution display panels remained strong. As a result, unit sales increased significantly compared with the previous year, when equipment installation stagnated due to circumstances related to COVID-19. In addition, these products are mostly manufactured at the domestic manufacturing facilities where impacts of COVID-19 related production disruption were very limited resulting in continuous production activities with better cost reduction. These factors resulted in total sales for the business unit of ¥545,742 million, a year-on-year increase of 18.2%, while income before income taxes totaled ¥44,650 million, a year-on-year increase of 105.9%.

Sales by Segment (Billions of yen)



Sales by Geographic Area (Billions of yen)



SALES BY SEGMENT

	Millions of yen				
	2021	change	2020	change	2019
Printing	**1,938,847**	**+7.4%**	1,804,427	-13.8%	2,092,464
Imaging	**653,532**	**+20.7%**	541,314	-18.2%	661,706
Medical	**480,362**	**+10.2%**	436,074	-0.6%	438,525
Industrial and Others	**545,742**	**+18.2%**	461,522	-6.5%	493,784
Eliminations	**(105,126)**	**—**	(83,094)	—	(93,180)
Total	**3,513,357**	**+11.2%**	3,160,243	-12.1%	3,593,299

Note: Based on the realignment of Canon's internal reporting and management structure, from 2021, Canon has changed the name and structure of segments from Office Business Unit, Imaging System Business Unit, Medical System Business Unit and Industry and Others Business Unit to Printing Business Unit, Imaging Business Unit, Medical Business Unit, and Industrial and Others Business Unit. Major changes include moving Inkjet printers from Imaging System Business Unit to the Printing Business Unit, the same business unit as Office MFDs and Laser MFPs, and moving Network cameras from Industry and Others Business Unit to the Imaging Business Unit, the same business unit as Interchangeable-lens digital cameras. Net sales by segments for the fiscal years ended December 31, 2020 and 2019 also have been reclassified.

SALES BY GEOGRAPHIC AREA

	Millions of yen				
	2021	change	2020	change	2019
Japan	**830,378**	**+3.0%**	806,305	-7.6%	872,534
Americas	**968,839**	**+13.7%**	852,451	-17.2%	1,029,078
Europe	**894,898**	**+12.5%**	795,616	-9.8%	882,480
Asia and Oceania	**819,242**	**+16.1%**	705,871	-12.8%	809,207
Total	**3,513,357**	**+11.2%**	3,160,243	-12.1%	3,593,299

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

Sales by geographic area

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

In Japan, net sales increased by 3.0% from the previous year mainly owing to an increase in sales of CT systems and diagnostic ultrasound systems mainly due to capitalizing on opportunities with medical institutions.

In the Americas, net sales increased by 13.7% from the previous year mainly owing to an increase in sales of most products mainly due to the recovery from the decline of the demand caused by COVID-19.

In Europe, net sales increased by 12.5% from the previous year mainly owing to an increase in sales of most products mainly due to the recovery from the decline of the demand caused by COVID-19.

In Asia and Oceania, net sales increased by 16.1% from the previous year mainly owing to an increase in sales of most products mainly due to the recovery from the decline of the demand caused by COVID-19.

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 to net sales 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

Canon's basic policy for financial strategies is to maintain a sound financial position through consistent cash flow management, and the two basic principles of cash flow management are as follows:

- Canon strives to improve a highly profitable structure by further improving the profitability of existing businesses and accelerating the growth of new businesses.
- Canon strives to maintain financial soundness by keeping total capital investments for medium-term business expansion and growth within the range of depreciation and amortization expenses. However, Canon plans to actively engage in large-scale M&A for growth strategies, and also raises external funds as needed.

Raising Funds (Cash-In)
Canon is basically funded by net cash provided by operating activities. In procuring funds, Canon considers terms, currencies and methods in light of financial market conditions, and selects the most appropriate instrument from a variety of options.

Use of Funds (Cash-Out)
The principal use of cash is determined in accordance with the following priorities.

- Investment for growth such as capital investment, R&D, M&A, etc.:
  Canon values M&A as an option for early development and expansion of new businesses. The selection of investment targets is based on the growth potential and size of the market, and on the market being highly compatible with the Canon's business domains and technologies.
- Return to shareholders:
  Canon returns profits to shareholders stably and aggressively, mainly in the form of a dividend, taking into consideration medium- to long-term business prospects, planned future investments, cash flow and other factors.
- Repayment of borrowings:
  Canon has been repaying borrowings in recent years, following investment for growth and return to shareholders. In fiscal 2021, in particular, Canon made steady progress in repayment of borrowings by utilizing net cash provided by operating activities, which increased from the previous fiscal year due to significantly improved business performance.

Cash and cash equivalents decreased by ¥6,289 million to ¥401,395 million in fiscal 2021 compared to the previous year. Canon's cash and cash equivalents are primarily denominated in Japanese yen and in U.S. dollars, with the remainder denominated in other currencies.

Net cash provided by operating activities increased by ¥117,223 million to ¥451,028 million in fiscal 2021 compared to the previous year due to a significant increase in profit. 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.

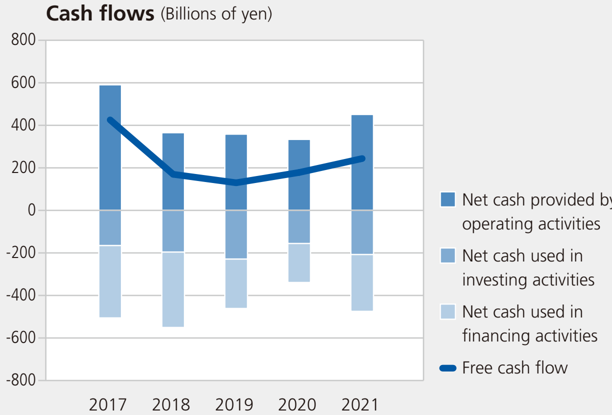
For fiscal 2021, cash inflow from cash received from customers increased due to sales improvement. There were no significant changes in Canon's collection rates. Cash outflow for payments for parts and materials increased due to an increase of inventory compared with the inventory in fiscal 2020 as a result of the global shortage of semiconductor chips and the disruption in logistic and distribution channels. Cash outflow for payments for income taxes increased due to an increase in taxable income.

Net cash used in investing activities increased by ¥51,817 million to ¥207,256 million in fiscal 2021 mainly due to an increase in acquisitions of business and in payment for purchases of fixed assets. Acquisitions of business increased by ¥31,624 million to ¥31,751 million in fiscal 2021 mainly due to the acquisition of Redlen that play an important role in PCCT development. Purchases of fixed assets increased by ¥12,631 million to ¥177,350 million in fiscal 2021 mainly due to capital investment to enhance production capacity and efficiency. Major purchases of fixed assets in fiscal 2021 included construction of new production base for consolidation and renovation at Canon Mold Co., Ltd. and capital investments to increase Complementary Metal Oxide Semiconductor ("CMOS") sensor production capacity at Canon Inc., Hiratsuka Plant, etc.

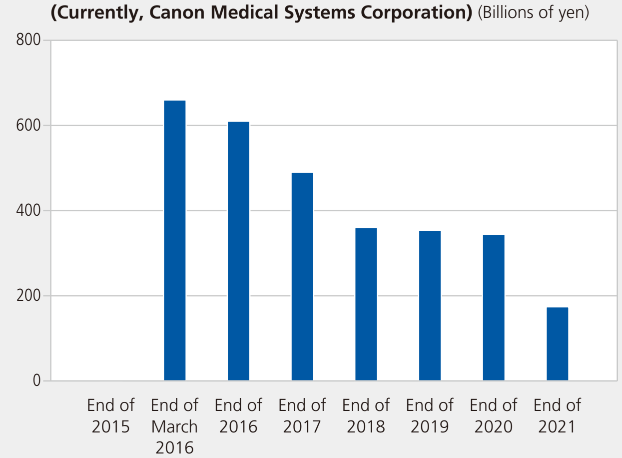
Canon defines "free cash flow" as cash flows from operating activities less cash flows from investing activities. For fiscal 2021, free cash flow increased by ¥65,406 million to ¥243,772 million as compared with ¥178,366 million for fiscal 2020.

Note: "Free cash flow" is a non-GAAP measure. Refer to the "Non-GAAP Financial Measures" section for the explanation and the reconciliation to the reported GAAP measure.

Cash flows (Billions of yen)



Outstanding balances of loans for the acquisition of Toshiba Medical Systems Corporation (Currently, Canon Medical Systems Corporation) (Billions of yen)



Canon's management places importance on cash flow management and frequently monitors this indicator. 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 and believes that such indicator is beneficial to investors. 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 ¥267,366 million in fiscal 2021, mainly due to a decrease of long-term loans by ¥170,000 million as a result of the refinancing and the repayment of loans which was provided for the acquisition of Toshiba Medical Systems Corporation (currently, Canon Medical Systems Corporation) and the dividend payout of ¥88,891 million. The Company paid dividends in fiscal 2021 of ¥85.00 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, issuance of corporate bond or 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.

Canon repaid ¥344,000 million of loans due in December 2021, which was provided for the acquisition of Toshiba Medical Systems Corporation (currently, Canon Medical Systems Corporation). In addition, on December 28, 2021, Canon entered into a borrowing agreement of ¥174,000 million with Mizuho Bank, Ltd. and MUFG Bank, Ltd. For further information, please refer to Note 9 of the Notes to Consolidated Financial Statements. As a result, short-term loans (including the current portion of long-term debt) decreased by ¥347,344 million to ¥44,891 million at December 31, 2021 compared with ¥392,235 million at December 31, 2020. Long-term debt (excluding the current portion) increased by ¥174,916 million to ¥179,750 million at December 31, 2021 compared with ¥4,834 million at December 31, 2020.

Canon's long-term debt mainly consists of bank borrowings and finance lease obligations.

In order to facilitate access to global capital markets, Canon obtains a credit rating from S&P Global Ratings ("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 February 28, 2022, Canon's debt ratings are: S&P: A (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.

As part of its ongoing business, Canon does not participate in transactions that create 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 its employees, affiliates and other companies. The guarantees for the employees are principally made for their housing loans. The guarantees for affiliates and other companies are made for their lease obligations and bank loans to ensure that those companies operate with less financial risk.

Canon would have to perform under a guarantee if the borrower defaults on a payment within the contract terms. The contract terms are 1 year to 15 years in case of employees with housing loans, and 1 year to 5 years in case of affiliates and other companies with lease obligations and bank loans. The maximum amount of undiscounted payments Canon would have had to make in the event of default is ¥2,078 million at December 31, 2021. The carrying amounts of the liabilities recognized for Canon's obligations as a guarantor under those guarantees at December 31, 2021 were not significant.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following table summarizes Canon's contractual obligations at December 31, 2021.

		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:					
Loan from the banks	**174,000**	—	174,000	—	—
Other debt	**7,040**	1,290	1,529	654	3,567
Operating lease obligations	**100,519**	32,941	37,738	18,648	11,192
Purchase commitments for:					
Property, plant and equipment	**76,229**	76,229	—	—	—
Parts and raw materials	**249,909**	249,909	—	—	—
Other long-term liabilities:					
Contribution to defined benefit pension plans	**34,107**	34,107	—	—	—
Total	**641,804**	394,476	213,267	19,302	14,759

Note: See Note 9, 11, 19 and 20 in the Notes to Consolidated Financial Statements for further details. 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 12, Income Taxes in the Notes to Consolidated Financial Statements for further details.

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 recorded at the time revenue is 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, 2021 accrued product warranty costs are included in accrued expenses and amounted to ¥16,949 million.

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.

Canon's management policy in recent periods to optimize inventory levels is intended to maintain an appropriate balance among relevant imperatives, including minimizing working capital, avoiding undue exposure to the risk of inventory obsolescence, and maintaining the ability to sustain sales despite the occurrence of unexpected disasters.

Canon's total inventory turnover measured in days were 66, 60, and 59 days at the end of the fiscal years 2021, 2020, and 2019, respectively. The inventory turnover in 2021 increased due to an increase in inventories of products in process at plants and in transit to dealers, in order to focus on recovering production from product supply shortages resulting from parts procurement difficulties and reduced operating rates at production sites.

Canon is committed to cash flow management in order to strengthen its financial base. While actively investing to expand its business performance, Canon is also ensuring stable free cash flow by keeping total capital investments within the range of depreciation and amortization.

Increase in property, plant and equipment on an accrual basis in 2021 amounted to ¥151,914 million compared with ¥132,302 million in 2020 and ¥178,088 million in 2019. For 2022, Canon projects its increase in property, plant and equipment will be approximately ¥180,000 million.

Employer contributions to Canon's worldwide defined benefit pension plans were ¥43,782 million in 2021, ¥26,965 million in 2020 and ¥30,383 million in 2019. Employer contributions to Canon's worldwide defined contribution pension plans were ¥22,660 million in 2021, ¥16,334 million in 2020, and ¥17,414 million in 2019. In addition, employer contributions to the multiemployer pension plan of certain subsidiaries were ¥4,822 million in 2021, ¥4,224 million in 2020 and ¥4,321 million in 2019.

Working capital in 2021 increased by ¥354,558 million to ¥817,512 million, compared with ¥462,954 million in 2020 and ¥873,962 million in 2019. The increase was primarily due to a decrease in short-term loans (including the current portion of long-term debt) and an increase in inventories. 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 2021 was 1.77 compared to 1.35 for 2020 and to 1.90 for 2019.

Return on assets (net income attributable to Canon Inc. divided by the average of total assets) was 4.6% in 2021, compared to 1.8% in 2020 and 2.6% in 2019. It improved from the previous fiscal year due to an increase in net income as a result of improved business performance.

Return on Canon Inc. shareholders' equity (net income attributable to Canon Inc. divided by the average of total Canon Inc. shareholders' equity) was 7.9% in 2021 compared with 3.2% in 2020 and 4.5% in 2019. It improved from the previous fiscal year due to a significantly increase in net income as a result of improved business performance, although shareholders' equity increased due to an increase in retained earnings resulting from an increase in profit and an increase in foreign currency translation adjustments resulting from the depreciation of the yen.

In Phase VI, one of Canon's management policies is to thoroughly implement cash flow management, and Canon is restrengthening its financial base.

In fiscal 2021, loans decreased by ¥170,000 million due to the refinancing and the repayment of loans which was provided for the acquisition of Toshiba Medical Systems Corporation (currently, Canon Medical Systems Corporation). As a result, **the debt to total assets ratios** were 6.8%, 10.9% and 10.8% as of December 31, 2021, 2020 and 2019, respectively. Canon had short-term loans, current operating lease liabilities, long-term debt, and noncurrent operating lease liabilities of ¥320,971 million as of December 31, 2021, ¥506,172 million as of December 31, 2020 and ¥514,946 million as of December 31, 2019.

Canon Inc. shareholders' equity to total assets ratios were 60.5%, 55.7% and 56.3% as of December 31, 2021, 2020 and 2019, respectively. Canon strengthened its financial base by reducing debt through an increase in other retained earnings due to an increase in profit and a decrease in long-term debt due to strict cash flow management.

Non-GAAP Financial Measures

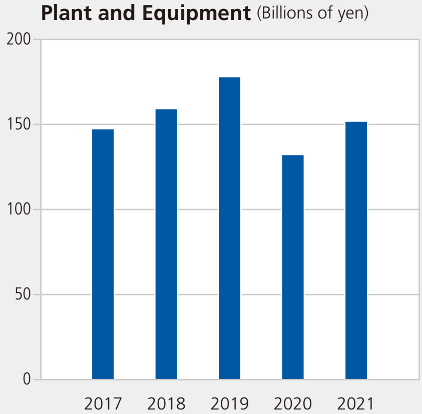
Canon has reported its financial results in accordance with U.S. GAAP. In addition, Canon has discussed its results using the combination of two GAAP cash flow measures, Net cash provided by operating activities and Net cash used for investing activities, which Canon refers to as "Free Cash Flow" which is a non-GAAP measure. Canon believes this measure is beneficial to an investor's understanding of its current liquidity and the alternatives of uses of financing activities because it takes into consideration its operating and investing activities.

A reconciliation of this non-GAAP financial measure and the most directly comparable measure calculated and presented in accordance with GAAP is set forth on the following table.

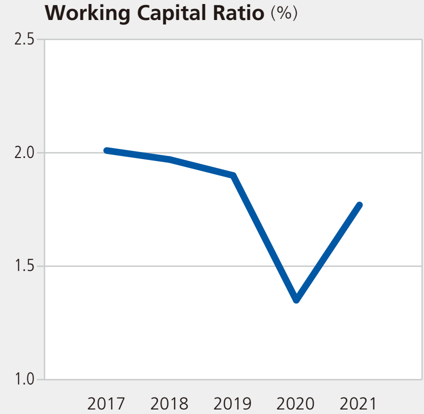
FREE CASH FLOW

	Millions of yen	
	2021	2020
Net cash provided by operating activities	**451,028**	333,805
Net cash used in investing activities	**(207,256)**	(155,439)
Free cash flow	**243,772**	178,366

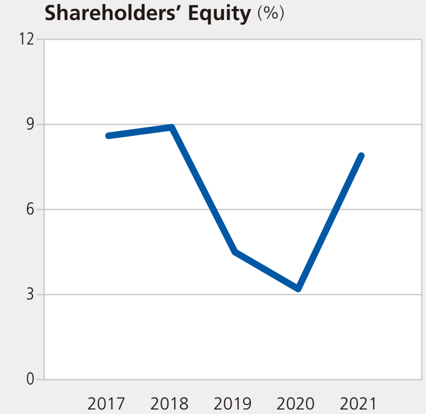
Increase in Property, Plant and Equipment (Billions of yen)



Working Capital Ratio (%)



Return on Canon Inc. Shareholders' Equity (%)



RESEARCH AND DEVELOPMENT, PATENTS AND LICENSES

Since its founding, Canon has diversified its business and increased its competitiveness by developing and diversifying core competence management that comprises various core competence technologies ("core technologies") to create industry-leading core products, fundamental technologies that form the basis of technology accumulation and basic technologies for value which are technology and expertise that support the Canon brand accumulated during the company's growth and the basis of commercialization technology. Canon's key R&D strategies are as follows:

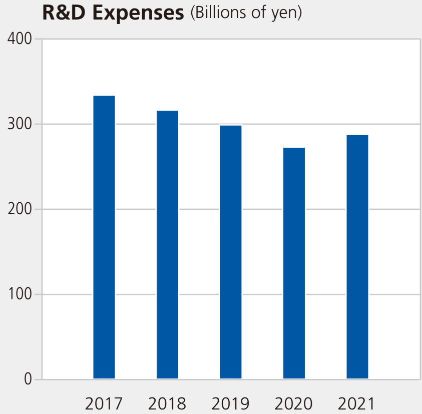
- Reinforce fundamental technologies and value creation technologies
- Create future businesses based on strong core technologies and fundamental technologies
- Enhance innovation-type R&D in response to the demands of the current age

Canon strives to implement the above R&D strategies as follows:

- ***Reinforce fundamental technologies and value creation technologies:***
  Contribute to higher efficiency of existing businesses by further evolving value creation technologies. Alongside this, extract the essence of a wide range of core technologies possessed by existing businesses, deepen fundamental technologies and inject them into core technologies of new businesses. In doing so, Canon will further strengthen the competitiveness of existing businesses and growing new businesses.

- ***Create future businesses based on strong core technologies and fundamental technologies:***
  Promote development of new business areas through technology diversification. For example, Canon will develop devices that utilize materials technology –the foundation of ink and toner materials– as well as materials with unique properties, and work on development of next-generation technologies that lead to business creation.

R&D Expenses (Billions of yen)



- ***Enhance innovation-type R&D in response to the demands of the current age:***
  Build upon trends such as DX and carbon neutrality, promote R&D that leads to corporate value improvement. In particular, focus on cyber-physical systems that closely integrate cyberspace, which enables the combination of various services, with physical (real world) space, the point of contact with people. Create various innovations by developing cyber-physical business models and products that stay one step ahead through developing advanced cyber technology with utilizing world-class core technologies in the physical field and business alliances.

R&D expenses were ¥287,338 million in fiscal 2021 and ¥272,312 million in fiscal 2020. The R&D expenses to net sales ratios were 8.2% in fiscal 2021 and 8.6% in fiscal 2020.

Canon believes that new products protected by a robust patent portfolio will not easily allow competitors to surpass them, and will give the company an advantage in establishing standards in the market and industry.

Canon obtained the third greatest number of patents in the United States in 2021, according to the annual ranking list, released by IFI CLAIMS® Patent Services.

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 risk 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 were as follows at December 31, 2021.

	Millions of yen
	Fair value
Fund trusts and others	609
Equity securities	28,640
	29,249

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 as of December 31, 2021. All of the foreign exchange contracts described in the following table have a contractual maturity date in 2022.

Millions of yen	U.S.$	Euro	Others	Total
Forwards to sell foreign currencies:				
Contract amounts	78,776	80,847	9,769	169,392
Estimated fair value	(1,014)	(545)	(93)	(1,652)
Forwards to buy foreign currencies:				
Contract amounts	19,550	897	7,006	27,453
Estimated fair value	99	3	(504)	(402)

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 9 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 in the same period as the hedged items affect earnings. Substantially all amounts recorded in accumulated other comprehensive income (loss) as of December 31, 2021 are expected to be recognized in net sales over the next twelve months. 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.

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

Under the corporate philosophy of kyosei—living and working together for the common good—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 corporation targeting continued growth and development.

Based on this basic management policy, Canon launched the Excellent Global Corporation Plan in 1996 and, from Phase I to Phase V, has worked to strengthen its management base and improve corporate value. In 2021, Canon started Phase VI of the "Excellent Global Corporation Plan," and under the basic policy to "accelerate our corporate portfolio transformation by improving productivity and creating new businesses," Canon reorganized our business divisions and group companies into four industry-oriented business groups of "Printing," "Imaging," "Medical" and "Industrial" in order to further promote the transformation of the business portfolio whose foundation was established in Phase V (from 2016 to 2020). Canon also launched a new organization to accelerate the commercialization of, among others, materials business and sales of components such as sensors to outside businesses.

During 2021, which was the first year of Phase VI, many production sites of Canon closed temporarily due to lockdowns as the global spread of COVID-19 infections continued without being contained. Canon was also forced to reduce production due to shortages of materials, mainly for semiconductors, and logistics disruptions. However, because economic activities resumed with increased availability of vaccinations, Canon was able to achieve an increase in both sales and profits through responding to a recovery in demand.

In 2022, although there are still no projections as to when COVID-19 will be brought under control and disruptions in production and logistics are expected to continue, Canon believes that the fundamentals of its business environment are sound and have not changed from 2021. Accordingly, under the basic policy of Phase VI that has been carried out since 2021, Canon will focus on the following measures.

1. Further strengthen competitiveness of industry-oriented business groups

While creating new businesses by combining technologies, regrouping the business domains, and utilizing M&A and other measures for each industry-oriented business group, as well as by strengthening the functions of development, production, and sales framework, Canon will thoroughly enhance business competitiveness.

(1) Printing Group

In the age of DX, although the shift to paperless documents will continue in the future given the fact the volume of printed pages at offices is being reduced as much as possible, printing demand is expected to remain based on the needs to share ideas and work results on hard copies. Due to the spread of COVID-19, the adoption of hybrid working styles that combine office work with teleworking is accelerating and there are demands to utilize cloud computing, etc. for providing printing environments and services not limited to a certain workplace. Canon aims to be global No. 1 in the office and home printing field by utilizing two digital printing technologies, namely electrophotographic technology as well as inkjet technology, and the strengths of its worldwide sales and service network, and by focusing on providing printing solutions that meet the needs of the DX era.

In addition, in the fields of catalog printing and other commercial printing and label printing, package printing and other industrial printing where there is expected to be a further shift from analog to digital in the future, Canon will take this opportunity to enhance workflow software that contributes to workload savings and supports increases in added value, as well as to introduce new competitive products to the market continuously utilizing the collective strengths of the entire group and establish a strong position.

(2) Imaging Group

Although the overall market for digital cameras has shrunk significantly due to the widespread use of smartphones, sales of mirrorless cameras equipped with full-frame sensors were strong even during the spread of COVID-19 infections and demand for high image quality photos was steady. As a company with the world's leading optical technology, Canon will continue to introduce cameras and interchangeable lenses to the market continuously in response to this demand, and establish its position as global No. 1 for mirrorless cameras by focusing on professional photographers and advanced amateurs who value "high image quality." In addition, given the increasing use and application of virtual reality images, 3D images and 360° images in various fields recently, Canon is working to capture these new video-experience markets using the Free Viewpoint Video System, the EOS VR System, which was introduced in 2021, and MREAL, etc., in order to expand the business.

In the field of broadcasting and video production, Canon will strengthen its lineup of high image quality remote camera systems in line with the continuing increase in IP streaming demand.

In the field of network cameras, Canon will strengthen its presence in the security domain, including for smart cities, utilizing the collective strength of the entire group, which includes Axis, one of the world's leading manufacturers of network cameras, Milestone Systems, a video management software vendor, and BriefCam, a video analytics software vendor. At the same time, for quality assurance work at production sites, out-of-stock detection at distribution centers, crowd level detection at shops and exhibition sites and other such uses which goes beyond the original scope of security, Canon is working on developing products and services that provide DX solutions using video for various operations.

In the field of mobility which is undergoing tremendous changes, such as the emergence of self-driving vehicles, Canon is working on entering the car camera and traffic infrastructure businesses by leveraging the optical and network technology that Canon has been developing through its long history, and will contribute to the widespread use of driving support and other mobility services.

(3) Medical Group

In order to respond to medical treatments that are becoming more advanced, Canon will expand the business domains to include healthcare IT and in vitro diagnostics with the diagnostic imaging business as the core, aiming to contribute to medical treatments around the world.

In the diagnostic imaging business, Canon will liaise with Redlen, which was acquired in 2021, in order to promote development of PCCT technology that makes it possible to achieve both unprecedented diagnostic functions and a significant reduction in radiation exposure, and are focused on early commercialization. In addition, by using Quality Electrodynamics's RF coil technology, which is a core technology for MRI systems, and other original technologies of the group companies, as well as by applying image-processing technologies, etc. that utilize AI, Canon will develop the next-generation high-performance MRI systems. In diagnostic ultrasound systems, Canon will work to reduce costs by standardizing platforms, bringing production in-house and utilizing Canon's production technology. Furthermore, by strengthening the sales network, with a particular focus on the United States, Canon aims to have the No. 1 global market share for CT systems and become one of the global leading companies for other diagnostic imaging systems.

In the healthcare IT field, by enabling medical institutions to integrate image and non-image data collected in clinical settings, analyze and process the data utilizing AI and other technologies and provide the data worldwide, Canon aims to offer high-quality diagnostic support and facilitate efficient medical treatments. In addition, in the in vitro diagnostics field, Canon will expand the portfolio into domains related to diagnostic equipment, such as test reagents for COVID-19, and expand the business.

In the component business, Canon will expand the existing business by capturing new customers, consolidating sales functions etc., and while also looking at growth opportunities through M&A, Canon will offer multi-layered solutions, comprised of finished goods, modules, processes, services etc., aiming to expand the BtoB business, whose sales account for 10% or more of the total sales of the Medical Group.

(4) Industrial Group

Given the widespread use of the 5G communications standard and cloud computing, demand for semiconductors, such as IC and memory chips, is expected to continue growing in the future. In addition, due to the increase in individualized listening, viewing and learning using online distribution and the shift to images with higher resolution, demand for LCD panels and OLED panels is expected to be strong. Production of Canon's semiconductor manufacturing equipment, FPD lithography equipment and OLED display manufacturing equipment is continuing at almost full capacity. Recognizing that our ability to respond flexibly to increased demand is an important issue, Canon will enhance the production system utilizing the collective strength of the entire group and strengthen our customer support system. In addition, Canon will improve the products by raising the performance of those products and introduce additional functions that contribute to improving customer productivity, and work to expand its market share.

Concurrently, Canon will accelerate the technological developments with a view to expanding the application of nanoimprint lithography technology, aiming for early commercialization, and focus on establishing next-generation manufacturing technology for OLED panels. Furthermore, Canon will create new products and services that combine core technologies in the group, such as ultra-precision positioning, ultra-precision processing and vacuum systems, and aim to expand the business domains by providing its customers with new values.

2. Improve group-wide productivity through extensive reinforcement of Canon's global headquarter functions

Canon will reaffirm its commitment to be fully focused on cash flow management across the entire group and further strengthen its financial base. In Japan, Canon will improve the productivity of its employees including administrative staff by reallocating headcounts to growth areas in response to the changes in the business portfolio and promote highly streamlined work using DX and other measures. In addition, in order to rebuild the production system to create a resilient system integrated across the group, Canon is working to further increase automation and in house production in all businesses through collaborative measures to expand production technologies, and will continue striving to achieve thorough cost reductions.

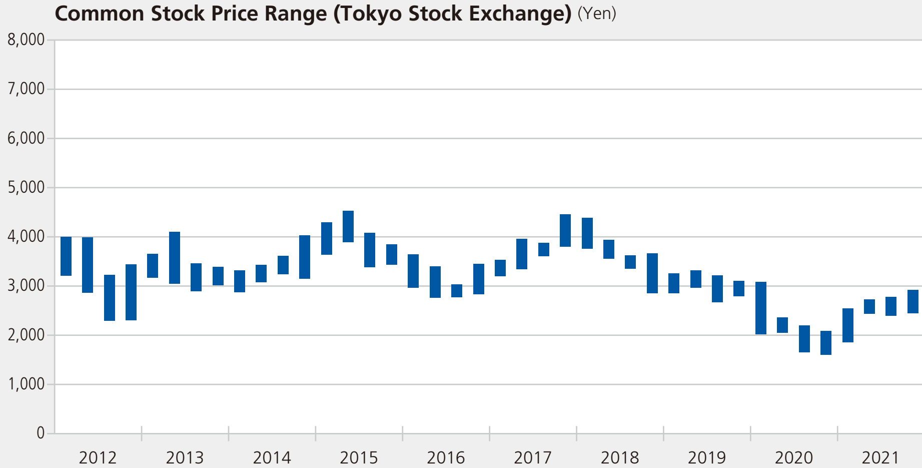
Forward looking statements

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. Despite the resurgence of COVID-19 infections due to new variants, economic activities have resumed and continued to recover due to the progress of vaccination programs. However, if the transmission further expands and is prolonged, it could lead to a slowdown of the world economy and the business of Canon, a slowdown in the business of Canon's customers, suppliers and partners and lower investment sentiment for those parties. A detailed description of these and other risk factors is included in our annual report on Form 20-F, which is on file with the United States Securities and Exchange Commission.

TEN-YEAR FINANCIAL SUMMARY

	Millions of yen (except per share amounts)			
	2021	2020	2019	2018
Net sales:				
Domestic	**830,378**	806,305	872,534	869,577
Overseas	**2,682,979**	2,353,938	2,720,765	3,082,360
Total	**3,513,357**	3,160,243	3,593,299	3,951,937
Percentage of previous year	**111.2%**	87.9%	90.9%	96.9%
Net income attributable to Canon Inc.	**214,718**	83,318	124,964	252,441
Percentage of sales	**6.1%**	2.6%	3.5%	6.4%
Advertising	**36,812**	31,273	46,665	58,729
Research and development expenses	**287,338**	272,312	298,503	315,842
Depreciation and amortization	**221,246**	227,825	237,327	251,554
Capital expenditure	**179,000**	161,727	211,228	200,504
Long-term debt, excluding current installments	**179,750**	4,834	357,340	361,962
Canon Inc. shareholders' equity	**2,873,773**	2,575,031	2,685,496	2,820,644
Total assets	**4,750,888**	4,625,614	4,771,918	4,902,955
Per share data:				
Net income attributable to Canon Inc. shareholders per share:				
Basic	**205.35**	79.37	116.79	233.80
Diluted	**205.29**	79.35	116.77	233.78
Dividend per share	**100.00**	80.00	160.00	160.00
Stock price:				
High	**2,938**	3,099	3,338	4,395
Low	**1,876**	1,627	2,688	2,877
Average number of common shares in thousands	**1,045,633**	1,049,802	1,069,957	1,079,753
Number of employees	**184,034**	181,897	187,041	195,056

Common Stock Price Range (Tokyo Stock Exchange) (Yen)



						Thousands of U.S. dollars (except per share amounts)
2017	2016	2015	2014	2013	2012	**2021**
884,828	706,979	714,280	724,317	715,863	720,286	**$ 7,220,678**
3,195,187	2,694,508	3,085,991	3,002,935	3,015,517	2,759,502	**23,330,252**
4,080,015	3,401,487	3,800,271	3,727,252	3,731,380	3,479,788	**30,550,930**
119.9%	89.5%	102.0%	99.9%	107.2%	97.8%	**111.2%**
242,081	150,334	219,943	254,627	229,829	224,854	**1,867,113**
5.9%	4.4%	5.8%	6.8%	6.2%	6.5%	**6.1%**
61,207	58,707	80,907	79,765	86,398	83,134	**320,104**
333,371	306,537	332,678	311,896	307,500	296,281	**2,498,591**
261,881	250,096	273,327	263,480	275,173	258,133	**1,923,878**
181,389	208,379	243,130	224,760	227,478	306,661	**1,556,522**
493,238	611,289	881	1,148	1,448	2,117	**$ 1,563,043**
2,863,986	2,776,327	2,959,929	2,971,963	2,904,212	2,592,630	**24,989,330**
5,201,626	5,142,279	4,431,720	4,464,854	4,246,796	3,959,542	**41,312,070**
223.03	137.66	201.41	228.88	200.21	191.59	**$ 1.79**
223.03	137.66	201.40	228.88	200.21	191.58	**1.79**
160.00	150.00	150.00	150.00	130.00	130.00	**0.87**
4,472	3,656	4,539	4,045	4,115	4,015	**25.55**
3,218	2,780	3,402	2,889	2,913	2,308	**16.31**
1,085,439	1,092,071	1,092,018	1,112,510	1,147,934	1,173,648	
197,776	197,673	189,571	191,889	194,151	196,968	

Notes: 1. U.S. dollar amounts are translated from yen at the rate of U.S.$1 = JPY115, the approximate exchange rate on the Tokyo Foreign Exchange Market as of December 30, 2021.

2. Canon adopted Accounting Standards Update (“ASU”) No. 2017-07 from the quarter beginning January 1, 2018. The adoption of the new presentation requirement of the service cost component and the other components of net benefit cost resulted in reclassification from cost of sales, and selling, general and administrative expenses, and research and development expenses into other income (deductions) for the years ended December 31 from 2017 to 2012 respectively.

3. Certain figures for the fiscal years ended December 31, 2019, 2018 and 2017 presented in the table above have been revised from the versions previously disclosed. During the year ended December 31, 2020, Canon corrected an immaterial error in its previously issued consolidated financial statements related to accounting for the Company’s and domestic subsidiaries’ compensated absence carryforward as disclosed in the previous fiscal year. For further details, please refer to Note 1 (y) of the Notes to Consolidated Financial Statements.

4. Depreciation and amortization and Capital expenditure are the total of tangible and intangible assets.

CONSOLIDATED BALANCE SHEETS

Canon Inc. and Subsidiaries
December 31, 2021 and 2020

	Millions of yen	
ASSETS	**2021**	2020
Current assets:		
Cash and cash equivalents (Note 1)	**401,395**	407,684
Short-term investments (Note 2)	**3,377**	71
Trade receivables (Note 3)	**522,432**	546,771
Inventories (Note 4)	**650,568**	562,807
Prepaid expenses and other current assets (Notes 6, 15 and 18)	**314,489**	284,556
Allowance for credit losses (Notes 3 and 6)	**(13,916)**	(12,746)
Total current assets	**1,878,345**	1,789,143
Noncurrent receivables (Note 20)	**16,388**	17,276
Investments (Notes 2 and 22)	**60,967**	49,994
Property, plant and equipment, net (Notes 5 and 6)	**1,041,403**	1,037,680
Operating lease right-of-use assets (Note 19)	**95,791**	107,361
Intangible assets, net (Notes 7 and 8)	**301,793**	318,497
Goodwill (Notes 7 and 8)	**953,850**	915,564
Other assets (Notes 6, 11 and 12)	**404,720**	392,066
Allowance for credit losses (Note 6)	**(2,369)**	(1,967)
Total assets	**4,750,888**	4,625,614

LIABILITIES AND EQUITY		
Current liabilities:		
Short-term loans and current portion of long-term debt (Notes 1 and 9)	**44,891**	392,235
Short-term loans related to financial services	**42,300**	45,000
Other short-term loans and current portion of long-term debt	**2,591**	347,235
Trade payables (Note 10)	**338,604**	303,809
Accrued income taxes (Note 12)	**43,081**	18,761
Accrued expenses (Notes 11 and 20)	**323,929**	317,716
Current operating lease liabilities (Note 19)	**30,945**	32,307
Other current liabilities (Notes 5, 15 and 18)	**279,383**	261,361
Total current liabilities	**1,060,833**	1,326,189
Long-term debt, excluding current installments (Notes 9 and 21)	**179,750**	4,834
Accrued pension and severance cost (Note 11)	**248,467**	345,897
Noncurrent operating lease liabilities (Note 19)	**65,385**	76,796
Other noncurrent liabilities (Notes 12 and 15)	**98,024**	87,857
Total liabilities	**1,652,459**	1,841,573
Equity:		
Canon Inc. shareholders' equity:		
Common stock		
Authorized 3,000,000,000 shares; issued 1,333,763,464 shares in 2021 and 2020	**174,762**	174,762
Additional paid-in capital (Note 13)	**403,119**	404,620
Legal reserve (Note 13)	**68,015**	69,436
Retained earnings (Note 13)	**3,538,037**	3,409,371
Accumulated other comprehensive income (loss) (Note 14)	**(151,794)**	(324,789)
Treasury stock, at cost; 287,991,705 shares in 2021 and 287,989,819 shares in 2020	**(1,158,366)**	(1,158,369)
Total Canon Inc. shareholders' equity	**2,873,773**	2,575,031
Noncontrolling interests	**224,656**	209,010
Total equity	**3,098,429**	2,784,041
Total liabilities and equity	**4,750,888**	4,625,614

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME

Canon Inc. and Subsidiaries
Years ended December 31, 2021, 2020 and 2019

	Millions of yen		
	2021	2020	2019
Net sales (Notes 6, 15 and 18)			
Products and Equipment	**2,804,680**	2,489,829	2,835,428
Services	**708,677**	670,414	757,871
	3,513,357	3,160,243	3,593,299
Cost of sales (Notes 5, 8, 11 and 19)			
Products and Equipment	**1,552,766**	1,463,637	1,627,858
Services	**332,799**	320,738	355,408
	1,885,565	1,784,375	1,983,266
Gross profit	**1,627,792**	1,375,868	1,610,033
Operating expenses (Notes 1, 5, 8, 11, 16, 19 and 20):			
Selling, general and administrative expenses	**1,058,536**	993,009	1,137,110
Research and development expenses	**287,338**	272,312	298,503
	1,345,874	1,265,321	1,435,613
Operating profit	**281,918**	110,547	174,420
Other income (deductions):			
Interest and dividend income	**2,232**	2,923	5,526
Interest expense	**(647)**	(854)	(1,038)
Other, net (Notes 1, 2, 7, 11, 14 and 18)	**19,203**	17,664	16,585
	20,788	19,733	21,073
Income before income taxes	**302,706**	130,280	195,493
Income taxes (Note 12)	**71,866**	34,337	56,146
Consolidated net income	**230,840**	95,943	139,347
Less: Net income attributable to noncontrolling interests	**16,122**	12,625	14,383
Net income attributable to Canon Inc.	**214,718**	83,318	124,964
	Yen		
Net income attributable to Canon Inc. shareholders per share (Note 17):			
Basic	**205.35**	79.37	116.79
Diluted	**205.29**	79.35	116.77

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Canon Inc. and Subsidiaries
Years ended December 31, 2021, 2020 and 2019

	Millions of yen		
	2021	2020	2019
Consolidated net income	**230,840**	95,943	139,347
Other comprehensive income (loss), net of tax (Note 14):			
Foreign currency translation adjustments	**120,439**	(17,354)	(32,157)
Net gains and losses on derivative instruments	**(972)**	970	(1,068)
Pension liability adjustments	**56,508**	1,382	(3,630)
	175,975	(15,002)	(36,855)
Comprehensive income (loss)	**406,815**	80,941	102,492
Less: Comprehensive income attributable to noncontrolling interests	**19,102**	13,961	16,353
Comprehensive income (loss) attributable to Canon Inc.	**387,713**	66,980	86,139

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF EQUITY

Canon Inc. and Subsidiaries

Years ended December 31, 2021, 2020 and 2019

	Millions of yen									
	Common stock	Additional paid-in capital	Legal reserve	Other retained earnings	Total retained earnings	Accumulated other comprehensive income (loss)	Treasury stock	Total Canon Inc. shareholders' equity	Non-controlling interests	Total equity
Balance at December 31, 2018	174,762	404,389	67,116	3,501,950	3,569,066	(269,071)	(1,058,502)	2,820,644	189,501	3,010,145
Cumulative effects of accounting standard update—adoption of ASU No. 2017-12				122	122	(122)		—	—	—
Equity transactions with noncontrolling interests and other		641				(424)		217	(1,813)	(1,596)
Dividends to Canon Inc. shareholders (160.00 yen per share)				(171,487)	(171,487)			(171,487)		(171,487)
Dividends to noncontrolling interests									(5,557)	(5,557)
Transfers to legal reserve			456	(456)	—			—		—
Comprehensive income:										
Net income				124,964	124,964			124,964	14,383	139,347
Other comprehensive income (loss), net of tax (Note 14):										
Foreign currency translation adjustments						(32,043)		(32,043)	(114)	(32,157)
Net gains and losses on derivative instruments						(1,073)		(1,073)	5	(1,068)
Pension liability adjustments						(5,709)		(5,709)	2,079	(3,630)
Total comprehensive income (loss)								86,139	16,353	102,492
Repurchases and reissuance of treasury stock		(13)		(10)	(10)		(49,994)	(50,017)		(50,017)
Balance at December 31, 2019	174,762	405,017	67,572	3,455,083	3,522,655	(308,442)	(1,108,496)	2,685,496	198,484	2,883,980
Cumulative effects of accounting standard update—adoption of ASU No. 2016-13				(159)	(159)			(159)	—	(159)
Equity transactions with noncontrolling interests and other		(316)				(9)	(15)	(340)	1,091	751
Dividends to Canon Inc. shareholders (120.00 yen per share)				(126,938)	(126,938)			(126,938)		(126,938)
Dividends to noncontrolling interests									(4,526)	(4,526)
Transfers to legal reserve			1,864	(1,864)	—			—		—
Comprehensive income:										
Net income				83,318	83,318			83,318	12,625	95,943
Other comprehensive income (loss), net of tax (Note 14):										
Foreign currency translation adjustments						(17,355)		(17,355)	1	(17,354)
Net gains and losses on derivative instruments						987		987	(17)	970
Pension liability adjustments						30		30	1,352	1,382
Total comprehensive income (loss)								66,980	13,961	80,941
Repurchases and reissuance of treasury stock		(81)		(69)	(69)		(49,858)	(50,008)		(50,008)
Balance at December 31, 2020	174,762	404,620	69,436	3,409,371	3,478,807	(324,789)	(1,158,369)	2,575,031	209,010	2,784,041
Equity transactions with noncontrolling interests and other		(62)						(62)	1,725	1,663
Dividends to Canon Inc. shareholders (85.00 yen per share)				(88,891)	(88,891)			(88,891)		(88,891)
Dividends to noncontrolling interests									(5,181)	(5,181)
Transfers to legal reserve		(1,429)	(1,421)	2,850	1,429			—		—
Comprehensive income:										
Net income				214,718	214,718			214,718	16,122	230,840
Other comprehensive income (loss), net of tax (Note 14):										
Foreign currency translation adjustments						119,165		119,165	1,274	120,439
Net gains and losses on derivative instruments						(994)		(994)	22	(972)
Pension liability adjustments						54,824		54,824	1,684	56,508
Total comprehensive income (loss)								387,713	19,102	406,815
Repurchases and reissuance of treasury stock		(10)		(11)	(11)		3	(18)		(18)
Balance at December 31, 2021	174,762	403,119	68,015	3,538,037	3,606,052	(151,794)	(1,158,366)	2,873,773	224,656	3,098,429

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Canon Inc. and Subsidiaries
Years ended December 31, 2021, 2020 and 2019

	Millions of yen		
	2021	2020	2019
Cash flows from operating activities:			
Consolidated net income	**230,840**	95,943	139,347
Adjustments to reconcile consolidated net income to net cash provided by operating activities:			
Depreciation and amortization	**221,246**	227,825	237,327
Loss on disposal of fixed assets	**7,745**	4,326	5,991
Deferred income taxes	**(9,826)**	(15,542)	(6,523)
Decrease in trade receivables	**44,678**	15,120	43,504
(Increase) decrease in inventories	**(61,017)**	16,075	19,895
Increase (decrease) in trade payables	**52,138**	(4,636)	(35,509)
Increase (decrease) in accrued income taxes	**24,017**	43	(22,279)
(Decrease) increase in accrued expenses	**(8,673)**	(16,413)	9,738
Decrease in accrued pension and severance cost	**(41,477)**	(16,601)	(13,722)
Other, net (Note 6)	**(8,643)**	27,665	(19,308)
Net cash provided by operating activities	**451,028**	333,805	358,461
Cash flows from investing activities:			
Purchases of fixed assets (Note 5)	**(177,350)**	(164,719)	(215,671)
Proceeds from sale of fixed assets (Note 5)	**3,796**	7,815	885
Purchases of held-to-maturity securities	**(2,216)**	—	—
Purchases of securities	**(2,162)**	(592)	(4,907)
Proceeds from sale and maturity of securities	**1,714**	558	828
Acquisitions of businesses, net of cash acquired (Note 7)	**(31,751)**	(127)	(8,880)
Other, net	**713**	1,626	(823)
Net cash used in investing activities	**(207,256)**	(155,439)	(228,568)
Cash flows from financing activities:			
Proceeds from issuance of long-term debt (Note 9)	**175,100**	2,100	—
Repayments of long-term debt (Note 9)	**(347,029)**	(11,095)	(8,678)
(Decrease) increase in short-term loans related to financial services, net (Note 9)	**(2,700)**	5,100	5,200
Dividends paid	**(88,891)**	(126,938)	(171,487)
Repurchases and reissuance of treasury stock, net	**(17)**	(50,008)	(50,012)
Other, net	**(3,829)**	(2,608)	(7,613)
Net cash used in financing activities	**(267,366)**	(183,449)	(232,590)
Effect of exchange rate changes on cash and cash equivalents	**17,305**	(47)	(5,134)
Net change in cash and cash equivalents	**(6,289)**	(5,130)	(107,831)
Cash and cash equivalents at beginning of year	**407,684**	412,814	520,645
Cash and cash equivalents at end of year	**401,395**	407,684	412,814
Supplemental disclosure for cash flow information:			
Cash paid during the year for:			
Interest	**599**	1,028	888
Income taxes	**71,573**	45,471	77,654

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 its subsidiaries (collectively "Canon") is one of the world's leading manufacturers of office multi-function devices ("MFDs"), laser printers, inkjet printers, cameras, medical equipment and lithography equipment. Products of the Printing Business Unit consist mainly of office MFDs, document solutions, laser multifunction printers ("MFPs"), laser printers, inkjet printers, image scanners, calculators, digital continuous feed presses, digital sheet-fed presses and large format printers. Products of the Imaging Business Unit consist mainly of interchangeable-lens digital cameras, interchangeable lenses, digital compact cameras, compact photo printers, network cameras, video management software, video content analytics software, digital camcorders, digital cinema cameras, broadcast equipment and multimedia projectors. Products of the Medical Business Unit consist mainly of computed tomography ("CT") systems, diagnostic ultrasound systems, diagnostic X-ray systems, magnetic resonance imaging ("MRI") systems, clinical chemistry analyzers, digital radiography systems and ophthalmic equipment. Products of the Industrial and Others Business Unit consist mainly of semiconductor lithography equipment, Flat Panel Display ("FPD") lithography equipment, Organic Light Emitting Diode ("OLED") display manufacturing equipment, vacuum thin-film deposition equipment, die bonders, handy terminals and document scanners. 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. Further segment information is described in Note 23.

Canon sells laser printers on an OEM basis to HP Inc.; such sales constituted 11.6%, 11.4% and 13.0% of consolidated net sales for the years ended December 31, 2021, 2020 and 2019, respectively, and are included in the Printing Business Unit.

Canon's manufacturing operations are conducted primarily at 29 plants in Japan and 13 overseas plants which are located in countries and regions such as the United States, Germany, France, the Netherlands, Taiwan, China, Malaysia, Thailand, Vietnam and Philippines.

(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 ("U.S. GAAP"). These adjustments were not recorded in the statutory books of account.

Canon has separated the presentation of allowance for credit losses from the related receivable balances which are included in trade receivables, prepaid expenses and other current assets, and other assets in the accompanying consolidated balance sheets, from 2021. Consolidated balance sheet for the year ended December 31, 2020 has also been reclassified.

Canon has also changed the presentation of "Short-term loans related to financial services" separated from "Short-term loans and current portion of long-term debt" in the consolidated balance sheets from 2021. Further, Canon has separated the presentation of "(Decrease) increase in short-term loans related to financial services, net" from "(Decrease) increase in short-term loans, net" and included the presentation of "(Decrease) increase in short-term loans, net" in "Cash flows from financing activities: Other, net" in the consolidated statements of cash flows from 2021. These changes were made to enhance the presentation of the Company's short-term borrowings for the users of the consolidated financial statements. To conform with the current year change in the presentation, the consolidated balance sheet for the year ended December 31, 2020 and the consolidated statement of cash flows for the years ended December 31, 2020 and 2019 have been reclassified.

(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 accounts including: revenue recognition, allowance for credit losses, inventories, long-lived assets, leases, goodwill and other intangible assets with indefinite useful lives, environmental liabilities, deferred tax assets, uncertain tax positions, employee retirement and severance benefit obligations and business combinations. Actual results could differ materially from those estimates. In addition, new waves of COVID-19 infections are being seen in some regions, and it is still difficult to predict when COVID-19 will be brought under control. However, each country and region continues to pursue both the infection control and economic activities. Actual results and outcomes may differ from management's estimates and assumptions due to risks and uncertainties, including uncertainty in the current economic environment triggered by COVID-19.

(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 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 were net losses of ¥21,746 million, ¥4,451 million and ¥4,236 million for the years ended December 31, 2021, 2020 and 2019, 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 ¥500 million at both December 31, 2021 and 2020, 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 equity securities and investments in affiliated companies.

Canon classifies investments in debt securities as held-to-maturity debt securities and available-for-sale securities. Canon does not hold any trading securities which are bought and held primarily for the purpose of sale in the near term. Canon reports investments with maturities of less than one year as short-term investments.

Available-for-sale debt securities and equity securities with readily determinable fair value that are not accounted for under the equity method are recorded at fair value which is determined based on quoted market prices, projected discounted cash flows or other valuation techniques as appropriate. The changes in fair value for equity securities are included in other, net in the consolidated statements of income. The changes in fair value for available-for-sale debt securities are included in net unrealized gains and losses on securities in the consolidated statements of comprehensive income.

Held-to-maturity debt securities are recorded at amortized cost. The fair values of equity securities are mainly measured at the quoted market price.

Available-for-sale debt 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 available-for-sale securities for which the declines are deemed to be other-than-temporary and there is no intent to sell, the impairment is separated into the amount related to credit loss, which is recognized in earnings and the amount related to all other factors is recognized in other comprehensive income (loss). For available-for-sale securities for which the declines are deemed to be other-than-temporary and there is an intent to sell, the impairment in its entirety is recognized in earnings. Canon recognizes an impairment loss to the extent the cost basis of the investment exceeds the fair value of the investment.

Canon measures non-marketable equity securities without readily determinable fair value at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for an identical or a similar investment of the same issuer.

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.

(h) Allowance for credit losses

Allowance for credit losses for trade and finance receivables is maintained for all customers based on ASC 326 "Financial Instruments – Credit Losses," considering various 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 net realizable 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 intangible assets 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 sum of 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, net

Property, plant and equipment are stated at cost less accumulated depreciation. 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.

(l) Leases

As for lessor accounting, Canon provides leasing arrangements to its customers primarily for the sale of office products. Revenue from the sale of these products under sales-type leases is recognized at the inception of the lease. Interest 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 product leases are bundled with maintenance contracts, revenue is allocated based upon the estimated standalone selling prices of the lease and non-lease components. Lease components generally include product and financing while non-lease components generally consist of maintenance contracts and supplies. Some of the contracts include options to extend or to terminate the lease. Canon takes such options into account to determine the lease term when it is reasonably certain that customers will exercise these options. The majority of Canon's lease contracts do not contain bargain purchase options for their customers. 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 50 years.

As for lessee accounting, Canon has operating and finance leases for various assets including office buildings, warehouses, employees' accommodations, and vehicles. Canon determines if an arrangement is a lease at the inception of each contract. Some of the contracts include options to extend or to terminate the lease. Canon takes such options into account to determine the lease term when it is reasonably certain that it will exercise these options. Canon's lease arrangements do not contain material residual value guarantees or material restrictive covenants. As a rate implicit in the most of Canon's leases cannot be determined, Canon uses incremental borrowing rates based on the information available at commencement to determine the present values of lease payments. Canon has lease contracts with lease and non-lease components, which are accounted for separately. Canon allocates the consideration in the lease contract to the lease and non-lease components based upon the estimated standalone prices. Costs associated with operating lease assets are recognized on a straight-line basis over the term of the lease.

(m) 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. 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 recognizes an impairment charge in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit.

Intangible assets with finite useful lives consist primarily of software, trademarks, patents and developed technology, license fees and customer relationships, which are amortized using the straight-line method. The estimated useful lives of software are from 3 years to 8 years, trademarks are 15 years, patents and developed technology are from 5 years to 21 years, license fees are 8 years, and customer relationships are from 7 years to 15 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 capitalizes the cost which was incurred subsequent to the stage of assuring the technological feasibility of the software for marketing purposes either developed or acquired.

(n) 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, and are included in other noncurrent liabilities in the consolidated balance sheets. Such liabilities are adjusted as further information develops or circumstances change. Costs of future obligations are not discounted to their present values.

(o) 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.

(p) 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.

(q) Net Income Attributable to Canon Inc. Shareholders per Share

Basic net income attributable to Canon Inc. shareholders 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. shareholders per share includes the effect from potential issuances of common stock based on the assumptions that all stock options were exercised.

(r) Revenue Recognition

Canon generates revenue through the sale of products of the Printing Business Unit, the Imaging Business Unit, the Medical Business Unit and the Industrial and Others Business Unit, supplies and related services under separate contractual arrangements. Revenue is recognized when, or as, control of promised goods or services transfers to customers in an amount that reflects the consideration to which Canon expects to be entitled in exchange for transferring these goods or services. For further information, please refer to Note 15.

(s) Research and Development Costs

Research and development costs are expensed as incurred.

(t) Advertising Costs

Advertising costs are expensed as incurred. Advertising expenses were ¥36,812 million, ¥31,273 million and ¥46,665 million for the years ended December 31, 2021, 2020 and 2019, respectively.

(u) Shipping and Handling Costs

Shipping and handling costs totaled ¥53,347 million, ¥47,721 million and ¥51,718 million for the years ended December 31, 2021, 2020 and 2019, respectively, and are included in selling, general and administrative expenses in the consolidated statements of income.

(v) 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, and reclassified in the same income statement line item in which the earnings effect of the hedged item is reported.

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.

(w) Guarantees

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

(x) Recent Accounting Guidance

Canon evaluates all recently issued accounting pronouncements applicable to its consolidated financial statements. No new accounting pronouncement issued or effective has had, or is expected to have, a material impact on Canon's consolidated financial statements.

(y) Correction of an Immaterial Error

During the year ended December 31, 2020, Canon corrected an error in its previously issued consolidated financial statements related to accounting for the Company and domestic subsidiaries' compensated absence carryforward in accordance with ASC 710 "Compensation." In evaluating whether the previously issued consolidated financial statements were materially misstated for the annual periods prior to December 31, 2020, Canon applied the guidance of ASC 250, "Accounting Changes and Error Corrections," SEC Staff Accounting Bulletin ("SAB") Topic 1.M "Assessing Materiality" and SAB Topic 1.N "Considering the Effects of Prior Period Misstatements when Quantifying Misstatements in Current Year Financial Statements," and concluded that the effect of the error on prior period financial statements was immaterial; however, the cumulative effect of correcting the prior period misstatements in the year ended December 31, 2020 would have been material to the December 31, 2020 consolidated financial statements. As a result, Canon previously revised its consolidated financial statements as follows:

Consolidated statement of income as revised in 2020

Year ended December 31	Millions of yen	
	2019	
	As revised	As previously reported
Selling, general and administrative expenses	1,137,110	1,136,863
Operating profit	174,420	174,667
Income before income taxes	195,493	195,740
Income taxes	56,146	56,223
Consolidated net income	139,347	139,517
Less: Net income attributable to noncontrolling interests	14,383	14,412
Net income attributable to Canon Inc.	124,964	125,105
	Yen	
Net income attributable to Canon Inc. shareholders per share:		
Basic	116.79	116.93
Diluted	116.77	116.91

Consolidated statement of comprehensive income as revised in 2020

Year ended December 31	Millions of yen	
	2019	
	As revised	As previously reported
Consolidated net income	139,347	139,517
Less: Comprehensive income attributable to noncontrolling interests	16,353	16,382
Comprehensive income (loss) attributable to Canon Inc.	86,139	86,280

Consolidated statement of cash flows as revised in 2020

Year ended December 31	Millions of yen	
	2019	
	As revised	As previously reported
Consolidated net income	139,347	139,517
Increase in accrued expenses	9,738	9,491
Deferred income taxes	(6,523)	(6,446)

The consolidated statement of equity has been revised, accordingly.

2. INVESTMENTS

Held-to-maturity debt securities included in short-term investments in the accompanying consolidated balance sheet were ¥2,164 million at December 31, 2021. There were no held-to-maturity debt securities as of December 31, 2020.

Held-to-maturity debt securities included in short-term investments at December 31, 2021 are as follows:

	Millions of yen		
	Carrying amount	Estimated fair value	Difference
Due within one year	2,164	2,167	3

There were no available-for-sale debt securities included in short-term investments and investments at December 31, 2021 and 2020, respectively.

The unrealized and realized gains and losses related to equity securities for the years ended December 31, 2021, 2020 and 2019 are as follows:

Years ended December 31	Millions of yen		
	2021	2020	2019
Net gains and (losses) recognized during the period on equity securities	**8,958**	1,959	2,148
Less: Net gains and (losses) recognized during the period on equity securities sold during the period	**467**	477	(76)
Unrealized gains and (losses) recognized during the period on equity securities still held at December 31	**8,491**	1,482	2,224

The carrying amount of non-marketable equity securities without readily determinable fair value totaled ¥6,661 million and ¥8,559 million at December 31, 2021 and 2020, respectively. The impairment or other adjustments resulting from observable price changes recorded during the years ended December 31, 2021 and 2020 were not significant.

Time deposits with original maturities of more than three months are ¥1,213 million and ¥71 million at December 31, 2021 and 2020, respectively, and are included in short-term investments in the accompanying consolidated balance sheets.

Investments in affiliated companies accounted for by the equity method are as follows:

Years ended December 31	Millions of yen, except percentage data		
	2021 Ownership percentage	**2021**	2020
Canon Korea Inc.	**50%**	**11,627**	10,719
Others	**—**	**10,398**	8,915
	—	**22,025**	19,634

The difference between the carrying amount of investment in each affiliate and Canon's share of its net assets is immaterial.

Canon's share of the net earnings in affiliated companies accounted for by the equity method, included in other income (deductions), were earnings of ¥1,396 million for the year ended December 31, 2021, and losses of ¥994 million and ¥311 million for the years ended December 31, 2020 and 2019, respectively.

3. TRADE RECEIVABLES

Trade receivables are summarized as follows:

December 31	Millions of yen	
	2021	2020
Notes	**28,616**	34,922
Accounts	**493,816**	511,849
Trade receivables	**522,432**	546,771
Less allowance for credit losses	**(12,494)**	(11,645)
	509,938	535,126

4. INVENTORIES

Inventories are summarized as follows:

December 31	Millions of yen	
	2021	2020
Finished goods	**395,381**	352,513
Work in process	**199,153**	160,696
Raw materials	**56,034**	49,598
	650,568	562,807

5. 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	
	2021	2020
Land	**276,306**	270,308
Buildings	**1,728,811**	1,687,921
Machinery and equipment	**1,849,271**	1,806,185
Construction in progress	**43,283**	37,324
Finance lease right-of-use assets	**6,533**	6,048
Cost	**3,904,204**	3,807,786
Less accumulated depreciation	**(2,862,801)**	(2,770,106)
Property, plant and equipment, net	**1,041,403**	1,037,680

Depreciation expenses for the years ended December 31, 2021, 2020 and 2019 were ¥156,333 million, ¥162,733 million and ¥170,418 million, respectively.

Amounts due for purchases of property, plant and equipment were ¥29,562 million and ¥27,688 million at December 31, 2021 and 2020, 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.

6. LESSOR ACCOUNTING

Lease income is included in Products and Equipment sales in the accompanying consolidated statements of income. Supplemental income statement information is as follows:

Years ended December 31	Millions of yen	
	2021	2020
Lease income – sales-type and direct financing leases		
Revenue at lease commencement	**84,895**	92,133
Interest income on lease receivables	**18,351**	18,594
	103,246	110,727
Lease income – operating leases	**27,122**	23,878
Variable lease income	**5,277**	5,343
	135,645	139,948

Finance Receivables and Operating Leases

Finance receivables represent financing leases, which consist of sales-type leases and direct financing leases. 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	
	2021	2020
Total minimum lease payments receivable	**366,051**	337,265
Unguaranteed residual values	**12,192**	11,459
Executory costs	**—**	—
Unearned income	**(31,619)**	(29,541)
	346,624	319,183
Less allowance for credit losses	**(3,791)**	(3,068)
	342,833	316,115
Less current portion	**(119,902)**	(108,837)
	222,931	207,278

Allowance for Credit Losses

The activities in the allowance for credit losses are as follows:

Years ended December 31	Millions of yen	
	2021	2020
Balance at beginning of year	**3,068**	2,627
Charge-offs	**(2,157)**	(2,199)
Provision	**2,331**	2,351
Translation adjustments and other	**549**	289
Balance at end of year	**3,791**	3,068

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 is evaluated collectively based on historical experiences 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, 2021 and December 31, 2020 are not significant.

Equipment leased to customers

The cost of equipment leased to customers under operating leases included in property, plant and equipment, net at December 31, 2021 and 2020 was ¥143,160 million and ¥132,763 million, respectively. Accumulated depreciation on equipment under operating leases at December 31, 2021 and 2020 was ¥87,879 million and ¥81,345 million, respectively.

Maturity Analysis

The following is a schedule by year of the future minimum lease payments to be received under finance leases and non-cancellable operating leases at December 31, 2021.

Year ending December 31:	Millions of yen	
	Financing leases	Operating leases
2022	131,113	11,578
2023	99,168	7,168
2024	68,241	4,914
2025	41,600	2,972
2026	18,550	1,471
Thereafter	7,379	1,402
	366,051	29,505

Information about transferring finance receivables

Canon has syndication arrangements to sell its entire interests in finance receivables to the third-party financial institutions. The transactions under the arrangements are accounted for as sales in accordance with ASC 860 "Transfers and Servicing." The transfers of finance receivables for the year ended December 31, 2020 and 2019 were ¥19,185 million and ¥11,710 million while there were no significant transfers of finance receivables for the year ended December 31, 2021. The amount that remained uncollected was ¥23,984 million and ¥36,339 million at December 31, 2021 and 2020, respectively. Cash proceeds from the transactions are included in other, net under the cash flow from operating activities in the consolidated statements of cash flows. Canon continues to provide collection and administrative services for the financial institutions. The amount associated with the servicing liability measured at fair value was not significant at December 31, 2021 and 2020. Canon also retains limited recourse obligations which cover credit defaults. The recourse obligations were not significant at December 31, 2021 and 2020.

7. ACQUISITIONS

On September 28, 2021, Canon acquired 87.0% of the issued shares of Redlen Technologies Inc. ("Redlen"), a Canada-based company, for the cash consideration of ¥31,640 million, making it a wholly owned subsidiary of Canon.

Redlen possesses advanced technologies of radiation detection and imaging solutions of Cadmium Zinc Telluride ("CZT") semiconductor detector modules which play an important role in the development of photon-counting CT systems ("PCCT"). This technology will enable Canon to accelerate the development of competitive PCCT systems, and strengthen its CT systems and the medical systems business. In addition, Canon will provide CZT semiconductor detector modules to medical equipment manufacturers around the world, thus helping to strengthen Canon's medical component business. In this way, Canon will continue to contribute to the advancement of global diagnostic imaging.

The acquisition was accounted for using the acquisition method of accounting. Acquisition-related costs were expensed as incurred and were not material. Prior to the acquisition date, Canon held an investment in Redlen at a value of ¥1,252 million. Using step acquisition accounting, Canon remeasured the acquisition-date carrying value of its previously held equity investment to its fair value of ¥5,223 million using the fair value of Redlen's issued shares on the acquisition date, which resulted in a gain of approximately ¥3,971 million, recorded in other, net of other income (deductions) in the consolidated statements of income.

The consideration for the acquisition was provisionally valued at the acquisition date based on the Share Purchase Agreement, and subsequently, an adjustment was made to the acquisition price within the measurement period after the acquisition date and determined as of December 31, 2021. As a result, the fair value of the previously held equity investment before the acquisition date and the gain on the step acquisition have been adjusted.

The final allocation of the purchase price to the assets acquired and the liabilities assumed on the acquisition date was as follows:

	Millions of yen
Current assets	**4,043**
Intangible assets	**8,955**
Goodwill	**28,826**
Others	**389**
Assets acquired	**42,213**
Liabilities assumed	**5,350**
Net assets acquired	**36,863**

The intangible assets acquired are composed by ¥8,929 million of technical assets and ¥26 million of other intangible assets, and is subject to amortization. The useful life of the technical assets and the other intangible assets are 21 years and 5 years, respectively. The weighted average useful life of the total intangible assets is approximately 21 years.

Goodwill is composed of the synergy effects of merging Redlen and Canon which is not tax deductible. The items is allocated to the Medical Business Unit when conducting the impairment test of goodwill. Net sales and net income of Redlen generated from the acquisition date which is reflected in the consolidated statement of income for the year ended December 31, 2021 was not material.

The operating results with the assumption of including the financial statements of Redlen in Canon's consolidated financial statements for the year ended December 31, 2020 and the year beginning on January 1, 2021 were not disclosed because the impact was not material.

8. GOODWILL AND OTHER INTANGIBLE ASSETS

Intangible assets subject to amortization acquired during the year ended December 31, 2021, including those recorded from businesses acquired as stated in Note 7, totaled ¥36,015 million, which primarily consist of software of ¥25,965 million. The weighted average amortization periods for intangible assets in total acquired during the year ended December 31, 2021 are approximately 9 years. The weighted average amortization period for software acquired during the year ended December 31, 2021 is approximately 5 years.

Intangible assets subject to amortization acquired during the year ended December 31, 2020, including those recorded from businesses acquired, totaled ¥31,413 million, which primarily consist of software of ¥29,137 million. The weighted average amortization periods for intangible assets in total acquired during the year ended December 31, 2020 are approximately 6 years. The weighted average amortization period for software acquired during the year ended December 31, 2020 is approximately 5 years.

The components of intangible assets subject to amortization at December 31, 2021 and 2020 were as follows:

December 31	Millions of yen			
	2021		2020	
	Gross carrying amount	Accumulated amortization	Gross carrying amount	Accumulated amortization
Software	**399,331**	**300,905**	379,504	279,372
Customer relationships	**158,513**	**59,465**	155,648	46,613
Patents and developed technology	**133,923**	**70,795**	124,315	59,328
Trademarks	**45,726**	**21,350**	44,914	17,800
License fees	**16,881**	**10,098**	13,651	6,065
Other	**18,765**	**10,521**	17,163	9,235
	773,139	**473,134**	735,195	418,413

Aggregate amortization expense for the years ended December 31, 2021, 2020 and 2019 was ¥64,913 million, ¥65,092 million and ¥66,909 million, respectively. Estimated amortization expense for intangible assets currently held for the next five years ending December 31 is ¥55,921 million in 2022, ¥47,476 million in 2023, ¥38,534 million in 2024, ¥31,977 million in 2025, and ¥28,302 million in 2026.

Intangible assets not subject to amortization other than goodwill at December 31, 2021 and 2020 were not significant.

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

The changes in the carrying amount of goodwill by segment for the years ended December 31, 2021 and 2020 were as follows:

Year ended December 31	Millions of yen				
	2021				
	Printing	Imaging	Medical	Industrial and Others	Total
Goodwill - gross	**142,185**	**289,999**	**506,513**	**9,283**	**947,980**
Accumulated impairment losses	**(32,416)**	**—**	**—**	**—**	**(32,416)**
Balance at beginning of year	**109,769**	**289,999**	**506,513**	**9,283**	**915,564**
Goodwill acquired during the year	**—**	**—**	**28,826**	**—**	**28,826**
Translation adjustments and other	**2,931**	**3,750**	**1,844**	**935**	**9,460**
Goodwill - gross	**146,025**	**293,749**	**537,183**	**10,218**	**987,175**
Accumulated impairment losses	**(33,325)**	**—**	**—**	**—**	**(33,325)**
Balance at end of year	**112,700**	**293,749**	**537,183**	**10,218**	**953,850**

Year ended December 31	Millions of yen				
	2020				
	Printing	Imaging	Medical	Industrial and Others	Total
Goodwill - gross	139,036	272,241	508,907	9,767	929,951
Accumulated impairment losses	(31,290)	—	—	—	(31,290)
Balance at beginning of year	107,746	272,241	508,907	9,767	898,661
Goodwill acquired during the year	—	—	—	—	—
Translation adjustments and other	2,023	17,758	(2,394)	(484)	16,903
Goodwill - gross	142,185	289,999	506,513	9,283	947,980
Accumulated impairment losses	(32,416)	—	—	—	(32,416)
Balance at end of year	109,769	289,999	506,513	9,283	915,564

* Based on the realignment of Canon's internal reporting and management structure, from the beginning of 2021, Canon has changed the name and structure of segments to Printing Business Unit, Imaging Business Unit, Medical Business Unit, and Industrial and Others Business Unit. Changes in the carrying amounts of goodwill by segment for the fiscal year ended December 31, 2020 also have been reclassified.

9. SHORT-TERM LOANS AND LONG-TERM DEBT

Short-term loans related to financial services are external loans held by Canon's lease subsidiaries for the purpose of financing its customers through loans. Short-term loans related to financial services consisting of bank borrowings at December 31, 2021 and 2020 were ¥42,300 million and ¥45,000 million, and other short-term loans consisting of bank borrowings were ¥1,301 million and ¥1,461 million respectively. The weighted average interest rate on short-term borrowings outstanding at December 31, 2021 and 2020 were 0.19% and 0.26%, respectively. Unused overdraft facilities at December 31, 2021 were ¥750,000 million. The overdraft facilities bear interest at a rate equal to a base rate plus a spread.

Long-term debt consisted of the following:

December 31	Millions of yen	
	2021	2020
Loan from banks; bearing interest of 0.21% at December 31, 2021 and 0.09% at December 31, 2020 *1	**174,000**	344,000
Other debt *2	**7,040**	6,608
	181,040	350,608
Less current portion	**(1,290)**	(345,774)
	179,750	4,834

*1 Canon prepaid ¥170,000 million of the outstanding loan under the unsecured revolving credit facility contracts on December 28, 2021 before its due date. The remaining balance of ¥174,000 million was refinanced with a new expiration date in December 2023 under the credit facilities. The outstanding loans under the credit facilities are ¥174,000 million at a floating interest of 0.21% and Canon has no unused credit facilities as of December 31, 2021.
*2 Other debt consisted of term-loans and finance lease obligations as of December 31, 2021 and 2020.

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

Year ending December 31:	Millions of yen
2022	1,290
2023	174,920
2024	609
2025	417
2026	237
Thereafter	3,567
	181,040

Both short-term and long-term bank loans are primarily 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.

10. TRADE PAYABLES

Trade payables are summarized as follows:

December 31	Millions of yen	
	2021	2020
Notes	**82,243**	83,468
Accounts	**256,361**	220,341
	338,604	303,809

11. 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. Canon Medical Systems Corporation ("CMSC") temporarily participated in Toshiba Corporate Pension Funds ("Toshiba Funds") after Toshiba Medical Systems Corporation (currently, Canon Medical Systems Corporation) was acquired by Canon in 2016. In April 2018, CMSC established a new pension provision which provides participants an equivalent level of benefits as compared to the Toshiba Funds. As of December 31, 2018, a majority of plan participants had been transferred from the Toshiba Funds into the new pension provision. Canon calculated the projected benefit obligations for the remaining participants within the Toshiba Funds based on the benefit level of the Toshiba Funds and included the proportional share of the plan assets to which CMSC had a legal right in the following tables for the remaining participants as of December 31, 2018. In March 2019, CMSC settled the pension obligations attributed to the remaining participants within the Toshiba Funds. The loss recognized due to the settlement in the consolidated statement of income for the year ended December 31, 2019 was not significant.

Obligations and funded status

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

December 31	Millions of yen			
	Japanese plans		Foreign plans	
	2021	2020	**2021**	2020
Change in benefit obligations:				
Projected benefit obligations at beginning of year	**911,121**	925,390	**477,337**	439,624
Service cost	**30,194**	30,604	**3,827**	5,303
Interest cost	**4,815**	4,064	**5,965**	6,087
Plan participants' contributions	**—**	—	**658**	860
Actuarial (gain) loss	**2,935**	(11,432)	**(21,133)**	43,202
Benefits paid	**(39,390)**	(36,646)	**(13,471)**	(12,351)
Plan amendments	**(41)**	(859)	**(10,617)**	(1,463)
Curtailments and settlements	**—**	—	**(682)**	(6,004)
Foreign currency exchange rate changes	**—**	—	**34,346**	2,079
Projected benefit obligations at end of year	**909,634**	911,121	**476,230**	477,337
Change in plan assets:				
Fair value of plan assets at beginning of year	**724,039**	704,169	**321,713**	294,829
Actual return on plan assets	**52,688**	36,060	**24,024**	23,912
Employer contributions	**11,652**	13,360	**32,130**	13,605
Plan participants' contributions	**—**	—	**658**	860
Benefits paid	**(31,636)**	(29,550)	**(13,471)**	(12,351)
Settlements	**—**	—	**1,743**	(805)
Foreign currency exchange rate changes	**—**	—	**28,115**	1,663
Fair value of plan assets at end of year	**756,743**	724,039	**394,912**	321,713
Funded status at end of year	**(152,891)**	(187,082)	**(81,318)**	(155,624)

Amounts recognized in the consolidated balance sheets at December 31, 2021 and 2020 are as follows:

December 31	Millions of yen			
	Japanese plans		Foreign plans	
	2021	2020	**2021**	2020
Other assets	**2,911**	2,684	**13,596**	2,236
Accrued expenses	**(1,208)**	(791)	**(1,041)**	(938)
Accrued pension and severance cost	**(154,594)**	(188,975)	**(93,873)**	(156,922)
	(152,891)	(187,082)	**(81,318)**	(155,624)

Amounts recognized in accumulated other comprehensive income (loss) at December 31, 2021 and 2020 before the effect of income taxes are as follows:

December 31	Millions of yen			
	Japanese plans		Foreign plans	
	2021	2020	**2021**	2020
Actuarial loss	**156,028**	192,931	**104,647**	142,455
Prior service credit	**(20,371)**	(28,633)	**(10,319)**	(520)
	135,657	164,298	**94,328**	141,935

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

December 31	Millions of yen			
	Japanese plans		Foreign plans	
	2021	2020	**2021**	2020
Accumulated benefit obligation	**883,462**	879,136	**462,306**	460,536

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	Millions of yen			
	Japanese plans		Foreign plans	
	2021	2020	**2021**	2020
Plans with projected benefit obligations in excess of plan assets:				
Projected benefit obligations	**895,898**	897,669	**473,860**	475,137
Fair value of plan assets	**739,581**	707,708	**391,054**	318,079
Plans with accumulated benefit obligations in excess of plan assets:				
Accumulated benefit obligations	**870,314**	874,327	**455,164**	453,120
Fair value of plan assets	**739,581**	707,708	**386,223**	312,748

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, 2021, 2020 and 2019 consisted of the following components:

Years ended December 31	Millions of yen					
	Japanese plans			Foreign plans		
	2021	2020	2019	**2021**	2020	2019
Service cost	**30,194**	30,604	30,903	**3,827**	5,303	6,264
Interest cost	**4,815**	4,064	5,074	**5,965**	6,087	8,643
Expected return on plan assets	**(21,618)**	(21,013)	(19,553)	**(15,221)**	(12,006)	(11,919)
Amortization of prior service credit	**(8,303)**	(8,732)	(11,877)	**(818)**	(675)	(133)
Amortization of actuarial loss	**8,768**	12,401	15,247	**7,341**	6,122	4,345
(Gain) loss on curtailments and settlements	**—**	—	(36)	**—**	236	(2,197)
	13,856	17,324	19,758	**1,094**	5,067	5,003

Service cost component of net periodic benefit cost for Canon's employee retirement and severance defined benefit plans is included in cost of sales and operating expenses in the consolidated statements of income. The components other than the service cost component are included in other, net of other income (deductions) in the consolidated statements of income.

Other changes in plan assets and benefit obligations recognized in other comprehensive income (loss) for the years ended December 31, 2021, 2020 and 2019 are summarized as follows:

Years ended December 31	Millions of yen					
	Japanese plans			Foreign plans		
	2021	2020	2019	**2021**	2020	2019
Current year actuarial (gain) loss	**(28,135)**	(26,479)	(19,328)	**(29,936)**	31,296	28,882
Current year prior service credit	**(41)**	(859)	—	**(10,617)**	(1,463)	362
Amortization of actuarial loss	**(8,768)**	(12,401)	(15,247)	**(7,341)**	(6,122)	(4,345)
Amortization of prior service credit	**8,303**	8,732	11,877	**818**	675	133
Curtailments and settlements	**—**	—	(960)	**(531)**	(966)	(1,411)
	(28,641)	(31,007)	(23,658)	**(47,607)**	23,420	23,621

Assumptions

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

December 31	Japanese plans		Foreign plans	
	2021	2020	**2021**	2020
Discount rate	**0.5%**	0.5%	**1.5%**	1.5%
Assumed rate of increase in future compensation levels	**2.6%**	2.6%	**0.7%**	0.9%
Interest crediting rate for cash balance plans	**1.9%**	1.9%	**1.0%**	1.0%

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

Years ended December 31	Japanese plans			Foreign plans		
	2021	2020	2019	**2021**	2020	2019
Discount rate	**0.5%**	0.5%	0.6%	**1.5%**	1.6%	2.4%
Assumed rate of increase in future compensation levels	**2.6%**	2.6%	2.6%	**0.9%**	1.0%	1.9%
Expected long-term rate of return on plan assets	**3.0%**	3.0%	3.0%	**4.4%**	4.8%	5.2%
Interest crediting rate for cash balance plans	**1.9%**	1.9%	1.9%	**1.0%**	1.0%	1.0%

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 25% is invested in equity securities, approximately 50% is invested in debt securities, and approximately 25% is invested in other products, such as investments in insurance contracts including life insurance company general accounts.

Outside Japan, investment policies vary by country, but Canon's model portfolio for foreign plans consists of three major components: approximately 20% is invested in equity securities, approximately 30% is invested in debt securities, and approximately 50% is invested in other products, such as investments in real estate assets.

The target allocation percentages of plan assets set by Canon's investment policies approximate the actual allocation percentages of plan assets at December 31, 2021 and 2020.

The equity securities are selected primarily from stocks that are listed on securities exchanges. Prior to investing, Canon investigates the business condition of the investee companies, and appropriately diversifies 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 investigates the quality of the issue, including rating, interest rate, and repayment dates, and appropriately diversifies the investments. Pooled funds are selected using strategies consistent with the equity and debt securities described above. As for insurance contracts, there are several types of insurance contracts between Canon and the life insurance companies including life insurance company general accounts which guarantee the payments of interest based on expected interest rates and return of capital, and insured pension plans which cover future designated contractual benefit payments to covered participants. With respect to investments in foreign financial products, Canon investigates the stability of the underlying governments and economies, the market characteristics such as settlement systems and the taxation systems. For each such investment, Canon selects the appropriate investment country and currency.

The three levels of input used to measure fair value are more fully described in Note 22. The fair values of Canon's pension plan assets at December 31, 2021 and 2020, by asset category, are as follows:

December 31	Millions of yen							
	2021							
	Japanese plans				Foreign plans			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Equity securities:								
Japanese companies (a)	95,698	—	—	95,698	—	—	—	—
Foreign companies	12,746	—	—	12,746	11,628	—	—	11,628
Pooled funds (b)	—	180,286	—	180,286	—	43,026	—	43,026
Debt securities:								
Government bonds (c)	133,691	—	—	133,691	—	—	—	—
Municipal bonds	—	1,264	—	1,264	—	2,899	—	2,899
Corporate bonds	—	19,373	—	19,373	—	7,821	—	7,821
Pooled funds (d)	—	145,348	—	145,348	—	138,687	—	138,687
Mortgage backed securities (and other asset backed securities)	—	11,449	—	11,449	—	6,826	—	6,826
Insurance contracts	—	114,624	—	114,624	—	6,287	39,398	45,685
Other assets	—	28,181	366	28,547	—	106,657	532	107,189
Investment measured at net asset value	—	—	—	13,717	—	—	—	31,151
	242,135	500,525	366	756,743	11,628	312,203	39,930	394,912

December 31	Millions of yen							
	2020							
	Japanese plans				Foreign plans			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Equity securities:								
Japanese companies (e)	80,201	—	—	80,201	—	—	—	—
Foreign companies	9,807	—	—	9,807	10,267	—	—	10,267
Pooled funds (f)	—	168,745	—	168,745	—	37,538	—	37,538
Debt securities:								
Government bonds (g)	136,771	—	—	136,771	—	—	—	—
Municipal bonds	—	1,126	—	1,126	—	2,324	—	2,324
Corporate bonds	—	15,617	—	15,617	—	6,375	—	6,375
Pooled funds (h)	—	140,825	—	140,825	—	108,499	—	108,499
Mortgage backed securities (and other asset backed securities)	—	8,308	—	8,308	—	2,696	—	2,696
Life insurance company general accounts	—	117,762	—	117,762	—	27,953	—	27,953
Other assets	—	28,731	1,356	30,087	—	102,159	—	102,159
Investment measured at net asset value	—	—	—	14,790	—	—	—	23,902
	226,779	481,114	1,356	724,039	10,267	287,544	—	321,713

(a) The plan's equity securities include common stock of the Company and certain of its subsidiaries in the amounts of ¥234 million.
(b) These funds invest in listed equity securities consisting of approximately 30% Japanese companies and 70% foreign companies for Japanese plans, and mainly foreign companies for foreign plans.
(c) This class includes approximately 80% Japanese government bonds and 20% foreign government bonds for Japanese plans.
(d) These funds invest in approximately 25% Japanese government bonds, 55% foreign government bonds, 5% Japanese municipal bonds, and 15% corporate bonds for Japanese plans. These funds invest in approximately 75% foreign government bonds and 25% corporate bonds for Japanese plans.
(e) The plan's equity securities include common stock of the Company and certain of its subsidiaries in the amounts of ¥282 million.
(f) These funds invest in listed equity securities consisting of approximately 30% Japanese companies and 70% foreign companies for Japanese plans, and mainly foreign companies for foreign plans.
(g) This class includes approximately 85% Japanese government bonds and 15% foreign government bonds for Japanese plans, and mainly foreign government bonds for foreign plans.
(h) These funds invest in approximately 25% Japanese government bonds, 55% foreign government bonds, 5% Japanese municipal bonds, and 15% corporate bonds for Japanese plans. These funds invest in approximately 60% foreign government bonds and 40% 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, investments in life insurance company general accounts and other assets. 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. Other assets are comprised principally of interest bearing cash and hedge funds.

The fair values of Level 3 asset, consisting of investments in insured pension plans and hedge funds, were ¥ 40,296 million and ¥1,356 million at December 31, 2021 and 2020, respectively. Amounts of actual returns on, purchases and sales of these assets during the years ended December 31, 2021 and 2020 were not significant.

Contributions

Canon expects to contribute ¥15,942 million to its Japanese defined benefit pension plans and ¥18,165 million to its foreign defined benefit pension plans for the year ending December 31, 2022.

Estimated future benefit payments

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

Year ending December 31:	Millions of yen	
	Japanese plans	Foreign plans
2022	44,169	15,228
2023	44,772	15,887
2024	44,699	17,151
2025	45,715	18,145
2026	44,479	19,199
2027 – 2031	228,342	116,447

Multiemployer pension plans

The amounts of cost recognized for the multiemployer pension plans primarily in the Netherlands for the years ended December 31, 2021, 2020 and 2019 were ¥4,822 million, ¥4,224 million and ¥4,321 million, respectively. The multiemployer pension plan in which the subsidiaries in the Netherlands participated was 97.6% funded as of December 31, 2020. The terms of the collective bargaining agreements are negotiated on a regular basis between the local labor unions and participating employers. Canon is not liable for other participating employers' obligations under the terms and conditions of the agreements.

Defined contribution plans

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, 2021, 2020 and 2019 were ¥22,660 million, ¥16,334 million and ¥17,414 million, respectively.

12. INCOME TAXES

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

Years ended December 31	Millions of yen		
	2021		
	Japanese	Foreign	Total
Income before income taxes	**165,927**	**136,779**	**302,706**
Income taxes:			
Current	**47,491**	**34,201**	**81,692**
Deferred	**6,883**	**(16,709)**	**(9,826)**
	54,374	**17,492**	**71,866**

Years ended December 31	Millions of yen		
	2020		
	Japanese	Foreign	Total
Income before income taxes	48,186	82,094	130,280
Income taxes:			
Current	24,063	25,816	49,879
Deferred	(6,007)	(9,535)	(15,542)
	18,056	16,281	34,337

Years ended December 31	Millions of yen		
	2019		
	Japanese	Foreign	Total
Income before income taxes	107,082	88,411	195,493
Income taxes:			
Current	39,483	23,186	62,669
Deferred	(4,276)	(2,247)	(6,523)
	35,207	20,939	56,146

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 31% for the years ended December 31, 2021, 2020 and 2019.

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	2021	2020	2019
Japanese statutory income tax rate	**31.0%**	31.0%	31.0%
Increase (reduction) in income taxes resulting from:			
Expenses not deductible for tax purposes	**0.7**	2.3	1.7
Income of foreign subsidiaries taxed at lower than Japanese statutory tax rate	**(3.9)**	(5.8)	(2.9)
Tax credit for research and development expenses	**(3.2)**	(1.7)	(2.3)
Change in valuation allowance	**(3.9)**	2.4	(1.6)
Deferred tax liabilities on undistributed earnings of foreign subsidiaries	**4.5**	2.6	2.4
Tax credit at foreign subsidiaries	**(0.3)**	(1.3)	(1.1)
Effect of enacted changes in tax laws	**(1.0)**	(1.5)	(0.2)
Other	**(0.2)**	(1.6)	1.7
Effective income tax rate	**23.7%**	26.4%	28.7%

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

December 31	Millions of yen	
	2021	2020
Other assets	**138,507**	154,226
Other noncurrent liabilities	**(43,402)**	(48,247)
	95,105	105,979

The tax effects of temporary differences that give rise to the deferred tax assets and deferred tax liabilities at December 31, 2021 and 2020 are presented below:

December 31	Millions of yen	
	2021	2020
Deferred tax assets:		
Inventories	**11,263**	10,551
Accrued business tax	**3,387**	1,629
Accrued pension and severance cost	**67,752**	95,386
Research and development – costs capitalized for tax purposes	**5,004**	4,989
Property, plant and equipment	**35,658**	34,923
Operating lease liabilities	**17,328**	20,163
Accrued expenses	**29,331**	28,243
Net operating losses carried forward	**33,873**	29,591
Other	**48,621**	42,741
	252,217	268,216
Less valuation allowance	**(19,073)**	(30,752)
Total deferred tax assets	**233,144**	237,464
Deferred tax liabilities:		
Undistributed earnings of foreign subsidiaries	**(19,677)**	(9,147)
Tax deductible reserve	**(4,007)**	(4,040)
Financing lease revenue	**(14,602)**	(15,041)
Operating lease right-of-use assets	**(17,066)**	(19,425)
Intangible assets	**(51,173)**	(54,948)
Other	**(31,514)**	(28,884)
Total deferred tax liabilities	**(138,039)**	(131,485)
Net deferred tax assets	**95,105**	105,979

The net changes in the total valuation allowance were a decrease of ¥11,679 million, an increase of ¥3,074 million and a decrease of ¥3,056 million for the years ended December 31, 2021, 2020 and 2019, respectively.

Based on 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 valuation allowance, at December 31, 2021.

At December 31, 2021, Canon had net operating losses which can be carried forward for income tax purposes of ¥175,581 million to reduce future taxable income. Periods available to reduce future taxable income vary in each tax jurisdiction and generally range from one year to an indefinite period as follows:

	Millions of yen
Within one year	1,206
After one year through five years	13,869
After five years through ten years	44,316
After ten years through twenty years	8,223
Indefinite period	107,967
	175,581

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 ¥16,162 million for a portion of undistributed earnings of foreign subsidiaries of ¥875,208 million as of December 31, 2021 because Canon intends to permanently reinvest such undistributed earnings of foreign subsidiaries. Deferred tax liabilities will be recognized when such undistributed earnings are no longer permanently reinvested.

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

Years ended December 31	Millions of yen		
	2021	2020	2019
Balance at beginning of year	**8,572**	8,120	8,649
Additions for tax positions of the current year	**1,168**	—	—
Additions for tax positions of prior years	**216**	208	204
Reductions for tax positions of prior years	**—**	(49)	(44)
Settlements with tax authorities	**(62)**	—	(402)
Other	**(81)**	293	(287)
Balance at end of year*	**9,813**	8,572	8,120

* The unrecognized tax benefits were offset by deferred tax assets in the amount of ¥1,695 million, ¥1,412 million and ¥933 million as of December 31, 2021, 2020 and 2019, respectively, and reported under "other noncurrent liabilities" on the consolidated balance sheets.

The total amounts of unrecognized tax benefits that would reduce the effective tax rate, if recognized, were ¥9,813 million and ¥8,572 million at December 31, 2021 and 2020, respectively.

Although Canon believes its estimates and assumptions of unrecognized tax benefits are reasonable, uncertainty regarding the final determination of tax examination settlements and any related litigation could affect the effective tax rate in a future period. Based on each of the items of which Canon is aware at December 31, 2021, 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, 2021 and 2020, and interest and penalties included in income taxes for the years ended December 31, 2021, 2020 and 2019 were not significant.

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 2021. Canon is also no longer subject to a transfer pricing examination by the tax authority for years before 2021. 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 2014 with few exceptions.

13. 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 resolution of the shareholders. Certain foreign subsidiaries are also required to appropriate their earnings to legal reserves under the laws of their respective countries.

Cash dividends and appropriations to the legal reserve charged to retained earnings for the years ended December 31, 2021, 2020 and 2019 represent dividends paid out during those years and the related appropriations to the legal reserve. Retained earnings at December 31, 2021 did not reflect current year-end dividends in the amount of ¥57,517 million which were approved by the shareholders in March 2022.

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 financial accounting standards of Japan. Such amount was ¥858,455 million at December 31, 2021.

Retained earnings at December 31, 2021 included Canon's equity in undistributed earnings of affiliated companies accounted for by the equity method in the amount of ¥17,858 million.

14. OTHER COMPREHENSIVE INCOME (LOSS)

Changes in accumulated other comprehensive income (loss) for the years ended December 31, 2021, 2020 and 2019 are as follows:

	Millions of yen			
	Foreign currency translation adjustments	Gains and losses on derivative instruments	Pension liability adjustments	Total
Balance at December 31, 2018	(63,815)	308	(205,564)	(269,071)
Cumulative effects of accounting standard update —adoption of ASU No. 2017-12	—	(122)	—	(122)
Equity transactions with noncontrolling interests and other	(424)	—	—	(424)
Other comprehensive income (loss) before reclassifications	(31,889)	(1,723)	(12,763)	(46,375)
Amounts reclassified from accumulated other comprehensive income (loss)	(154)	650	7,054	7,550
Net change during the year	(32,467)	(1,073)	(5,709)	(39,249)
Balance at December 31, 2019	(96,282)	(887)	(211,273)	(308,442)
Equity transactions with noncontrolling interests and other	(9)	—	—	(9)
Other comprehensive income (loss) before reclassifications	(17,355)	(1,199)	(7,530)	(26,084)
Amounts reclassified from accumulated other comprehensive income (loss)	—	2,186	7,560	9,746
Net change during the year	(17,364)	987	30	(16,347)
Balance at December 31, 2020	(113,646)	100	(211,243)	(324,789)
Other comprehensive income (loss) before reclassifications	**119,689**	**(3,330)**	**49,759**	**166,118**
Amounts reclassified from accumulated other comprehensive income (loss)	**(524)**	**2,336**	**5,065**	**6,877**
Net change during the year	**119,165**	**(994)**	**54,824**	**172,995**
Balance at December 31, 2021	**5,519**	**(894)**	**(156,419)**	**(151,794)**

Reclassifications out of accumulated other comprehensive income (loss) for the years ended December 31, 2021, 2020 and 2019 are as follows:

Years ended December 31	Amount reclassified from accumulated other comprehensive income (loss) *			Affected line items in consolidated statements of income
	Millions of yen			
	2021	2020	2019	
Foreign currency translation adjustments	**(759)**	—	—	Selling, general and administrative expenses
	—	—	(154)	Other, net
	235	—	—	Income taxes
	(524)	—	(154)	Consolidated net income
	—	—	—	Net income attributable to noncontrolling interests
	(524)	—	(154)	Net income attributable to Canon Inc.
Gains and losses on derivative instruments	**3,285**	3,034	661	Net Sales
	(959)	(775)	(2)	Income taxes
	2,326	2,259	659	Consolidated net income
	10	(73)	(9)	Net income attributable to noncontrolling interests
	2,336	2,186	650	Net income attributable to Canon Inc.
Pension liability adjustments	**7,519**	10,082	9,953	Other, net
	(1,625)	(2,484)	(2,523)	Income taxes
	5,894	7,598	7,430	Consolidated net income
	(829)	(38)	(376)	Net income attributable to noncontrolling interests
	5,065	7,560	7,054	Net income attributable to Canon Inc.
Total amount reclassified, net of tax and noncontrolling interests	**6,877**	9,746	7,550	

* Amounts in parentheses indicate gains in consolidated statements of income.

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
2021:			
Foreign currency translation adjustments			
Amount arising during the year	**122,075**	**(1,112)**	**120,963**
Reclassification adjustments for gains and losses realized in net income	**(759)**	**235**	**(524)**
Net change during the year	**121,316**	**(877)**	**120,439**
Net gains and losses on derivative instruments:			
Amount arising during the year	**(4,596)**	**1,298**	**(3,298)**
Reclassification adjustments for gains and losses realized in net income	**3,285**	**(959)**	**2,326**
Net change during the year	**(1,311)**	**339**	**(972)**
Pension liability adjustments:			
Amount arising during the year	**68,729**	**(18,115)**	**50,614**
Reclassification adjustments for gains and losses realized in net income	**7,519**	**(1,625)**	**5,894**
Net change during the year	**76,248**	**(19,740)**	**56,508**
Other comprehensive income (loss)	**196,253**	**(20,278)**	**175,975**
2020:			
Foreign currency translation adjustments			
Amount arising during the year	(17,583)	229	(17,354)
Reclassification adjustments for gains and losses realized in net income	—	—	—
Net change during the year	(17,583)	229	(17,354)
Net gains and losses on derivative instruments:			
Amount arising during the year	(1,731)	442	(1,289)
Reclassification adjustments for gains and losses realized in net income	3,034	(775)	2,259
Net change during the year	1,303	(333)	970
Pension liability adjustments:			
Amount arising during the year	(2,495)	(3,721)	(6,216)
Reclassification adjustments for gains and losses realized in net income	10,082	(2,484)	7,598
Net change during the year	7,587	(6,205)	1,382
Other comprehensive income (loss)	(8,693)	(6,309)	(15,002)
2019:			
Foreign currency translation adjustments			
Amount arising during the year	(32,396)	393	(32,003)
Reclassification adjustments for gains and losses realized in net income	(154)	—	(154)
Net change during the year	(32,550)	393	(32,157)
Net gains and losses on derivative instruments:			
Amount arising during the year	(2,180)	453	(1,727)
Reclassification adjustments for gains and losses realized in net income	661	(2)	659
Net change during the year	(1,519)	451	(1,068)
Pension liability adjustments:			
Amount arising during the year	(9,916)	(1,144)	(11,060)
Reclassification adjustments for gains and losses realized in net income	9,953	(2,523)	7,430
Net change during the year	37	(3,667)	(3,630)
Other comprehensive income (loss)	(34,032)	(2,823)	(36,855)

15. REVENUE

Revenue from sales of products of the Printing Business Unit, such as office MFDs, laser printers and inkjet printers, and the Imaging Business Unit, such as digital cameras, is primarily recognized upon shipment or delivery, depending upon when the customer obtains controls of these products.

Revenue from sales of equipment of the Medical Business Unit and the Industrial and Others Business Unit that are sold with customer acceptance provisions related to their functionality, including certain medical equipment such as CT systems and MRI systems, and lithography equipment such as semiconductor and FPD lithography equipment, is recognized when the equipment is installed at the customer site and the agreed-upon specifications are objectively satisfied and confirmed.

Most of Canon's service revenue is generated from maintenance service in the products of the Printing Business Unit and the Medical Business Unit which is recognized over time. For the service contracts of the Printing Business Unit, the customer typically pays a variable amount based on usage, a stated fixed fee or a stated base fee plus a variable amount which frequently include the provision of consumables as well as break fix activities. The majority portion of service revenue from the products of the Printing Business Unit is recognized as billed since the invoiced amount directly correlates with the value to the customer of the underlying performance obligation to date. For the service contracts of the Medical Business Unit, the customer typically pays a stated fixed fee for the stand ready maintenance service and revenue is recognized ratably over the contract period.

The majority of service arrangements for the products are executed in combination with related products. Transaction prices for products and services need to be allocated to each performance obligation on a relative standalone selling price basis where judgements are required. Canon estimates the standalone selling price using a range of prices that would meet the allocation objective based on all the information that is reasonably available including market conditions and other observable inputs. If transaction prices of the product or service contracts are not within the acceptable range then the revenue is subject to allocation based on the estimated standalone selling prices. Canon recognizes the incremental costs of obtaining a contract as an expense when related products of the Printing Business Unit are sold.

Revenue from sales of certain industrial equipment which do not have alternative use and for which Canon has enforceable right to payment to the customers for the performance completed to date is recognized over time with progress towards completion measured using the cost based input method as the basis to recognize revenue and an estimated margin. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses become evident. Changes in job performance, job conditions, estimated margin and final contract settlements may result in revisions to projected costs and revenue and are recognized in the period in which the revisions to estimates are identified and the amounts can be reasonably estimated. Factors that may affect future project costs and margins include, production efficiencies, availability and costs of labor and materials. These factors can impact the accuracy of Canon's estimates and materially impact future reported revenue and cost of sales.

The transaction prices that Canon is entitled to receive in exchange for transferring goods or services to the customer include certain forms of variable consideration, including product discounts, customer promotions and volume-based rebates mainly for the products of the Imaging Business Unit, which are sold predominantly through distributors and retailers. Canon includes estimated amounts in the transaction price only to the extent it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is resolved. Variable considerations are estimated based upon historical trends and other known factors at the time of sale, and are subsequently adjusted in each period based on current information. In addition, Canon may provide a right of return on its products for a short time period after a sale. These rights are accounted for as variable consideration when determining the transaction price, and accordingly Canon recognizes revenue based on the estimated amount to which Canon expects to be entitled after considering expected returns.

Disaggregated revenue by timing is as follows. Disaggregated revenue by business unit, product and geographic area are described in Note 23.

	Millions of yen					
	Printing	Imaging	Medical	Industrial and Others	Corporate and eliminations	Consolidated
2021:						
Revenue recognized at a point in time	**1,419,043**	**646,849**	**329,323**	**439,914**	**(105,126)**	**2,730,003**
Revenue recognized over time	**519,804**	**6,683**	**151,039**	**105,828**	**—**	**783,354**
Total	**1,938,847**	**653,532**	**480,362**	**545,742**	**(105,126)**	**3,513,357**
2020:						
Revenue recognized at a point in time	1,316,556	534,685	287,849	336,235	(83,094)	2,392,231
Revenue recognized over time	487,871	6,629	148,225	125,287	—	768,012
Total	1,804,427	541,314	436,074	461,522	(83,094)	3,160,243
2019:						
Revenue recognized at a point in time	1,520,393	651,629	290,702	391,272	(93,180)	2,760,816
Revenue recognized over time	572,071	10,077	147,823	102,512	—	832,483
Total	2,092,464	661,706	438,525	493,784	(93,180)	3,593,299

* Based on the realignment of Canon's internal reporting and management structure, from the beginning of 2021, Canon has changed the name and structure of segments to Printing Business Unit, Imaging Business Unit, Medical Business Unit, and Industrial and Others Business Unit. Changes in the disaggregated revenue by timing and by segment for the fiscal year ended December 31, 2020 and 2019 also have been reclassified.

Revenue recognized over time includes primarily revenue from maintenance service in the products of the Printing Business Unit and the Medical Business Unit and sales of certain equipment of the Industrial and Others Unit which do not have alternative use and for which Canon has enforceable right to payment to the customers for the performance completed to date.

Canon recognizes contract assets primarily for unbilled receivables mainly arising from services contracts for the products of the Printing Business Unit. Contract assets are reclassified to trade receivables when they are billed under the terms of the contract. The difference between the opening and closing balances of contract assets primarily results from the timing difference of Canon's performance and billing to customers. Contract assets at December 31, 2021 and 2020 were ¥44,722 million and ¥42,752 million, respectively, and are included in prepaid expenses and other current assets in the consolidated balance sheets.

Canon typically bills to the customer when the performance obligation is satisfied and collects the payment in relatively short term except for certain maintenance service of the products of the Printing Business Unit and the Medical Business Unit and certain industrial equipment for which Canon occasionally receives the payment in advance from customers. The amount received in excess of revenue recognized is recorded as deferred revenue until the performance obligation for distinct goods or services are satisfied. Deferred revenue at December 31, 2021 and 2020 were ¥132,087 million and ¥135,455 million, respectively, and are included in other current liabilities and other non-current liabilities in the accompanying consolidated balance sheets. Revenue recognized for the year ended December 31, 2021, which had been included in the deferred revenue balance at December 31, 2020, was ¥112,232 million.

Remaining performance obligations for products and equipment at December 31, 2021 primarily arise from the sales of certain industrial equipment, amounting to ¥150,833 million, 66% of which is expected to be recognized as revenue within one year and remaining 34% is within two years. Disclosure of remaining performance obligations is not required for the majority of services since the related revenue is recognized on an as billed basis applying the right to invoice practical expedient or is generated from the contracts with original expected duration of less than one year. The portion of fixed maintenance service contract for the products of the Printing Business Unit and the Medical Business Unit with original expected duration of more than one year is approximately 13% of total service revenue and the average remaining period for these fixed contracts as of December 31, 2021 is about two years.

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

16. STOCK-BASED COMPENSATION

On April 28, 2021, based on the approval of the board of directors, the Company granted stock options to its directors and executive officers to acquire 43,700 shares of common stock. Those to whom stock acquisition rights are granted (the "Holder(s)") shall be entitled to exercise all the stock acquisition rights together within 10 days (in case the last day is not a business day, the following business day) from after the date when they cease to hold any position as a director or an executive officer of the Company. These option awards have a 30 year exercisable period. The grant-date fair value per share of the stock options granted during the year ended December 31, 2021 was ¥2,227.

On May 1, 2020, based on the board of the directors, the Company granted stock options to its directors and executive officers to acquire 88,600 shares of common stock. Those to whom stock acquisition rights are granted (the "Holder(s)") shall be entitled to exercise all the stock acquisition rights together within 10 days (in case the last day is not a business day, the following business day) from after the date when they cease to hold any position as a director or an executive officer of the Company. These option awards have a 30 year exercisable period. The grant-date fair value per share of the stock options granted during the year ended December 31, 2020 was ¥1,459.

On March 25, 2020, based on the board of the directors, the Company granted stock options to its executive officer to acquire 10,300 shares of common stock. The Holder shall be entitled to exercise all the stock acquisition rights together within 10 days (in case the last day is not a business day, the following business day) from after the date when they cease to hold any position as a director or an executive officer of the Company. These option awards have a 30 year exercisable period. The grant-date fair value per share of the stock options granted during the year ended December 31, 2020 was ¥1,703.

The compensation cost recognized for these stock options for the years ended December 31, 2021 was ¥97 million and 2020 was ¥147 million and 2019 was ¥265 million, and it is included in selling, general and administrative expenses in the consolidated statements of income.

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

Years ended December 31	**2021**	2020	
		Granted on March 25, 2020	Granted on May 1, 2020
Expected term of option (in years)	**5.0**	6.0	6.0
Expected volatility	**24.83%**	20.32%	20.92%
Dividend yield	**3.04%**	6.25%	6.97%
Risk-free interest rate	**(0.10%)**	(0.12%)	(0.17%)

A summary of option activity under the stock option plans as of and for the years ended December 31, 2021, 2020 and 2019 is presented below:

	Shares	Weighted-average exercise price	Weighted-average remaining contractual term	Aggregate intrinsic value
		Yen	Year	Millions of yen
Outstanding at January 1, 2019	74,000	1	29.3	222
Granted	116,300	1		
Exercised	(4,500)	1		
Outstanding at December 31, 2019	185,800	1	29.0	555
Granted	98,900	1		
Exercised	(37,100)	1		
Outstanding at December 31, 2020	247,600	1	28.4	324
Granted	**43,700**	**1**		
Exercised	**(4,800)**	**1**		
Outstanding at December 31, 2021	**286,500**	**1**	**27.8**	**802**
Exercisable at December 31, 2021	**286,500**	**1**	**27.8**	**802**

The total fair values of shares vested during the years ended December 31, 2021 and 2020 were ¥97 million and ¥147 million, respectively, and 2019 was ¥265 million. Cash received from the exercise of stock options for the years ended December 31, 2021, 2020 and 2019 were not significant.

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

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

Years ended December 31	Millions of yen		
	2021	2020	2019
Basic net income attributable to Canon Inc.	**214,718**	83,318	124,964
Diluted net income attributable to Canon Inc.	**214,714**	83,315	124,962

	Number of shares		
Average common shares outstanding	**1,045,632,588**	1,049,802,197	1,069,956,767
Effect of dilutive securities:			
Stock options	**277,066**	229,691	158,173
Diluted common shares outstanding	**1,045,909,654**	1,050,031,888	1,070,114,940

	Yen		
Net income attributable to Canon Inc. shareholders per share:			
Basic	**205.35**	79.37	116.79
Diluted	**205.29**	79.35	116.77

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 speculative 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 in the same period as the hedged items affect earnings. Substantially all amounts recorded in accumulated other comprehensive income (loss) as of December 31, 2021 are expected to be recognized in net sales over the next twelve months. 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.

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, 2021 and 2020 are set forth below:

December 31	Millions of yen	
	2021	2020
To sell foreign currencies	**169,392**	137,721
To buy foreign currencies	**27,453**	27,220

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, 2021 and 2020.

Derivatives designated as hedging instruments

December 31		Millions of yen	
		Fair value	
	Balance sheet location	**2021**	2020
Assets:			
Foreign exchange contracts	Prepaid expenses and other current assets	**42**	426
Liabilities:			
Foreign exchange contracts	Other current liabilities	**777**	416

Derivatives not designated as hedging instruments

December 31		Millions of yen	
		Fair value	
	Balance sheet location	**2021**	2020
Assets:			
Foreign exchange contracts	Prepaid expenses and other current assets	**23**	107
Liabilities:			
Foreign exchange contracts	Other current liabilities	**1,342**	809

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, 2021, 2020 and 2019.

Derivatives in cash flow hedging relationships

Years ended December 31	Millions of yen		
	Gain (loss) recognized in OCI	Gain (loss) reclassified from accumulated OCI into income	
	Amount	Location	Amount
2021: Foreign exchange contracts	**(4,596)**	Net sales	**(3,285)**
2020: Foreign exchange contracts	(1,731)	Net sales	(3,034)
2019: Foreign exchange contracts	(2,180)	Net sales	(661)

Derivatives not designated as hedging instruments

Years ended December 31		Millions of yen		
		Gain (loss) recognized in income on derivative		
	Location	**2021**	2020	2019
Foreign exchange contracts	Other, net	**(6,099)**	104	805

19. LESSEE ACCOUNTING

Lease costs are included in cost of sales or selling general and administrative expense in accompanying consolidated statements of income. Supplemental income statement information is as follows:

Years ended December 31	Millions of yen	
	2021	2020
Operating lease cost	**39,699**	40,053
Short-term lease cost	**13,961**	14,245
Other lease cost	**71**	120
	53,731	54,418

Operating lease cash flow

Supplemental cash flow information is as follows:

Years ended December 31	Millions of yen	
	2021	2020
Cash paid for amount included in the measurement of lease liabilities		
Operating cash flows from operating leases	**39,879**	36,733
Noncash activity - Rights of use assets obtained in exchange for lease liabilities		
Operating leases	**21,588**	30,700

Maturity Analysis

The following is a schedule by year of the future minimum lease payments under operating leases at December 31, 2021.

Years ending December 31:	Millions of yen
2022	32,941
2023	22,512
2024	15,226
2025	10,816
2026	7,832
Thereafter	11,192
Total future minimum lease payments	100,519
Less Imputed Interest	(4,189)
	96,330

Remaining lease term and discount rate

The following is remaining lease term and discount rate under operating leases at December 31, 2021 and 2020.

December 31	**2021**	2020
Weighted-average remaining lease term	**54 months**	56 months
Weighted-average discount rate	**2.1%**	2.1%

20. COMMITMENTS AND CONTINGENT LIABILITIES

Commitments

At December 31, 2021, commitments outstanding for the purchase of property, plant and equipment approximated ¥76,229 million, and commitments outstanding for the purchase of parts and raw materials approximated ¥249,909 million.

Guarantees

Canon occupies sales offices and other facilities under lease arrangements accounted for as operating leases. Deposits mainly for restoration made under such arrangements aggregated ¥10,812 million and ¥10,962 million at December 31, 2021 and 2020, respectively, and are included in noncurrent receivables in the accompanying consolidated balance sheets.

Canon provides guarantees for its employees, affiliates and other companies. The guarantees for the employees are principally made for their housing loans. The guarantees for affiliates and other companies are made for their lease obligations and bank loans to facilitate financing.

Canon would have to perform under a guarantee if the borrower defaults on a payment within the contract terms. The contract terms are 1 year to 15 years in case of employees with housing loans, and 1 year to 5 years in case of affiliates and other companies with lease obligations and bank loans. The maximum amount of undiscounted payments Canon would have had to make in the event of default is ¥2,078 million at December 31, 2021. The carrying amounts of the liabilities recognized for Canon's obligations as a guarantor under those guarantees at December 31, 2021 were not significant.

Canon also offers assurance-type warranties under which it generally guarantees the performance of products delivered and services rendered for a certain period or term. Estimated product warranty costs are recorded at the time revenue is recognized and are included in selling, general and administrative expenses in the accompanying consolidated statements of income. Estimates for accrued product warranty costs are based on historical experience. Accrued product warranty costs are included in accrued expenses in the accompanying consolidated balance sheets and the changes for the years ended December 31, 2021 and 2020 are summarized as follows:

Years ended December 31	Millions of yen	
	2021	2020
Balance at beginning of the year	**14,300**	15,846
Additions	**15,687**	11,355
Utilization	**(11,928)**	(10,657)
Other	**(1,110)**	(2,244)
Balance at end of the year	**16,949**	14,300

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, and cash flows.

21. 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, 2021 and 2020 are set forth below. The following summary excludes cash and cash equivalents, trade receivables, noncurrent receivables, short-term loans, trade payables and accrued expenses, and the fair values of these instruments approximate their carrying amounts. The summary also excludes investments and derivative instruments which are disclosed in Note 2 and Note 22, and Note 18, respectively.

December 31	Millions of yen			
	2021		2020	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Long-term debt, including current installments	**(177,410)**	**(177,343)**	(346,317)	(346,275)

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 22.

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

No single customer accounted for more than 10 percent of consolidated trade receivables as of December 31, 2021 or 2020.

22. 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, 2021 and 2020.

December 31	Millions of yen			
	2021			
	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	—	500	—	500
Investments:				
Fund trusts and others	281	328	—	609
Equity securities	28,640	—	—	28,640
Prepaid expenses and other current assets:				
Derivatives	—	65	—	65
Total assets	28,921	893	—	29,814
Liabilities:				
Other current liabilities:				
Derivatives	—	2,119	—	2,119
Total liabilities	—	2,119	—	2,119

December 31	Millions of yen			
	2020			
	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	—	500	—	500
Investments:				
Fund trusts and others	284	248	—	532
Equity securities	18,683	—	—	18,683
Prepaid expenses and other current assets:				
Derivatives	—	533	—	533
Total assets	18,967	1,281	—	20,248
Liabilities:				
Other current liabilities:				
Derivatives	—	1,225	—	1,225
Total liabilities	—	1,225	—	1,225

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.

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.

Assets and liabilities measured at fair value on a nonrecurring basis

There were no significant assets or liabilities to be measured at fair value on a nonrecurring basis during the year ended December 31, 2021 and 2020.

23. SEGMENT INFORMATION

Canon reports in four segments: the Printing Business Unit, the Imaging Business Unit, the Medical Business Unit, and the Industrial and Others Business Unit, which are based on the organizational structure and information reviewed by Canon's management to evaluate results and allocate resources.

Based on the realignment of Canon's internal reporting and management structure, from 2021, Canon has changed the name and structure of segments from Office Business Unit, Imaging System Business Unit, Medical System Business Unit and Industry and Others Business Unit to Printing Business Unit, Imaging Business Unit, Medical Business Unit, and Industrial and Others Business Unit. Major changes include moving Inkjet printers from Imaging System Business Unit to the Printing Business Unit, the same business unit as Office multifunction devices (MFDs) and Laser multifunction printers (MFPs), and moving Network cameras from Industry and Others Business Unit to the Imaging Business Unit, the same business unit as Interchangeable-lens digital cameras. Prior period amounts also have been reclassified.

The primary products included in each segment are as follows:

Printing Business Unit:
Office multifunction devices (MFDs) / Document solutions /
Laser multifunction printers (MFPs) / Laser printers /
Inkjet printers / Image scanners / Calculators /
Digital continuous feed presses / Digital sheet-fed presses /
Large format printers

Imaging Business Unit:
Interchangeable-lens digital cameras / Interchangeable lenses /
Digital compact cameras /Compact photo printers /
Network cameras / Video management software /
Video content analytics software / Digital camcorders /
Digital cinema cameras / Broadcast equipment /
Multimedia projectors

Medical Business Unit:
Computed tomography (CT) systems /
Diagnostic ultrasound systems / Diagnostic X-ray systems /
Magnetic resonance imaging (MRI) systems /
Clinical chemistry analyzers / Digital radiography systems /
Ophthalmic equipment

Industrial and Others Business Unit:
Semiconductor lithography equipment / FPD (Flat panel display) lithography equipment / OLED display manufacturing equipment / Vacuum thin-film deposition equipment / Die bonders / Handy terminals / Document scanners

The accounting policies of the segments are substantially the same as those described in the significant accounting policies in Note 1. Canon evaluate results and allocate resources for each segment based on income before income taxes.

Information about operating results and assets for each segment as of and for the years ended December 31, 2021, 2020 and 2019 is as follows:

	Millions of yen					
	Printing	Imaging	Medical	Industrial and Others	Corporate and eliminations	Consolidated
2021:						
Net sales:						
External customers	**1,934,012**	**651,494**	**480,029**	**449,915**	**(2,093)**	**3,513,357**
Intersegment	**4,835**	**2,038**	**333**	**95,827**	**(103,033)**	**—**
Total	**1,938,847**	**653,532**	**480,362**	**545,742**	**(105,126)**	**3,513,357**
Operating cost and expenses	**1,713,154**	**574,814**	**450,942**	**501,434**	**(8,905)**	**3,231,439**
Operating profit	**225,693**	**78,718**	**29,420**	**44,308**	**(96,221)**	**281,918**
Other income (deductions)	**7,259**	**(256)**	**4,876**	**342**	**8,567**	**20,788**
Income before income taxes	**232,952**	**78,462**	**34,296**	**44,650**	**(87,654)**	**302,706**
Total assets	**1,009,922**	**236,143**	**311,247**	**345,883**	**2,847,693**	**4,750,888**
Depreciation and amortization	**69,549**	**21,840**	**12,435**	**27,677**	**89,745**	**221,246**
Capital expenditures	**63,609**	**12,069**	**11,888**	**25,759**	**65,675**	**179,000**
2020:						
Net sales:						
External customers	1,800,898	539,560	435,368	385,177	(760)	3,160,243
Intersegment	3,529	1,754	706	76,345	(82,334)	—
Total	1,804,427	541,314	436,074	461,522	(83,094)	3,160,243
Operating cost and expenses	1,657,319	535,584	410,830	441,006	4,957	3,049,696
Operating profit	147,108	5,730	25,244	20,516	(88,051)	110,547
Other income (deductions)	5,076	(778)	300	1,171	13,964	19,733
Income before income taxes	152,184	4,952	25,544	21,687	(74,087)	130,280
Total assets	913,931	239,605	286,749	348,614	2,836,715	4,625,614
Depreciation and amortization	69,725	22,201	11,781	28,720	95,398	227,825
Capital expenditures	56,613	12,540	7,244	21,276	64,054	161,727
2019:						
Net sales:						
External customers	2,089,024	660,105	437,456	405,114	1,600	3,593,299
Intersegment	3,440	1,601	1,069	88,670	(94,780)	—
Total	2,092,464	661,706	438,525	493,784	(93,180)	3,593,299
Operating cost and expenses*	1,908,436	634,773	411,781	465,197	(1,308)	3,418,879
Operating profit	184,028	26,933	26,744	28,587	(91,872)	174,420
Other income (deductions)	6,066	905	539	—	13,563	21,073
Income before income taxes	190,094	27,838	27,283	28,587	(78,309)	195,493
Total assets	1,002,778	288,545	273,525	310,110	2,896,960	4,771,918
Depreciation and amortization	74,958	24,561	11,760	29,086	96,962	237,327
Capital expenditures	61,789	18,929	7,074	28,436	95,000	211,228

* During 2019, the Company implemented a restructuring plan centered in Europe with the goal of reorganizing sales structure and improving profitability mainly in the Printing Business Unit. The employee severance charges in the Printing Business Unit under the plan for the year ended December 31, 2019 were ¥15,656 million and most of the charges are included in selling, general and administrative expenses in the consolidated statements of income. The restructuring charges for the years ended December 31, 2021 and 2020 were not significant.

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. Amortization costs of identified intangible assets resulting from the purchase price allocation of Toshiba Medical Systems Corporation (currently, Canon Medical Systems Corporation) are also included in corporate expenses. Segment assets are based on those directly associated with each segment. Corporate assets primarily consist of cash and cash equivalents, investments, deferred tax assets, goodwill, identified intangible assets from acquisitions and corporate properties. Capital expenditures represent the additions to property, plant and equipment and intangible assets measured on an accrual basis.

Information about sales by product and service to external customers for each segment for the years ended December 31, 2021, 2020 and 2019 is as follows:

Years ended December 31	Millions of yen		
	2021	2020	2019
Printing			
Office multifunction devices	**477,000**	455,357	573,297
Office others	**279,366**	267,123	292,378
Office	**756,366**	722,480	865,675
Laser printers	**560,159**	502,157	624,597
Inkjet printers and Others	**328,932**	326,041	296,622
Prosumer	**889,091**	828,198	921,219
Production	**288,555**	250,220	302,130
Total	**1,934,012**	1,800,898	2,089,024
Imaging			
Cameras	**432,885**	347,240	466,306
Network cameras and Others	**218,609**	192,320	193,799
Total	**651,494**	539,560	660,105
Medical			
Diagnostic equipment	**480,029**	435,368	437,456
Industrial and Others			
Lithography equipment	**213,699**	142,516	157,160
Industrial equipment	**112,274**	126,762	107,281
Others	**123,942**	115,899	140,673
Total	**449,915**	385,177	405,114
Corporate	**(2,093)**	(760)	1,600
Consolidated	**3,513,357**	3,160,243	3,593,299

Based on the realignment of Canon's internal reporting and management structure, from the beginning of 2021, Canon has changed products category. Production includes Digital continuous feed presses, Digital sheet-fed presses and Large format printers in the primary products. Network cameras and Others include Network cameras, Video management software, Video content analytics software, Digital camcorders, Digital cinema cameras, Broadcast equipment and Multimedia projectors in the primary products. Industrial equipment includes OLED display manufacturing equipment, Vacuum thin-film deposition equipment and Die bonders in the primary products. Prior period amounts also have been reclassified.

Information by major geographic area as of and for the years ended December 31, 2021, 2020 and 2019 is as follows:

	Millions of yen		
	2021	2020	2019
Net sales:			
Japan	**830,378**	806,305	872,534
Americas	**968,839**	852,451	1,029,078
Europe	**894,898**	795,616	882,480
Asia and Oceania	**819,242**	705,871	809,207
Total	**3,513,357**	3,160,243	3,593,299
Long-lived assets:			
Japan	**986,638**	1,011,109	1,053,074
Americas	**152,137**	133,648	148,669
Europe	**158,297**	175,516	191,050
Asia and Oceania	**141,915**	143,265	159,217
Total	**1,438,987**	1,463,538	1,552,010

Net sales are attributed to areas based on the location where the products are shipped and the services are performed 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 were ¥907,909 million, ¥801,376 million and ¥958,442 million for the years ended December 31, 2021, 2020 and 2019, respectively.

Long-lived assets represent property, plant and equipment, intangible assets, and operating lease right-of-use assets for each geographic area.

24. SUBSEQUENT EVENT

On January 5, 2022, Canon borrowed ¥70,000 million under its existing overdraft facilities with Mizuho Bank, Ltd. and MUFG Bank, Ltd. for required operating funds. Additionally, on March 16, 2022, Canon borrowed ¥30,000 million under its existing overdraft facilities with Mizuho Bank, Ltd. and MUFG Bank, Ltd. for required operating funds. The overdraft facilities bear interest at a rate equal to a base rate plus a spread.

SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS

Years ended December 31	Millions of yen				
	Balance at beginning of period	Addition-charged to income	Deduction bad debts written off	Translation adjustments and other	Balance at end of period
2021:					
Allowance for credit losses					
Trade receivables	**11,645**	**1,857**	**(1,540)**	**532**	**12,494**
Finance receivables	**3,068**	**2,331**	**(2,157)**	**549**	**3,791**
2020:					
Allowance for credit losses					
Trade receivables	10,359	3,419	(1,983)	(150)	11,645
Finance receivables	2,627	2,351	(2,199)	289	3,068
2019:					
Allowance for credit losses					
Trade receivables	11,477	1,840	(2,189)	(769)	10,359
Finance receivables	2,675	1,495	(1,653)	110	2,627

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) and 15d-15(f) promulgated under the Exchange Act, 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 U.S. 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 Canon; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of Canon are being made only in accordance with authorizations of management and directors of Canon; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of Canon's assets that could have a material effect on the financial statements.

Because there are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. 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, 2021. In making this assessment, management used the criteria established in Internal Control–Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

Based on its assessment, management concluded that, as of December 31, 2021, Canon's internal control over financial reporting was effective.

Canon's independent registered public accounting firm, Deloitte Touche Tohmatsu LLC, has issued an audit report on the effectiveness of Canon's internal control over financial reporting. This report appears in Item 18.

Remediation of Previously Reported Material Weaknesses in Internal Control over Financial Reporting

As described in Canon's previous Annual Report on Form 20-F, Canon's management concluded that Canon's internal control over financial reporting was not effective as of December 31, 2020 due to identified deficiencies in the risk assessment and control activities principles associated with the COSO framework, which, either individually or in the aggregate, constituted material weaknesses relating to (i) identifying and analyzing significant changes that could impact the system of internal control and control activities, and (ii) integrating control activities to ensure that responses to risks are performed in a timely manner. Factors contributing to the material weaknesses described above included the failure to generate or maintain sufficient evidence supporting Canon's consideration of the significant changes and the impact on its internal controls over financial reporting.

During the year ended December 31, 2021, management implemented measures to remediate the identified deficiencies, including generation and maintenance of sufficient evidence to support Canon's consideration of significant changes and the impact of such changes on its system of internal control and control activities. The following remediation steps were completed:

- Improved open and timely communications within the organization with established policies and procedures, in writing, to facilitate and maintain the identification of significant changes that could impact Canon's system of internal control and control activities
- Strengthened controls and documentation around management's review of accounting positions and treatment
- Implemented controls and documentation around management's review of the basis applied for transactions to be considered material to the financial statements in a timely manner.

As a result of these efforts, Canon's management concluded that the material weaknesses had been remediated as of December 31, 2021.

Fujio Mitarai
Chairman & CEO

Toshizo Tanaka
Executive Vice President & CFO

March 30, 2022

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Deloitte.

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To the Shareholders and the Board of Directors of
Canon Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Canon Inc. and subsidiaries (the "Company") as of December 31, 2021 and 2020, the related consolidated statements of income, comprehensive income, equity, and cash flows, for each of the two years in the period ended December 31, 2021, and the related notes and the schedule listed in the Index at Item 18 (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021 and 2020, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2021, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2021, based on criteria established in *Internal Control — Integrated Framework (2013*) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 30, 2022, expressed an unqualified opinion on the Company's internal control over financial reporting.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current-period audit of the financial statements that were communicated or required to be communicated to the audit committee and that (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Goodwill—Medical Reporting Unit—Refer to Notes 1 and 8 to the Financial Statements

Critical Audit Matter Description

The Company tests goodwill for impairment annually in the fourth quarter of each year, or more frequently if indicators of potential impairment exist. Fair value of a reporting unit is determined primarily based on the discounted cash flow analysis, which involves estimates of projected future cash flows and discount rates. The Company's total consolidated goodwill was ¥953,850 million as of December 31, 2021, of which ¥537,183 million was allocated to the Medical Reporting Unit. Estimates of projected future cash flows for the Medical Reporting Unit are based on a mid-term management plan that considered the future market growth of medical equipment and growth in geographies where the Company operates its medical business. Estimates of discount rates are determined based on the weighted average cost of capital, which considers primarily market and industry data as well as specific risk factors. With regard to the goodwill attributed to the Medical Reporting Unit, fair value in excess of reported carrying value as a percentage is lower than other reporting units. As a result, a future reduction in cash flows of the Medical Reporting Unit could trigger an impairment.

Given the significant judgments made by management to estimate the fair value of the Medical Reporting Unit, performing audit procedures to evaluate the reasonableness of management's estimates and assumptions related to the projected future cash flows and selection of the discount rate required a high degree of auditor judgment and an increased extent of effort, including the need to involve fair value specialists.

How the Critical Audit Matter Was Addressed in the Audit

Our audit procedures related to the projected future cash flows and selection of the discount rate used by management to estimate the fair value of the Medical Reporting Unit included the following, among others:

- We tested the effectiveness of controls over management's goodwill impairment evaluation, including management's controls over projected future cash flows and selection of the discount rate.
- We evaluated management's ability to accurately project future cash flows by comparing actual results to management's historical projections.
- We evaluated the reasonableness of management's projected future cash flows by comparing the projections to:
  - —Historical cash flows.
  - —Internal communications to management and the Board of Directors.
  - —Projected information included in Company press releases as well as in analyst and industry reports for the Company and certain of its peer companies.
- With the assistance of our fair value specialists, we evaluated the reasonableness of the valuation methodology and discount rate by:
  - —Examining whether the methodology, assumptions, and models used were consistent with existing valuation practices that are both generally accepted in practice and recognized as appropriate in similar circumstances and testing the use and weighting of valuation techniques.
  - —Testing the source information underlying the determination of the discount rate and the mathematical accuracy of the calculation.
  - —Developing a range of independent estimates and comparing those to the discount rate selected by management.

Revenue—Long-Term Contracts in the Industrial and Others Segment—Refer to Note 15 to the Financial Statements

Critical Audit Matter Description

The Company recognized revenue on long-term contracts of certain industrial equipment in the Industrial and Others segment totaling ¥105,828 million for the year ended December 31, 2021. The Company recognized revenue over the contract term ("over time") for long-term contracts of certain industrial equipment for which there is no alternative use and for which the Company has an enforceable right to payment from customers for performance completed to date. The Company considers costs incurred and future project costs in accordance with the input method to determine progress, and as such, revenue is recognized over time based on costs incurred to date plus the estimate of margins at completion. Changes in job performance, job conditions, estimated margin and final contract settlements may result in revisions to projected costs and revenue and are recognized in the period in which the revisions to estimates are identified and the amounts can be reasonably estimated. Factors that may affect future project costs and margins include production efficiencies and availability and costs of labor and materials.

Given the judgments necessary to estimate future project costs and the margins at completion of certain long-term contracts for certain industrial equipment in the Industrial and Others segment, auditing these estimates for certain contracts required extensive audit effort and a high degree of auditor judgment.

How the Critical Audit Matter Was Addressed in the Audit

Our audit procedures related to the estimates of future costs and the margins at completion for certain long-term contracts of industrial equipment in the Industrial and Others segment included the following, among others:

- We tested the effectiveness of controls over long-term contract revenue recognized over time, including management's controls over the estimates of future costs and the margins at completion for certain long-term contracts.
- We evaluated management's ability to estimate future costs and margins at completion accurately by comparing actual costs and margins at completion for similar contracts that were previously completed to management's historical estimates for such contracts.
- We evaluated the reasonableness of management's estimates of future costs and margins at completion by comparing the estimates to management's work plans, engineering specifications, meeting minutes and fee proposals, and by performing corroborating inquiries with management, project managers, and engineers, among others.
- We selected samples from actual costs incurred subsequent to December 31, 2021 and traced them to the future costs estimate schedule to determine whether the selected cost was properly considered in the future costs.

Deloitte Touche Tohmatsu LLC

March 30, 2022

We have served as the Company's auditor since 2020.

Deloitte.

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To the Shareholders and the Board of Directors of
Canon Inc.

Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of Canon Inc. and subsidiaries (the "Company") as of December 31, 2021, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2021, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements as of and for the year ended December 31, 2021, of the Company and our report dated March 30, 2022, expressed an unqualified opinion on those financial statements.

Basis for Opinion

The Company's 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 are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. 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.

Definition and Limitations of Internal Control over Financial Reporting

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.

Deloitte Touche Tohmatsu LLC

March 30, 2022

EY
Building a better working world

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To the Shareholders and the Board of Directors of
Canon Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated statements of income, comprehensive income, equity and cash flows of Canon Inc. and subsidiaries (the Company) for the year ended December 31, 2019, and the related notes and financial statement schedule listed in the Index at Item 18 (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the results of the Company's operations and its cash flows for the year ended December 31, 2019, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Ernst & Young ShinNihon LLC

We served as the Company's auditor for SEC reporting purposes from 2004, and as its Japanese statutory auditor from 1978, to 2020.

Tokyo, Japan
March 27, 2020,
except for the effects on the consolidated financial statement of the correction of an error as described in Note 1(y) and the realignment of segments described in Note 23, as to which the dates are
March 30, 2021 and March 30, 2022, respectively

TRANSFER AND REGISTRAR'S OFFICE

Canon Inc.

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

Manager of the Register of Shareholders

Mizuho Trust & Banking Co., Ltd.
1-3-3, Marunouchi, Chiyoda-ku, Tokyo 100-8241, Japan

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

JPMorgan Chase Bank, N.A.
383 Madison Avenue, Floor 11, New York, NY 10179, USA

SHAREHOLDER INFORMATION

Stock Exchange Listings:

Tokyo, 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 of each year

Further Information:

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

MAJOR CONSOLIDATED SUBSIDIARIES

(As of December 31, 2021)

Manufacturing

Canon Precision Inc.
Canon Tokki Corporation
Fukushima Canon Inc.
Canon Medical Systems Corporation
Canon Electron Tubes & Devices Co., Ltd.
Canon Components, Inc.
Canon Semiconductor Equipment Inc.
Canon Chemicals Inc.
Canon Electronics Inc.
Canon Finetech Nisca Inc.
Canon ANELVA Corporation
Nagahama Canon Inc.
Canon Machinery Inc.
Oita Canon Materials Inc.
Oita Canon Inc.
Nagasaki Canon Inc.
Miyazaki Canon Inc.
Canon Virginia, Inc.
Canon Bretagne S.A.S.
Canon Production Printing Netherlands B.V.
Canon Production Printing Germany GmbH & Co.KG
Axis Communications AB
Canon Dalian Business Machines, Inc.
Canon (Suzhou) Inc.
Canon Zhongshan Business Machines Co., Ltd.
Canon Inc., Taiwan
Canon Vietnam Co., Ltd.
Canon Hi-Tech (Thailand) Ltd.
Canon Prachinburi (Thailand) Ltd.
Canon Business Machines (Philippines), Inc.
Canon Opto (Malaysia) Sdn. Bhd.
Canon Medical Systems Manufacturing Asia Sdn. Bhd.
Canon Machinery (Malaysia) Sdn. Bhd.

Research & Development

Canon Research Centre France S.A.S.

Marketing & Other

Canon Marketing Japan Inc.
Canon System and Support Inc.
Canon IT Solutions Inc.
Canon Medical Finance Co., Ltd.
Canon U.S.A., Inc.
Canon Canada Inc.
Canon Solutions America, Inc.
Canon Financial Services, Inc.
Canon Medical Systems USA, Inc.
Axis AB
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 Italia S.p.A.
Canon Medical Systems Europe B.V.
Milestone Systems A/S
Canon (China) Co., Ltd.
Canon Hongkong Co., Ltd.
Canon Semiconductor Equipment Taiwan, Inc.
Canon Singapore Pte. Ltd.
Canon India Pvt. Ltd.
Canon Australia Pty. Ltd.

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