

CHUGOKU MARINE PAINTS, LTD.

**Consolidated Financial Statements
for the years ended March 31, 2017 and 2016**



Independent Auditor's Report

The Board of Directors
CHUGOKU MARINE PAINTS, LTD.

We have audited the accompanying consolidated financial statements of CHUGOKU MARINE PAINTS, LTD. and its consolidated subsidiaries, which comprise the consolidated balance sheet as at March 31, 2017, and the consolidated statements of income, comprehensive income, changes in net assets, and cash flows for the year then ended and a summary of significant accounting policies and other explanatory information, all expressed in Japanese yen.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of CHUGOKU MARINE PAINTS, LTD. and its consolidated subsidiaries as at March 31, 2017, and their consolidated financial performance and cash flows for the year then ended in conformity with accounting principles generally accepted in Japan.

Convenience Translation

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

Ernst & Young ShinNihon LLC

June 22, 2017

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Balance Sheets

March 31, 2017 and 2016

ASSETS	Millions of Yen		Thousands of U.S. Dollars (Note 4)
	<u>2017</u>	<u>2016</u>	<u>2017</u>
Current assets:			
Cash on hand and in banks (Notes 17 and 19)	¥ 36,918	¥ 34,019	\$ 329,067
Trade notes and accounts receivable (Note 19)	32,605	42,043	290,623
Short-term investment securities (Notes 16 and 19)	186	255	1,658
Inventories (Note 5)	14,057	15,961	125,296
Deferred tax assets (Note 11)	1,064	1,082	9,484
Other current assets	1,289	1,132	11,490
Allowance for doubtful accounts (Note 19)	(2,118)	(2,433)	(18,879)
Total current assets	<u>84,001</u>	<u>92,059</u>	<u>748,739</u>
Property, plant and equipment:			
Buildings and structures	18,957	19,080	168,972
Machinery, equipment and vehicles	15,992	15,749	142,544
Tools, furniture and fixtures	4,604	4,542	41,038
	<u>39,553</u>	<u>39,371</u>	<u>352,554</u>
Less, accumulated depreciation	(28,305)	(27,871)	(252,295)
	<u>11,248</u>	<u>11,500</u>	<u>100,259</u>
Land	13,181	13,208	117,488
Construction in progress	2,398	404	21,374
Total property, plant and equipment	<u>26,827</u>	<u>25,112</u>	<u>239,121</u>
Investments and other assets:			
Investment securities (Notes 6, 16 and 19)	8,382	8,314	74,713
Net defined benefit asset (Note 7)	81	45	722
Deferred tax assets (Note 11)	549	546	4,893
Other assets	2,218	2,314	19,770
Total investments and other assets	<u>11,230</u>	<u>11,219</u>	<u>100,098</u>
Total assets	<u>¥ 122,058</u>	<u>¥ 128,390</u>	<u>\$1,087,958</u>

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Balance Sheets

March 31, 2017 and 2016

LIABILITIES AND NET ASSETS	Millions of Yen		Thousands of U.S. Dollars (Note 4)
	2017	2016	2017
Current liabilities:			
Short-term borrowings (Notes 6 and 19)	¥ 17,356	¥ 18,521	\$ 154,702
Current portion of long-term debt (Note 6)	32	1,058	285
Notes and accounts payable:			
Trade (Note 19)	11,646	14,379	103,806
Other	2,744	3,336	24,458
	<u>14,390</u>	<u>17,715</u>	<u>128,264</u>
Income taxes payable (Note 11)	837	1,670	7,461
Other current liabilities (Note 6)	3,886	4,186	34,637
Total current liabilities	<u>36,501</u>	<u>43,150</u>	<u>325,349</u>
Non-current liabilities:			
Long-term debt (Note 6)	2,706	1,728	24,120
Net defined benefit liability (Note 7)	1,356	1,345	12,087
Deferred tax liabilities on land revaluation	2,252	2,252	20,073
Deferred tax liabilities (Note 11)	605	589	5,392
Other liabilities (Note 6)	469	509	4,181
Total non-current liabilities	<u>7,388</u>	<u>6,423</u>	<u>65,853</u>
Total liabilities	<u>43,889</u>	<u>49,573</u>	<u>391,202</u>
Net assets (Note 8):			
Shareholders' equity:			
Common stock	11,626	11,626	103,628
Capital surplus	7,784	7,784	69,382
Retained earnings	49,046	46,522	437,169
Treasury stock, at cost	(1,703)	(1,201)	(15,179)
Total shareholders' equity	<u>66,753</u>	<u>64,731</u>	<u>595,000</u>
Accumulated other comprehensive income:			
Net unrealized holding gain on other securities	2,109	2,015	18,798
Revaluation gain on land	3,863	3,863	34,433
Foreign currency translation adjustments	(32)	2,677	(285)
Remeasurements of defined benefit plans (Note 7)	(143)	(153)	(1,275)
Total accumulated other comprehensive income	<u>5,797</u>	<u>8,402</u>	<u>51,671</u>
Non-controlling interests	<u>5,619</u>	<u>5,684</u>	<u>50,085</u>
Total net assets (Note 15)	<u>78,169</u>	<u>78,817</u>	<u>696,756</u>
Commitments and contingent liabilities (Note 14)			
Total liabilities and net assets	<u>¥ 122,058</u>	<u>¥ 128,390</u>	<u>\$1,087,958</u>

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Statements of Income

For the years ended March 31, 2017 and 2016

	Millions of Yen		Thousands of U.S. Dollars (Note 4)
	<u>2017</u>	<u>2016</u>	<u>2017</u>
Net sales	¥ 82,368	¥ 115,067	\$ 734,183
Cost of sales (Note 5)	<u>55,759</u>	<u>78,927</u>	<u>497,005</u>
Gross profit	26,609	36,140	237,178
Selling, general and administrative expenses (Note 9)	<u>21,138</u>	<u>26,127</u>	<u>188,413</u>
Operating profit	<u>5,471</u>	<u>10,013</u>	<u>48,765</u>
Non-operating income (expenses):			
Interest and dividend income	507	495	4,519
Interest expense	(316)	(296)	(2,817)
Foreign currency exchange gain (loss), net	41	(275)	366
Royalty income	77	97	686
Revenue from technical training	84	107	749
Rental income	109	123	972
Other, net	<u>103</u>	<u>153</u>	<u>918</u>
Non-operating income, net	<u>605</u>	<u>404</u>	<u>5,393</u>
Ordinary profit	6,076	10,417	54,158
Special gains (losses), net (Note 10)	<u>78</u>	<u>(33)</u>	<u>695</u>
Profit before income taxes	<u>6,154</u>	<u>10,384</u>	<u>54,853</u>
Income taxes (Note 11):			
Current	1,838	3,077	16,383
Deferred	<u>(5)</u>	<u>(147)</u>	<u>(45)</u>
	1,833	2,930	16,338
Profit	<u>4,321</u>	<u>7,454</u>	<u>38,515</u>
Profit attributable to non-controlling interests	<u>678</u>	<u>952</u>	<u>6,043</u>
Profit attributable to owners of parent (Note 15)	<u>¥ 3,643</u>	<u>¥ 6,502</u>	<u>\$ 32,472</u>

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income For the years ended March 31, 2017 and 2016

	Millions of Yen		Thousands of U.S. Dollars (Note 4)
	2017	2016	2017
Profit	¥ 4,321	¥ 7,454	\$ 38,515
Other comprehensive income (Note 20):			
Net unrealized holding gain (loss) on other securities	95	(2,047)	847
Revaluation reserve for land	—	118	—
Foreign currency translation adjustments	(3,010)	(3,050)	(26,829)
Remeasurements of defined benefit plans	8	(244)	71
Total other comprehensive income	(2,907)	(5,223)	(25,911)
Comprehensive income	¥ 1,414	¥ 2,231	\$ 12,604
Total comprehensive income attributable to			
Owners of parent	¥ 1,039	¥ 1,720	\$ 9,261
Non-controlling interests	375	511	3,343

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets

For the years ended March 31, 2017 and 2016

For the year ended March 31, 2017

	Millions of Yen						
	Shareholders' equity						Total shareholders' equity
	Number of shares of common stock issued (Thousands)	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost		
Balance as of April 1, 2016	69,069	¥ 11,626	¥ 7,784	¥ 46,522	¥ (1,201)	¥ 64,731	
Cash dividends				(1,119)		(1,119)	
Profit attributable to owners of parent				3,643		3,643	
Acquisition of treasury stock					(502)	(502)	
Disposal of treasury stock			0		0	0	
Net changes in items other than shareholders' equity							
Total changes in items during the year		—	0	2,524	(502)	2,022	
Balance as of March 31, 2017	69,069	¥ 11,626	¥ 7,784	¥ 49,046	¥ (1,703)	¥ 66,753	
	Accumulated other comprehensive income						
	Net unrealized holding gain on other securities	Revaluation gain on land	Foreign currency translation adjustments	Remeasurements of defined benefit plans	Total accumulated other comprehensive income	Non-controlling interests	Total net assets
Balance as of April 1, 2016	¥ 2,015	¥ 3,863	¥ 2,677	¥ (153)	¥ 8,402	¥ 5,684	¥ 78,817
Cash dividends							(1,119)
Profit attributable to owners of parent							3,643
Acquisition of treasury stock							(502)
Disposal of treasury stock							0
Net changes in items other than shareholders' equity	94		(2,709)	10	(2,605)	(65)	(2,670)
Total changes in items during the year	94	—	(2,709)	10	(2,605)	(65)	(648)
Balance as of March 31, 2017	¥ 2,109	¥ 3,863	¥ (32)	¥ (143)	¥ 5,797	¥ 5,619	¥ 78,169
	Thousands of U.S. Dollars (Note 4)						
	Shareholders' equity						
	Number of shares of common stock issued (Thousands)	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Total shareholders' equity	
Balance as of April 1, 2016	69,069	\$ 103,628	\$ 69,382	\$ 414,672	\$ (10,705)	\$ 576,977	
Cash dividends				(9,975)		(9,975)	
Profit attributable to owners of parent				32,472		32,472	
Acquisition of treasury stock					(4,474)	(4,474)	
Disposal of treasury stock			0		0	0	
Net changes in items other than shareholders' equity							
Total changes in items during the year		—	0	22,497	(4,474)	18,023	
Balance as of March 31, 2017	69,069	\$ 103,628	\$ 69,382	\$ 437,169	\$ (15,179)	\$ 595,000	
	Accumulated other comprehensive income						
	Net unrealized holding gain on other securities	Revaluation gain on land	Foreign currency translation adjustments	Remeasurements of defined benefit plans	Total accumulated other comprehensive income	Non-controlling interests	Total net assets
Balance as of April 1, 2016	\$ 17,961	\$ 34,433	\$ 23,861	\$ (1,364)	\$ 74,891	\$ 50,664	\$ 702,532
Cash dividends							(9,975)
Profit attributable to owners of parent							32,472
Acquisition of treasury stock							(4,474)
Disposal of treasury stock							0
Net changes in items other than shareholders' equity	837		(24,146)	89	(23,220)	(579)	(23,799)
Total changes in items during the year	837	—	(24,146)	89	(23,220)	(579)	(5,776)
Balance as of March 31, 2017	\$ 18,798	\$ 34,433	\$ (285)	\$ (1,275)	\$ 51,671	\$ 50,085	\$ 696,756

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets For the years ended March 31, 2017 and 2016

For the year ended March 31, 2016

	Millions of Yen						
	Shareholders' equity						Total shareholders' equity
	Number of shares of common stock issued (Thousands)	Common Stock	Capital surplus	Retained earnings	Treasury stock, at cost		
Balance as of April 1, 2015	69,069	¥ 11,626	¥ 7,784	¥ 41,079	¥ (1,192)	¥ 59,297	
Cash dividends				(1,059)		(1,059)	
Profit attributable to owners of parent				6,502		6,502	
Acquisition of treasury stock					(9)	(9)	
Net changes in items other than shareholders' equity							
Total changes in items during the year		—	—	5,443	(9)	5,434	
Balance as of March 31, 2016	69,069	¥ 11,626	¥ 7,784	¥ 46,522	¥ (1,201)	¥ 64,731	
	Accumulated other comprehensive income						
	Net unrealized holding gain on other securities	Revaluation gain on land	Foreign currency translation adjustments	Remeasure- ments of defined benefit plans	Total accumulated other comprehensive income	Non-controlling interests	Total net assets
Balance as of April 1, 2015	¥ 4,063	¥ 3,745	¥ 5,292	¥ 84	¥ 13,184	¥ 5,745	¥ 78,226
Cash dividends							(1,059)
Profit attributable to owners of parent							6,502
Acquisition of treasury stock							(9)
Net changes in items other than shareholders' equity	(2,048)	118	(2,615)	(237)	(4,782)	(61)	(4,843)
Total changes in items during the year	(2,048)	118	(2,615)	(237)	(4,782)	(61)	591
Balance as of March 31, 2016	¥ 2,015	¥ 3,863	¥ 2,677	¥ (153)	¥ 8,402	¥ 5,684	¥ 78,817

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

For the years ended March 31, 2017 and 2016

	Millions of Yen		Thousands of U.S. Dollars (Note 4)
	<u>2017</u>	<u>2016</u>	<u>2017</u>
Cash flows from operating activities:			
Profit before income taxes	¥ 6,154	¥ 10,384	\$ 54,853
Depreciation and amortization	1,728	1,738	15,402
Increase in allowance for doubtful accounts	47	602	419
Increase in net defined benefit asset	(36)	(45)	(321)
Increase (decrease) in net defined benefit liability	32	(67)	285
Interest and dividend income	(507)	(495)	(4,519)
Interest expense	316	296	2,817
Foreign currency exchange loss, net	102	434	909
Loss on sales of property, plant and equipment, net	9	5	80
(Gain) loss on sales of investment securities	(113)	2	(1,007)
Loss on valuation of investment securities	29	20	259
Decrease in trade notes and accounts receivable	7,115	3,128	63,419
Decrease in inventories	1,138	781	10,144
Decrease in trade notes and accounts payable	(2,094)	(4,448)	(18,665)
Other, net	(552)	631	(4,920)
Subtotal	<u>13,368</u>	<u>12,966</u>	<u>119,155</u>
Interest and dividend income received	502	489	4,475
Interest expense paid	(320)	(301)	(2,852)
Income taxes paid	(2,800)	(2,823)	(24,958)
Settlement package paid	—	(557)	—
Net cash provided by operating activities	<u>10,750</u>	<u>9,774</u>	<u>95,820</u>
Cash flows from investing activities:			
Increase in time deposits	(17,543)	(12,380)	(156,368)
Decrease in time deposits	16,009	10,904	142,696
Decrease (increase) in short-term loans receivable, net	10	(1)	89
Payments for purchases of investment securities	(116)	(526)	(1,034)
Decrease in short-term investment securities, net	—	106	—
Payments for purchases of property, plant and equipment	(3,941)	(1,661)	(35,128)
Proceeds from sales of property, plant and equipment	7	18	62
Proceeds from sales of investment securities	192	0	1,711
Other, net	(66)	(12)	(588)
Net cash used in investing activities	<u>¥ (5,448)</u>	<u>¥ (3,552)</u>	<u>\$ (48,560)</u>

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

For the years ended March 31, 2017 and 2016

	Millions of Yen		Thousands of U.S. Dollars (Note 4)
	<u>2017</u>	<u>2016</u>	<u>2017</u>
Cash flows from financing activities:			
Decrease in short-term borrowings, net	¥ (556)	¥ (844)	\$ (4,956)
Increase in long-term debt	1,010	1,700	9,002
Repayment of long-term debt	(1,058)	(2,346)	(9,430)
Proceeds from sales of treasury stock	0	—	0
Payments for purchases of treasury stock	(502)	(9)	(4,474)
Cash dividends	(1,120)	(1,060)	(9,983)
Other, net	<u>(511)</u>	<u>(575)</u>	<u>(4,555)</u>
Net cash used in financing activities	<u>(2,737)</u>	<u>(3,134)</u>	<u>(24,396)</u>
Effect of exchange rate changes on cash and cash equivalents	<u>(990)</u>	<u>(660)</u>	<u>(8,825)</u>
Net increase in cash and cash equivalents	<u>1,575</u>	<u>2,428</u>	<u>14,039</u>
Cash and cash equivalents at beginning of year	<u>26,828</u>	<u>24,400</u>	<u>239,130</u>
Cash and cash equivalents at end of year (Note 17)	<u>¥ 28,403</u>	<u>¥ 26,828</u>	<u>\$ 253,169</u>

The accompanying notes are an integral part of these consolidated financial statements.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

1. Summary of Significant Accounting Policies

a. Basis of presentation

The accompanying consolidated financial statements of CHUGOKU MARINE PAINTS, LTD. (the “Company”) and its consolidated subsidiaries (collectively, the “Companies”) have been prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and have been compiled from the consolidated financial statements prepared by the Company as required by the Financial Instruments and Exchange Act of Japan.

Certain amounts from prior years have been reclassified to conform to the current year’s presentation.

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

b. Principles of consolidation and accounting for investments in unconsolidated subsidiaries and affiliates

The accompanying consolidated financial statements include the accounts of the Companies. As of March 31, 2017 and 2016, the Company consolidated 24 subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Any difference between the cost of an investment in a subsidiary and the amount of underlying equity in net assets (goodwill) is treated as an asset, and amortized on a straight-line basis over a period of five years.

The fiscal year-ends of consolidated subsidiaries are December 31, except for Kobe Paints, Ltd., whose year-end is March 31. For consolidation purposes, the Company uses their financial statements as of and for the year ended December 31 except for Kobe Paints, Ltd. with necessary consolidation adjustments made to reflect any significant transactions which occurred between January 1 and March 31.

As of March 31, 2017 and 2016, there were no unconsolidated subsidiaries or affiliates accounted for by the equity method.

c. Foreign currency translation

The Company translates the revenue and expense accounts of the overseas consolidated subsidiaries at the average rates of exchange in effect during the year. The balance sheet accounts, except for the components of shareholders’ equity, are translated into yen at the rates of exchange in effect at the balance sheet date. The components of shareholders’ equity are translated at their historical exchange rates. Differences arising from translation where two exchange rates have been used are presented under “Foreign currency translation adjustments” and “Non-controlling interests” which are components of net assets.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

Current and non-current monetary assets and liabilities denominated in foreign currencies of the Company and its domestic consolidated subsidiaries are translated into yen at the exchange rates in effect at the balance sheet date, except for those hedged by forward foreign exchange contracts which are translated at the contracted rates. All revenues and expenses denominated in foreign currencies of the Company and its domestic consolidated subsidiaries are translated at the average rates of exchange during the year. Gains and losses arising from foreign exchange translation differences are credited or charged to income in the years in which they are made or incurred, except for those arising from forward foreign exchange contracts.

d. Cash and cash equivalents

Cash and cash equivalents in the consolidated statements of cash flows are composed of cash on hand, bank deposits withdrawable on demand, and short-term investment securities with an original maturity of three months or less which are readily convertible to cash and represent a minor risk of fluctuation in value.

e. Inventories

Inventories are mainly stated at cost determined by the moving-average method. Balance sheet amounts are calculated based on the method of reducing the book value in accordance with any decline in profitability.

f. Short-term investment securities and investment securities

Held-to-maturity bonds are either amortized or accumulated to face value. Other securities with quoted market prices are carried at market value. The difference between the acquisition cost and the carrying value of other securities, including unrealized gains and losses, net of the applicable income taxes, is recognized as a component of net assets and is reflected as "Net unrealized holding gain on other securities." The cost of other securities sold is computed by the moving-average method. Other securities without quoted market prices are stated at cost based on the moving-average method.

If a decline in fair value below cost of an individual security is deemed to be material and other than temporary, the carrying value of the individual security is written down.

g. Property, plant and equipment and depreciation (except leased assets)

Property, plant and equipment are stated on the basis of cost. The Company and the domestic consolidated subsidiaries calculate depreciation principally by the declining-balance method based on the estimated useful lives of the respective assets, except for buildings (exclusive of any facilities attached to buildings) acquired on or after April 1, 1998 and facilities attached to buildings and structures acquired on or after April 1, 2016, which are depreciated by the straight-line method. The overseas consolidated subsidiaries calculate depreciation principally by the straight-line method.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

h. Intangible assets (except leased assets)

Intangible assets, included in other assets, are amortized on a straight-line basis over the period stipulated in the Corporation Tax Act of Japan, except for computer software for internal use which is amortized on a straight-line basis over its estimated useful lives (three to ten years).

i. Leases

Noncancellable lease transactions that transfer substantially all risks and rewards associated with the ownership of assets are accounted for as finance leases. All other lease transactions are accounted for as operating leases and relating payments are charged to expense as incurred.

Leased assets capitalized as finance leases are initially accounted for at their acquisition costs and depreciated over the respective lease term by the straight-line method with a zero residual value.

j. Allowance for doubtful accounts

Allowance for doubtful accounts is provided to cover possible losses on uncollectible accounts. It consists of an estimated uncollectible amount with respect to identified doubtful receivables and an amount calculated based on the historical bad debt ratio with respect to the remaining receivables.

k. Accrued product warranty costs

Accrued product warranty costs are included in "Other current liabilities." Provision for estimated warranty costs is recorded based on the ratio of actual warranty costs incurred for the year against the related annual sales amount.

l. Accrued bonuses

Accrued bonuses are included in "Other current liabilities." Certain consolidated subsidiaries provide for accrued bonuses for employees based on the amount attributed to services rendered during the year and estimated to be paid.

m. Retirement benefits

(i) Method for attributing expected retirement benefits to periods

In the calculation of retirement benefit obligations, the expected retirement benefits are attributed to periods up to the end of the current fiscal year based on the benefit formula method.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

(ii) Accounting method for actuarial gains and losses

The actuarial gains and losses are amortized from the year following the year in which the gains or losses are recognized by the straight-line method over a certain period (10 years) that is within the average remaining years of service of the eligible employees when the gains or losses occur.

(iii) Application of the simplified method for small-sized enterprises

Certain consolidated subsidiaries apply the simplified method in the calculation of their net defined benefit liability and retirement benefit expenses. Under the simplified method, the benefits payable assuming the voluntary retirement of all eligible employees at the fiscal year-end are deemed as the retirement benefit obligations.

n. Income taxes

Income taxes of the Company and its domestic subsidiaries consist of corporate income tax, local inhabitant taxes and enterprise tax.

Deferred income taxes are determined using the asset and liability method, whereby deferred tax assets and liabilities are recognized in respect of temporary differences between the tax bases of the assets and liabilities and the amounts reported in the financial statements.

o. Consumption taxes

The consumption taxes paid and withheld on purchases and sales of goods and services are not included in the respective amounts of cost, expense or revenue in the accompanying consolidated statements of income. The net balance of consumption taxes withheld and paid is included in “Other current assets” or “Other current liabilities” in the accompanying consolidated balance sheets.

p. Derivative financial instruments

All derivatives are stated at fair value, with changes in fair value included in profit or loss for the period in which they arise unless derivative instruments are used for hedging purposes. Certain consolidated subsidiaries utilize forward foreign exchange contracts to reduce the risk arising from exchange rate fluctuations in foreign-currency-denominated receivables and payables. Receivables and payables hedged by qualified forward foreign exchange contracts are translated at the corresponding contract rates when the criteria are met.

At inception, the forward foreign exchange contracts are fixed at the same amount and at the same maturing as the hedged items in accordance with the Company’s risk management objective and policy for undertaking the hedge. As certain subsidiaries deem the hedging relationship regarding exchange rate fluctuations to be highly effective, the evaluation of hedge effectiveness at the fiscal year-end is not performed.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

q. Impairment on fixed assets

In accordance with the accounting standard for impairment of fixed assets, the Companies periodically review their fixed assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Companies recognize an impairment loss in their statement of income if certain indicators of asset impairment exist and if the book value of an asset exceeds the undiscounted sum of its future cash flows. The standard states that impairment losses should be measured as the excess of the book value over the higher of (1) the fair market value of the asset, net of disposition costs, or (2) the present value of future cash flows arising from ongoing utilization of the asset and from its disposal after use. The standard covers land, factories, buildings and other forms of property, plant and equipment as well as intangible assets. Fixed assets are to be grouped at the lowest levels for which there are identifiable cash flows which are independent of the cash flows from other groups of assets.

r. Earnings and cash dividends per share

Basic earnings per share of common stock is based on the weighted average number of shares of common stock outstanding during each period.

Diluted earnings per share has not been presented for both the years ended March 31, 2017 and 2016 as the Company had no potentially dilutive shares of common stock.

Cash dividends per share is applicable to the respective years and includes dividends to be paid on or after the effective date. Dividends are charged to retained earnings in the year in which they are paid.

Net assets per share is computed based on the net assets reduced by non-controlling interests and the number of shares of common stock outstanding at the year-end.

s. Shareholders' equity

The Companies Act of Japan (the "Act") provides that an amount equal to 10% of the amount of the deduction from surplus as a result of the payment of such dividends of surplus shall be transferred to additional paid-in capital (a component of "Capital surplus") or legal reserve (a component of "Retained earnings") on the dividend date until the sum of additional paid-in capital and legal reserve equals 25% of the common stock account. Such distributions can be made at any time by resolution of the shareholders' meeting or the board of directors if certain conditions are met.

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Notes to Consolidated Financial Statements

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2. Accounting Changes

Adoption of Practical Solution on a Change in Depreciation Method due to Tax Reform 2016

Due to amendments to the Corporation Tax Act of Japan, the Companies adopted the “Practical Solution on a change in depreciation method due to Tax Reform 2016” (Accounting Standards Board of Japan (ASBJ) Practice Issue Task Force No. 32, issued on June 17, 2016) from the year ended March 31, 2017. Accordingly, the depreciation method for facilities attached to buildings and structures acquired on or after April 1, 2016 was changed from the declining-balance method to the straight-line method.

The effect of this change on the consolidated financial statements for the year ended March 31, 2017 is immaterial.

3. Additional Information

Adoption of Revised Implementation Guidance on Recoverability of Deferred Tax Assets

The Companies adopted the “Revised Implementation Guidance on Recoverability of Deferred Tax Assets” (ASBJ Guidance No. 26, issued on March 28, 2016) from the year ended March 31, 2017.

4. U.S. Dollar Amounts

Amounts in U.S. dollars are included solely for the convenience of readers outside Japan. The rate of ¥112.19 = U.S. \$1.00, the rate of exchange prevailing as of March 31, 2017, has been used in the translation. The inclusion of such amounts is not intended to imply that Japanese yen has been or could be readily converted, realized or settled in U.S. dollars at this or any other rate.

5. Inventories

Inventories as of March 31, 2017 and 2016 comprised of the following:

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Merchandise and finished goods	¥ 7,831	¥ 9,199	\$ 69,801
Raw materials and supplies	5,770	6,354	51,431
Work in process	456	408	4,064
Total	<u>¥ 14,057</u>	<u>¥ 15,961</u>	<u>\$ 125,296</u>

Cost of sales for the years ended March 31, 2017 and 2016 includes a reversal of loss on valuation of inventories of ¥35 million (\$312 thousand) and ¥54 million, respectively.

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Notes to Consolidated Financial Statements

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6. Short-Term Borrowings and Long-Term Debt

Short-term borrowings from banks outstanding consisted primarily of six-month notes issued by the Company to banks bearing interest at the weighted-average interest rate of 1.6% and 1.4% as of March 31, 2017 and 2016, respectively. Customarily, these notes are renewed at maturity subject to re-negotiation of the interest rates and other conditions.

Long-term debt and lease obligations as of March 31, 2017 and 2016 consisted of the following:

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Loans from banks and an insurance company	¥ 2,738	¥ 2,786	\$ 24,405
Lease obligations	15	25	133
Less, current portion of long-term debt	(32)	(1,058)	(285)
Less, current portion of lease obligations	(7)	(11)	(62)
Total long-term debt (*1) and lease obligations	<u>¥ 2,714</u>	<u>¥ 1,742</u>	<u>\$ 24,191</u>

(*1) The weighted-average interest rates on loans from banks and an insurance company were as follows:

As of March 31, 2017:	0.9%
As of March 31, 2016:	1.2

The maturities of long-term debt (excluding lease obligations) were as follows:

	Millions of Yen	Thousands of U.S. Dollars
Years ending March 31:		
2018	¥ 32	\$ 285
2019	1,703	15,180
2020	1,003	8,940
Total	<u>¥ 2,738</u>	<u>\$ 24,405</u>

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

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The maturities of lease obligations were as follows:

	Millions of Yen		Thousands of U.S. Dollars
Years ending March 31:			
2018	¥ 7		\$ 62
2019	4		35
2020	3		27
2021	1		9
2022 and thereafter	0		0
Total	¥ 15		\$ 133

The Companies' assets pledged as collateral for long-term debt of ¥500 million (\$4,457 thousand) as of March 31, 2017 and for current portion of long-term debt of ¥500 million as of March 31, 2016 were summarized as follows:

	Millions of Yen		Thousands of U.S. Dollars
<u>As of March 31</u>	2017	2016	2017
Investment securities	¥ 1,419	¥ 1,233	\$ 12,648

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

7. Retirement Benefit Plans

a. Overview of retirement benefit plan adopted by the Company

The Companies, excluding certain overseas consolidated subsidiaries, have defined benefit plans such as corporate defined benefit pension plans and/or lump-sum payment plans covering all of its employees. Certain consolidated subsidiaries, on the other hand, have defined contribution pension plans. In addition, the Companies may occasionally pay supplementary benefits to retiring employees.

Certain consolidated subsidiaries adopt the simplified method in the calculation of net defined benefit liability and retirement benefit expenses for their corporate defined benefit pension plans and/or lump-sum payment plans.

b. Defined benefit plan

(1) The changes in the retirement benefit obligations during the years ended March 31, 2017 and 2016 (except for plans to which the simplified method is applied)

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Projected benefit obligations at April 1	¥ 4,497	¥ 4,261	\$ 40,084
Service cost	288	258	2,567
Interest cost	24	44	214
Actuarial gains and losses	81	268	722
Prior service cost	(4)	-	(36)
Retirement benefits paid	(188)	(413)	(1,675)
Other	(2)	79	(18)
Projected benefit obligations at March 31	¥ 4,696	¥ 4,497	\$ 41,858

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Notes to Consolidated Financial Statements

March 31, 2017 and 2016

- (2) The changes in plan assets during the years ended March 31, 2017 and 2016 (except for plans to which the simplified method is applied)

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Plan assets at April 1	¥ 3,727	¥ 3,851	\$ 33,220
Expected return on plan assets	56	58	499
Actuarial gains and losses	37	(77)	330
Contribution by the Company	304	295	2,710
Retirement benefits paid	(171)	(400)	(1,524)
Other	(0)	(0)	(0)
Plan assets at March 31	<u>¥ 3,953</u>	<u>¥ 3,727</u>	<u>\$ 35,235</u>

- (3) The changes in net defined benefit liabilities for plans to which the simplified method is applied during the years ended March 31, 2017 and 2016

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Net defined benefit liability at April 1	¥ 530	¥ 673	\$ 4,724
Retirement benefit expenses	188	183	1,676
Retirement benefits paid	(68)	(73)	(606)
Contribution to plans	(116)	(158)	(1,034)
Other	(2)	(95)	(18)
Net defined benefit liability at March 31	<u>¥ 532</u>	<u>¥ 530</u>	<u>\$ 4,742</u>

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

- (4) Reconciliation between retirement benefit obligations and plan assets at end of year and “Net defined benefit liability” and “Net defined benefit asset” for retirement recognized on the consolidated balance sheets

<u>As of March 31</u>	<u>Millions of Yen</u>		<u>Thousands of</u>
	<u>2017</u>	<u>2016</u>	<u>U.S. Dollars</u>
			<u>2017</u>
Projected benefit obligation for funded plans	¥ 5,515	¥ 5,298	\$ 49,158
Plan assets	(4,775)	(4,504)	(42,562)
	<u>740</u>	<u>794</u>	<u>6,596</u>
Projected benefit obligation for unfunded plans	535	506	4,769
Net balance of liability and asset recognized on the consolidated balance sheets	<u>1,275</u>	<u>1,300</u>	<u>11,365</u>
Net defined benefit liability	1,356	1,345	12,087
Net defined benefit asset	(81)	(45)	(722)
Net balance of liability and asset recognized on the consolidated balance sheets	<u>¥ 1,275</u>	<u>¥ 1,300</u>	<u>\$ 11,365</u>

- (5) The components of retirement benefit expenses

<u>For the years ended March 31</u>	<u>Millions of Yen</u>		<u>Thousands of</u>
	<u>2017</u>	<u>2016</u>	<u>U.S. Dollars</u>
			<u>2017</u>
Service cost	¥ 288	¥ 258	\$ 2,567
Interest cost	24	44	214
Expected return on plan assets	(56)	(58)	(499)
Amortization of actuarial gains and losses	58	(9)	517
Amortization of prior service cost	(4)	-	(36)
Retirement benefit expenses applying the simplified method	<u>188</u>	<u>183</u>	<u>1,676</u>
Retirement benefit expenses under defined benefit plans	<u>¥ 498</u>	<u>¥ 418</u>	<u>\$ 4,439</u>

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

(6) Remeasurements of defined benefit plans

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Actuarial gains and losses	¥ (14)	¥ 353	\$ (125)
Total	¥ (14)	¥ 353	\$ (125)

(7) Accumulated remeasurements of defined benefit plans

The components of accumulated remeasurements of defined benefit plans (before tax) are as follows:

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Unrecognized actuarial gains and losses	¥ 214	¥ 228	\$ 1,907
Total	¥ 214	¥ 228	\$ 1,907

(8) Plan assets

(a) Percentage of major categories to total plan assets is as follows:

<u>As of March 31</u>	2017	2016
Bonds	15%	14%
Stocks	16	17
General accounts	55	56
Other	14	13
Total	100%	100%

(b) Determination of expected rate of return on plan assets

In determining the expected rate of return on plan assets, the Company takes into consideration the current and future plan asset allocation as well as the current and expected rate of return on various asset categories comprising plan assets.

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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(9) Assumptions used in accounting for the above plan

	2017	2016
Discount rate	0.4%	0.3%
Expected rate of return on plan assets	1.5	1.5
Assumed rate of increase in future compensation levels	3.1	3.1

c. Defined contribution plan

The required contribution of certain consolidated subsidiaries to their defined contribution plans amounts to ¥77 million (\$686 thousand) and ¥87 million as of March 31, 2017 and 2016.

8. Net Assets

a. Shares issued and outstanding/ Treasury stock

For the year ended March 31, 2017

	Shares			
	Number of shares at April 1, 2016	Increase	Decrease	Number of shares at March 31, 2017
Shares issued:				
Common stock	69,068,822	-	-	69,068,822
Treasury stock:				
Common stock (Note)	2,865,271	699,814	35	3,565,050

Notes:

1. Details of the increase are as follows: (Shares)

Increase due to purchase of treasury stock by resolution of the board of directors: 697,000

Increase due to purchase of shares less than standard unit: 2,814

2. Details of the decrease are as follows:

Decrease due to sale of shares less than standard unit: 35

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Notes to Consolidated Financial Statements

March 31, 2017 and 2016

For the year ended March 31, 2016

	Shares			Number of shares at March 31, 2016
	Number of shares at April 1, 2015	Increase	Decrease	
Shares issued:				
Common stock	69,068,822	–	–	69,068,822
Treasury stock:				
Common stock (Note)	2,855,630	9,641	–	2,865,271

Note: Increase of common stock in treasury by 9,641 shares is due to purchase of shares less than standard unit.

b. Share subscription rights

The Companies have no subscription rights as of March 31, 2017 and 2016.

c. Dividends

(1) Dividends from retained earnings

The following appropriation of retained earnings applicable to the year ended March 31, 2017 was resolved by the board of directors on October 28, 2016:

- (a) Total amount of dividends: ¥524 million (\$4,671 thousand)
- (b) Dividends per share: ¥8.00 (\$0.07)
- (c) Cut-off date: September 30, 2016
- (d) Effective date: December 1, 2016

The following appropriation of retained earnings applicable to the year ended March 31, 2017 was approved at an annual general shareholders' meeting held on June 23, 2016:

- (a) Total amount of dividends: ¥595 million (\$5,304 thousand)
- (b) Dividends per share: ¥9.00 (\$0.08)
- (c) Cut-off date: March 31, 2016
- (d) Effective date: June 24, 2016

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

The following appropriation of retained earnings applicable to the year ended March 31, 2016 was resolved by the board of directors on October 30, 2015:

- (a) Total amount of dividends: ¥463 million
- (b) Dividends per share: ¥7.00
- (c) Cut-off date: September 30, 2015
- (d) Effective date: December 1, 2015

The following appropriation of retained earnings applicable to the year ended March 31, 2016 was approved at an annual general shareholders' meeting held on June 25, 2015:

- (a) Total amount of dividends: ¥596 million
- (b) Dividends per share: ¥9.00
- (c) Cut-off date: March 31, 2015
- (d) Effective date: June 26, 2015

(2) Dividends whose effective date is after the end of the current fiscal year and whose cut-off date is in the current fiscal year

The following appropriation of retained earnings which has not been reflected in the accompanying consolidated financial statements as of and for the year ended March 31, 2017 was approved at an annual general shareholders' meeting held on June 22, 2017:

- (a) Total amount of dividends: ¥655 million (\$5,838 thousand)
- (b) Source of dividends: Retained earnings
- (c) Dividends per share: ¥10.00 (\$0.09)
- (d) Cut-off date: March 31, 2017
- (e) Effective date: June 23, 2017

Note: Dividends per share include a commemorative dividend of ¥2 (\$0.02) per share for the 100th Founding Anniversary.

The following appropriation of retained earnings which has not been reflected in the accompanying consolidated financial statements as of and for the year ended March 31, 2016 was approved at an annual general shareholders' meeting held on June 23, 2016:

- (a) Total amount of dividends: ¥595 million
- (b) Source of dividends: Retained earnings
- (c) Dividends per share: ¥9.00
- (d) Cut-off date: March 31, 2016
- (e) Effective date: June 24, 2016

CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

March 31, 2017 and 2016

9. Selling, General and Administrative Expenses

Significant components of “Selling, general and administrative expenses” for the years ended March 31, 2017 and 2016 were as follows:

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Depreciation	¥ 379	¥ 345	\$ 3,378
Provision of allowance for doubtful accounts	212	688	1,890
Provision for bonuses	52	53	463
Provision for product warranties	9	324	80
Retirement benefit expenses	384	347	3,423
Directors’ compensations and employees’ salaries and bonuses	7,155	7,880	63,776
Transportation expenses	3,514	4,399	31,322
Sales commission	2,034	3,917	18,130
Other	7,399	8,174	65,951
Total	<u>¥ 21,138</u>	<u>¥ 26,127</u>	<u>\$ 188,413</u>

Research and development cost included in general and administrative expenses and manufacturing costs for the years ended March 31, 2017 and 2016 amounted to ¥1,859 million (\$16,570 thousand) and ¥1,788 million, respectively.

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Notes to Consolidated Financial Statements

March 31, 2017 and 2016

10. Special Gains (Losses), net

Components of “Special gains (losses), net” for the years ended March 31, 2017 and 2016 were as follows:

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Special gains:			
Gain on sales of property, plant and equipment	¥ 5	¥ 8	\$ 45
Gain on sales of investment securities	113	—	1,007
	<u>118</u>	<u>8</u>	<u>1,052</u>
Special losses:			
Loss on sales of property, plant and equipment	1	4	9
Loss on sales of investment securities	—	2	—
Loss on valuation of investment securities	29	20	258
Loss on valuation of golf club membership	5	15	45
Provision of allowance for doubtful accounts	5	—	45
	<u>40</u>	<u>41</u>	<u>357</u>
Total	<u>¥ 78</u>	<u>¥ (33)</u>	<u>\$ 695</u>

Gain on sales of property, plant and equipment for the years ended March 31, 2017 and 2016 primarily resulted from the sales of “Buildings and structures,” “Machinery, equipment and vehicles,” “Tools, furniture and fixtures” and “Land” amounted ¥5 million (\$45 thousand) and ¥8 million, respectively.

Loss on sales of property, plant and equipment for the years ended March 31, 2017 and 2016 primarily resulted from the sales of “Machinery, equipment and vehicles” and “Tools, furniture and fixtures” amounted ¥1 million (\$9 thousand) and ¥4 million, respectively.

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Notes to Consolidated Financial Statements

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11. Income Taxes

The Companies are subject to several taxes based on income which, in the aggregate, resulted in a statutory tax rate of approximately 30.7% and 32.8% for the years ended March 31, 2017 and 2016, respectively.

Significant components of deferred tax assets and liabilities as of March 31, 2017 and 2016 were as follows:

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Deferred tax assets:			
Net defined benefit liability	¥ 403	¥ 402	\$ 3,592
Allowance for doubtful accounts	688	729	6,133
Loss on valuation of investment securities	389	402	3,467
Loss on valuation of inventories	124	124	1,105
Accrued bonuses	184	183	1,640
Accrued enterprise tax	47	69	419
Long-term accrued amount payable	19	19	169
Elimination of unrealized gains	93	148	829
Tax loss carryforwards	176	186	1,569
Other	359	300	3,200
Gross deferred tax assets	2,482	2,562	22,123
Less, valuation allowance	(621)	(645)	(5,535)
Total deferred tax assets	1,861	1,917	16,588
Deferred tax liabilities:			
Net unrealized holding gain on other securities	(779)	(813)	(6,944)
Net defined benefit asset	(22)	(13)	(196)
Other	(52)	(52)	(463)
Total deferred tax liabilities	(853)	(878)	(7,603)
Net deferred tax assets	¥ 1,008	¥ 1,039	\$ 8,985

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Reconciliations of the statutory tax rates to the effective tax rates for the years ended March 31, 2017 and 2016 were as follows:

<u>For the years ended March 31</u>	2017	2016
Statutory tax rates	30.7%	32.8%
Increase (decrease) in taxes resulting from:		
Difference in statutory tax rates between parent and consolidated subsidiaries	(4.6)	(8.3)
Entertainment and other non-deductible expenses	4.7	3.0
Dividend income and other non-taxable income	(4.4)	(4.0)
Dividends from retained earnings	7.7	8.2
Tax credit for investments in production facilities	(0.3)	–
Foreign tax credit	(0.3)	(0.7)
Special tax credit for research and development cost and others	(2.4)	(1.4)
Increase in valuation allowance of deferred tax assets	(0.1)	(0.3)
Other	(1.2)	(1.1)
Effective tax rates	29.8%	28.2%

12. Lease Transactions

The amounts of the outstanding future lease payments for noncancellable operating lease transactions subsequent to March 31, 2017 and 2016 were as follows:

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Due within one year	¥ 92	¥ 100	\$ 820
Due after one year	56	81	499
Total	¥ 148	¥ 181	\$ 1,319

13. Asset Retirement Obligations

The liability related to the restoration of Tokyo office arising from contractual requirements set forth in the lease agreement is recorded as “Asset retirement obligation.”

Instead of recording the asset retirement obligation as a liability, a portion of the deposit deemed to be finally uncollectible is recognized as expense. The uncollectible amount is reasonably estimated based on the lease agreement.

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Notes to Consolidated Financial Statements

March 31, 2017 and 2016

14. Commitments and Contingencies

The Companies were contingently liable for outstanding endorsed notes of ¥830 million (\$7,398 thousand) and ¥2,118 million as of March 31, 2017 and 2016, respectively.

The Company provided guarantees to an intermediary trading company of ¥828 million (\$7,380 thousand) and ¥907 million for the collection of its accounts receivable from contracted sales agents/distributors as of March 31, 2017 and 2016, respectively.

15. Amounts per Share

Profit attributable to owners of parent per share for the years ended March 31, 2017 and 2016 and net assets per share as of March 31, 2017 and 2016 were as follows:

<u>As of and for the years ended March 31</u>	Yen		U.S. Dollars
	2017	2016	2017
Profit attributable to owners of parent	¥ 55.50	¥ 98.21	\$ 0.49
Net assets	1,107.57	1,104.67	9.87

The bases for calculation of profit attributable to owners of parent per share were as follows:

<u>For the years ended March 31</u>	Shares	
	2017	2016
The number of shares of common stock used for the calculation of profit attributable to owners of parent per share	65,647,425	66,207,725

<u>For the years ended March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Profit attributable to owners of parent	¥ 3,643	¥ 6,502	\$ 32,472
Amount not attributable to shareholders of common stock	—	—	—
Profit attributable to owners of parent available for distribution to shareholders of common stock	¥ 3,643	¥ 6,502	\$ 32,472

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March 31, 2017 and 2016

The bases for calculation of net assets per share were as follows:

<u>As of March 31</u>	Shares	
	2017	2016
The number of shares of common stock used for the calculation of net assets per share	65,503,772	66,203,551

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Total net assets	¥ 78,169	¥ 78,817	\$ 696,756
Amounts deducted from total net assets:			
Non-controlling interests	5,619	5,684	50,085
Net assets attributable to shares of common stock	¥ 72,550	¥ 73,133	\$ 646,671

16. Securities

There were no held-to-maturity bonds as of March 31, 2017 and 2016.

Other securities as of March 31, 2017 were summarized as follows:

<u>As of March 31, 2017</u>	Millions of Yen			
	Acquisition cost	Fair value	Gross unrealized gain	Gross unrealized loss
Other Securities:				
With fair value	¥ 5,028	¥ 7,913	¥ 2,926	¥ (41)
Without fair value	655			

<u>As of March 31, 2017</u>	Thousands of U.S. Dollars			
	Acquisition cost	Fair value	Gross unrealized gain	Gross unrealized loss
Other Securities:				
With fair value	\$ 44,817	\$ 70,532	\$ 26,081	\$ (366)
Without fair value	5,839			

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Notes to Consolidated Financial Statements

March 31, 2017 and 2016

Other securities as of March 31, 2016 were summarized as follows:

<u>As of March 31, 2016</u>	Millions of Yen			
	Acquisition cost	Fair value	Gross unrealized gain	Gross unrealized loss
Other Securities:				
With fair value	¥ 5,084	¥ 7,908	¥ 3,142	¥ (318)
Without fair value	660			

Total sales of other securities for the years ended March 31, 2017 and 2016 amounted to ¥187 million (\$1,667 thousand) and ¥0 million, respectively. The related gain amounted to ¥113 million (\$1,007 thousand) for the year ended March 31, 2017, and the related loss amounted to ¥2 million for the year ended March 31, 2016.

Impairment losses on other securities of ¥29 million (\$258 thousand) and held-to maturity bonds of ¥20 million were recognized for the years ended March 31, 2017 and 2016, respectively.

In the event the fair value of securities declines by 50% or more of the acquisition cost, the securities are written down to their fair value. In the event the fair value declines between 30 and 50%, an impairment loss is recognized in the amount deemed necessary considering the possibility of recovery in fair value.

For equity securities whose fair value is deemed extremely difficult to determine, in the event the value of those equity securities declines by 50% or more from the acquisition cost due to a deterioration in the issuer's financial condition, an impairment loss is recognized unless a recovery in value is supported by reasonable grounds.

17. Supplementary Cash Flow Information

Cash and cash equivalents as of March 31, 2017 and 2016 consisted of the following:

<u>As of March 31</u>	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Cash on hand and in banks	¥ 36,918	¥ 34,019	\$ 329,067
Less, time deposits with deposit term of over three months	(8,701)	(7,446)	(77,556)
Short-term investment securities (MMF and others)	186	255	1,658
Cash and cash equivalents	¥ 28,403	¥ 26,828	\$ 253,169

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18. Derivative Transactions

Summary of transactions

Derivative transactions to which hedge accounting was not applied as of March 31, 2017 and 2016 were as follows:

Currency-related transactions

	Millions of Yen					
	2017			2016		
	Contract or notional amount	Fair value	Valuation gain (loss)	Contract or notional amount	Fair value	Valuation gain (loss)
Foreign exchange forward contracts:						
Short-term:						
Sell USD and buy JPY	¥ 54	¥ (3)	¥ (3)	¥ 135	¥ 1	¥ 1
Sell USD and buy EUR	706	(18)	(18)	631	(2)	(2)
Buy USD and sell JPY	13	0	0	17	(0)	(0)
Buy SGD and sell EUR	–	–	–	43	(0)	(0)
Buy JPY and sell EUR	62	(2)	(2)	25	0	0
Buy GBP and sell EUR	112	2	2	154	(2)	(2)
Total			<u>¥ (21)</u>			<u>¥ (3)</u>

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Thousands of U.S. Dollars			
2017			
	Contract or notional amount	Fair value	Valuation gain (loss)
Foreign exchange forward contracts:			
Short-term:			
Sell USD and buy JPY	\$ 481	\$ (27)	\$ (27)
Sell USD and buy EUR	6,293	(160)	(160)
Buy USD and sell JPY	116	0	0
Buy SGD and sell EUR	-	-	-
Buy JPY and sell EUR	553	(18)	(18)
Buy GBP and sell EUR	998	18	18
Total			\$ (187)

The fair value has been quoted from financial institutions with which the Companies enter into foreign exchange forward contracts.

There were no interest-related transactions as of March 31, 2017 and 2016.

There were no derivative transactions to which hedge accounting was applied as of March 31, 2017 and 2016.

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19. Financial Instruments

The Companies operate funds through highly liquid financial assets and finance short-term operating capital with bank loans. Derivative transactions are only utilized to hedge the following risks, and it is our policy not to enter into derivative transactions for speculative purposes.

Operating receivables such as “Trade notes and accounts receivable” are exposed to credit risk. Operating receivables denominated in foreign currencies from overseas operations are exposed to foreign currency risk. The Companies utilize foreign exchange forward contracts within the actual orders to hedge the risk. “Short-term investment securities” and “Investment securities” mainly consist of securities of companies with a business relationship and are exposed to market fluctuation risk.

Operating payables such as “Trade notes and accounts payable” are mainly due within one year. Some of the operating payables relating to imports of raw materials are denominated in foreign currencies and exposed to foreign currency risk. The Companies utilize foreign exchange forward contracts within the actual orders to hedge the risk. “Short-term borrowings” are mainly used for the purpose of financing operating capital.

The Companies utilize foreign exchange forward contracts to hedge foreign currency risk on operating receivables and payables denominated in foreign currencies. Please see Note 1. p. Derivative financial instruments, for hedge accounting.

Risk management on financial instruments is summarized as follows:

(1) Management of credit risk (risk of default by the counter parties)

In accordance with the Company’s internal rules, the Sales Planning Dept. of the Company monitors the major customers’ credit conditions periodically and manages the due date and balance per each customer. The Company keeps track of the adverse financial conditions of the customers in the early stage to mitigate the bad debt. The consolidated subsidiaries follow the Company’s internal rules and manage the risk in the same manner. Regarding the derivative transactions, the Companies only deal with highly rated financial institutions and thus, there is little credit risk.

(2) Management of market risk (risk of fluctuations in foreign exchange)

The Companies utilize foreign exchange forward contracts within the actual orders to hedge foreign currency risk on the operating receivables and payables denominated in foreign currencies.

Regarding the “Short-term investment securities” and “Investment securities,” the Companies regularly review the fair value and issuers’ financial conditions and readjust the Companies’ portfolio according to the market condition and the business relationship with the counterparties on an ongoing basis. Execution and management of derivative transactions for the Companies are managed in accordance with the Company’s internal rules.

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(3) Management of liquidity risk on financing (risk of default at the due dates)

The treasury department of the Company timely prepares and updates the cash management plan based on the report from each department. The Company manages the liquidity risk by maintaining the on-hand liquidity. The consolidated subsidiaries manage the risk in accordance with the Company's internal rules.

As well as the values based on market prices, fair values of financial instruments include values which are reasonably calculated in case that market prices are not available. As the calculation of those values includes variable factors, those values may vary in case different assumptions are applied. The contract or notional amount described in Note 18., Derivative Transactions, does not indicate market risk related to the derivative transactions.

The carrying value on the consolidated balance sheets, fair value and their difference of financial instruments as of March 31, 2017 and 2016 was as follows:

<u>As of March 31</u>	Millions of Yen					
	2017			2016		
	Carrying value	Fair value	Difference	Carrying value	Fair value	Difference
Cash on hand and in banks	¥ 36,918	¥ 36,918	–	¥ 34,019	¥ 34,019	–
Trade notes and accounts receivable	32,605			42,043		
Allowance for doubtful accounts (*1)	(2,115)			(2,433)		
	<u>30,490</u>	<u>30,490</u>	<u>–</u>	<u>39,610</u>	<u>39,610</u>	<u>–</u>
Short-term investment securities and investment securities	7,913	7,913	–	7,908	7,908	–
Total assets	<u>¥ 75,321</u>	<u>¥ 75,321</u>	<u>–</u>	<u>¥ 81,537</u>	<u>¥ 81,537</u>	<u>–</u>
Short-term borrowings	¥ 17,356	¥ 17,356	–	¥ 18,521	¥ 18,521	–
Trade notes and accounts payable	11,646	11,646	–	14,379	14,379	–
Total liabilities	<u>¥ 29,002</u>	<u>¥ 29,002</u>	<u>–</u>	<u>¥ 32,900</u>	<u>¥ 32,900</u>	<u>–</u>
Derivatives (*2)	¥ (21)	¥ (21)	–	¥ (3)	¥ (3)	–

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<u>As of March 31</u>	Thousands of U.S. Dollars		
	2017		
	Carrying value	Fair value	Difference
Cash on hand and in banks	\$ 329,067	\$ 329,067	-
Trade notes and accounts receivable	290,623		
Allowance for doubtful accounts (*1)	(18,852)		
	<u>271,771</u>	<u>271,771</u>	-
Short-term investment securities and investment securities	70,532	70,532	-
Total assets	<u>\$ 671,370</u>	<u>\$ 671,370</u>	-
Short-term borrowings	\$ 154,702	\$ 154,702	-
Trade notes and accounts payable	103,806	103,806	-
Total liabilities	<u>\$ 258,508</u>	<u>\$ 258,508</u>	-
Derivatives (*2)	\$ (187)	\$ (187)	-

(*1) Allowance for doubtful accounts relating to trade notes and accounts receivable is deducted.

(*2) Derivative assets and liabilities are presented on a net basis.

Carrying value of financial instruments whose fair value was deemed extremely difficult to determine, which was not included in the above tables, as of March 31, 2017 and 2016 was as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Unlisted equity securities	¥ 655	¥ 660	\$ 5,839

Valuation method of fair value of financial instruments and information about securities and derivative transactions are summarized as follows:

Cash on hand and in banks

The carrying value is deemed as the fair value since it is scheduled to be settled in a short period of time.

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Trade notes and accounts receivable

The carrying value is deemed as the fair value since it is scheduled to be settled in a short period of time.

Short-term investment securities and Investment securities

The fair value of stocks is based on the price on stock exchanges and that of bonds is based on the price on bond markets or the price presented by the counterparty financial institutions. The carrying value of MMF and others are deemed as the fair value since it is scheduled to be settled in a short period of time. Please see Note 16., Securities, for the notes regarding the securities by classification.

Short-term borrowings

The carrying value is deemed as the fair value since it is scheduled to be settled in a short period of time.

Trade notes and accounts payable

The carrying value is deemed as the fair value since it is scheduled to be settled in a short period of time.

Derivative transactions

Please see Note 18., Derivative Transactions.

Redemption schedule for monetary assets as of March 31, 2017 and 2016 was as follows:

	Millions of Yen			
	2017			
	Due in one year or less	Due after one year through five years	Due after five years through ten years	Due after ten years
Cash on hand and in banks	¥ 36,892	–	–	–
Trade notes and accounts receivable	32,605	–	–	–
Total	¥ 69,497	–	–	–

	Thousands of U.S. Dollars			
	2017			
	Due in one year or less	Due after one year through five years	Due after five years through ten years	Due after ten years
Cash on hand and in banks	\$ 328,835	–	–	–
Trade notes and accounts receivable	290,623	–	–	–
Total	\$ 619,458	–	–	–

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	Millions of Yen			
	2016			
	Due in one year or less	Due after one year through five years	Due after five years through ten years	Due after ten years
Cash on hand and in banks	¥ 33,996	–	–	–
Trade notes and accounts receivable	42,043	–	–	–
Total	¥ 76,039	–	–	–

20. Other Comprehensive Income

Reclassification adjustments and tax effects allocated to each component of other comprehensive income for the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Net unrealized holding gain (loss) on other securities:			
Amount arising during the year	¥ 145	¥ (3,017)	\$ 1,293
Reclassification adjustments	(84)	2	(749)
Amount before tax effect	61	(3,015)	544
Tax effect	34	968	303
Net unrealized holding gain (loss) on other securities	95	(2,047)	847
Revaluation reserve for land:			
Tax effect	–	118	–
Foreign currency translation adjustments:			
Amount arising during the year	(3,010)	(3,050)	(26,829)
Remeasurements of defined benefit plans:			
Amount arising during the year	(40)	(344)	(356)
Reclassification adjustments	53	(9)	472
Amount before tax effect	13	(353)	116
Tax effect	(5)	109	(45)
Net remeasurements of defined benefit plans	8	(244)	71
Total other comprehensive income	¥ (2,907)	¥ (5,223)	\$ (25,911)

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21. Segment Information

(1) Outline of reportable segment

The Companies' reportable segments are those for which discrete financial information is available and regularly evaluated by the Company's board of directors in order to make decisions about resource allocations and assess their performances.

The Companies are mainly engaged in manufacturing and sales of paints, which are organized by geographical area based on comprehensive strategy for lines of business by each area, although each subsidiary is independently operated. As a result, the Companies have five reportable segments, (1) Japan (the Company), (2) China (CHUGOKU MARINE PAINTS (Shanghai), Ltd. and CHUGOKU MARINE PAINTS (Guang Dong), Ltd.), (3) Korea (CHUGOKU SAMHWA PAINTS, Ltd.), (4) South East Asia (CHUGOKU MARINE PAINTS (Singapore) Pte., Ltd. and CHUGOKU PAINTS (Malaysia) Sdn. Bhd.) and (5) Europe and U.S. (CHUGOKU PAINTS B.V.), respectively. "Japan" engages in the real estate management business in addition to manufacturing and sales of paints, and other reportable segments engage in manufacturing and sales of paints.

(2) Method of calculating net sales, profit (loss), assets and other items by reportable segment

Accounting policies of the reportable segments are consistent with those described in Note 1., Summary of Significant Accounting Policies. Reportable segment profit corresponds to operating profit. Intersegment sales and transfers are based on the prevailing market price.

(3) Net sales, profit (loss), assets and other items by reportable segment

For the year ended March 31, 2017

	Millions of Yen					
	Reportable segment					Total
	Japan	China	Korea	South East Asia	Europe/ U.S.	
Net sales:						
External sales	¥ 35,530	¥ 16,552	¥ 10,297	¥ 10,035	¥ 9,954	¥ 82,368
Intersegment sales or transfers	3,207	4,035	303	2,824	714	11,083
Total	¥ 38,737	¥ 20,587	¥ 10,600	¥ 12,859	¥ 10,668	¥ 93,451
Segment profit (loss)	¥ 3,167	¥ (465)	¥ 610	¥ 1,536	¥ (933)	¥ 3,915
Segment assets	¥ 62,723	¥ 34,964	¥ 8,223	¥ 15,204	¥ 10,915	¥ 132,029
Other items:						
Depreciation and amortization	¥ 716	¥ 611	¥ 69	¥ 198	¥ 77	¥ 1,671
Amortization of goodwill	—	—	—	—	27	27
Increase in property, plant and equipment and intangible assets	911	372	46	249	2,384	3,962

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For the year ended March 31, 2017

	Thousands of U.S. Dollars					
	Reportable segment					
	Japan	China	Korea	South East Asia	Europe/ U.S.	Total
Net sales:						
External sales	\$ 316,695	\$ 147,535	\$ 91,782	\$ 89,446	\$ 88,725	\$ 734,183
Intersegment sales or transfers	28,585	35,966	2,701	25,172	6,364	98,788
Total	<u>\$ 345,280</u>	<u>\$ 183,501</u>	<u>\$ 94,483</u>	<u>\$ 114,618</u>	<u>\$ 95,089</u>	<u>\$ 832,971</u>
Segment profit (loss)	<u>\$ 28,229</u>	<u>\$ (4,145)</u>	<u>\$ 5,437</u>	<u>\$ 13,691</u>	<u>\$ (8,316)</u>	<u>\$ 34,896</u>
Segment assets	<u>\$ 559,079</u>	<u>\$ 311,650</u>	<u>\$ 73,295</u>	<u>\$ 135,520</u>	<u>\$ 97,290</u>	<u>\$ 1,176,834</u>
Other items:						
Depreciation and amortization	\$ 6,382	\$ 5,446	\$ 615	\$ 1,765	\$ 686	\$ 14,894
Amortization of goodwill	-	-	-	-	241	241
Increase in property, plant and equipment and intangible assets	8,120	3,316	410	2,219	21,250	35,315

For the year ended March 31, 2016

	Millions of Yen					
	Reportable segment					
	Japan	China	Korea	South East Asia	Europe/ U.S.	Total
Net sales:						
External sales	¥ 38,501	¥ 31,859	¥ 15,842	¥ 13,186	¥ 15,679	¥ 115,067
Intersegment sales or transfers	4,842	8,359	470	4,344	1,102	19,117
Total	<u>¥ 43,343</u>	<u>¥ 40,218</u>	<u>¥ 16,312</u>	<u>¥ 17,530</u>	<u>¥ 16,781</u>	<u>¥ 134,184</u>
Segment profit (loss)	<u>¥ 2,773</u>	<u>¥ 2,064</u>	<u>¥ 515</u>	<u>¥ 2,907</u>	<u>¥ (1,042)</u>	<u>¥ 7,217</u>
Segment assets	<u>¥ 63,298</u>	<u>¥ 41,368</u>	<u>¥ 9,343</u>	<u>¥ 16,611</u>	<u>¥ 10,719</u>	<u>¥ 141,339</u>
Other items:						
Depreciation and amortization	¥ 577	¥ 734	¥ 77	¥ 221	¥ 96	¥ 1,705
Amortization of goodwill	-	-	-	-	30	30
Increase in property, plant and equipment and intangible assets	838	200	55	136	190	1,419

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(4) Reconciliation between the total amounts of reportable segments and consolidated amounts

(a) Segment profit

	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Total of the segment profit	¥ 3,915	¥ 7,217	\$ 34,896
Elimination of intersegment transaction	2,650	3,845	23,620
Other corporate expenses	(1,094)	(1,049)	(9,751)
Operating profit on consolidated statements of income	<u>¥ 5,471</u>	<u>¥ 10,013</u>	<u>\$ 48,765</u>

Note: “Other corporate expenses” are mainly general and administrative expenses which are not allocated to each reportable segment.

(b) Segment assets

	Millions of Yen		Thousands of U.S. Dollars
	2017	2016	2017
Total of the segment assets	¥ 132,029	¥ 141,339	\$ 1,176,834
Elimination of intersegment transaction	(23,382)	(24,894)	(208,414)
Other corporate assets	13,411	11,945	119,538
Total assets on consolidated balance sheets	<u>¥ 122,058</u>	<u>¥ 128,390</u>	<u>\$ 1,087,958</u>

Note: “Other corporate assets” are mainly cash on hand and in banks and investment securities which are not allocated to each reportable segment.

(c) Other items

	Millions of Yen		
	2017		
	Reportable segments total	Adjustments	Consolidated
Depreciation and amortization	¥ 1,671	¥ 57	¥ 1,728
Amortization of goodwill	27	-	27
Increase in property, plant and equipment and intangible assets	3,962	10	3,972

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	Thousands of U.S. Dollars		
	2017		
	Reportable segments total	Adjustments	Consolidated
Depreciation and amortization	\$ 14,894	\$ 508	\$ 15,402
Amortization of goodwill	241	–	241
Increase in property, plant and equipment and intangible assets	35,315	89	35,404

	Millions of Yen		
	2016		
	Reportable segments total	Adjustments	Consolidated
Depreciation and amortization	¥ 1,705	¥ 33	¥ 1,738
Amortization of goodwill	30	–	30
Increase in property, plant and equipment and intangible assets	1,419	378	1,797

Note: “Adjustments” for “Increase in property, plant and equipment and intangible assets” are mainly intangible assets which are not allocated to each reportable segment.

(Related information)

(1) Information by product and service

	Millions of Yen					Millions of Yen				
	2017					2016				
	Paint for ships	Paint for industrial use	Paint for containers	Other	Total	Paint for ships	Paint for industrial use	Paint for containers	Other	Total
External sales	¥ 64,910	¥ 12,019	¥ 5,109	¥ 330	¥ 82,368	¥ 92,063	¥ 12,242	¥ 10,436	¥ 326	¥ 115,067

	Thousands of U.S. Dollars				
	2017				
	Paint for ships	Paint for industrial use	Paint for containers	Other	Total
External sales	\$ 578,572	\$ 107,131	\$ 45,539	\$ 2,941	\$ 734,183

(2) Information by geographic area

(a) Net sales

Information about net sales by geographic area is omitted since the same information is disclosed in the information of reportable segment.

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(b) Property, plant and equipment

	Millions of Yen						Millions of Yen					
	2017						2016					
	Japan	China	Korea	South East Asia	Europe/ U.S.	Total	Japan	China	Korea	South East Asia	Europe/ U.S.	Total
Property, plant and equipment	¥ 16,568	¥ 4,985	¥ 750	¥ 1,538	¥ 2,986	¥ 26,827	¥ 16,389	¥ 5,666	¥ 826	¥ 1,557	¥ 674	¥ 25,112

	Thousands of U.S. Dollars					
	2017					
	Japan	China	Korea	South East Asia	Europe/ U.S.	Total
Property, plant and equipment	\$ 147,678	\$ 44,433	\$ 6,685	\$ 13,709	\$ 26,616	\$ 239,121

(3) Information about major customers

Information about major customers is omitted since there are no external sales to customers constituting more than 10% of net sales of the consolidated statements of income.

(Information about amortization of goodwill and unamortized balances by reportable segment)

	Millions of Yen						
	2017						
	Reportable segment						Elimination or corporate
Japan	China	Korea	South East Asia	Europe/ U.S.			
Amortization during the year	-	-	-	-	¥ 27	-	¥ 27
Unamortized balances	-	-	-	-	27	-	27

	Thousands of U.S. Dollars						
	2017						
	Reportable segment						Elimination or corporate
Japan	China	Korea	South East Asia	Europe/ U.S.			
Amortization during the year	-	-	-	-	\$ 241	-	\$ 241
Unamortized balances	-	-	-	-	241	-	241

	Millions of Yen						
	2016						
	Reportable segment						Elimination or corporate
Japan	China	Korea	South East Asia	Europe/ U.S.			
Amortization during the year	-	-	-	-	¥ 30	-	¥ 30
Unamortized balances	-	-	-	-	58	-	58