CANON ANNUAL REPORT 2015

Fiscal Year Ended December 31, 2015

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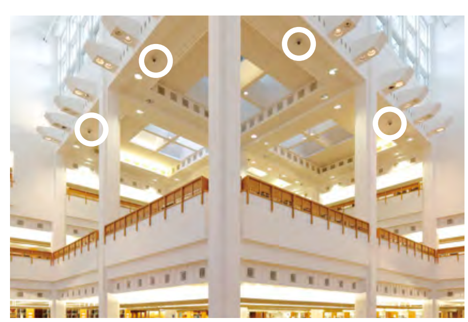


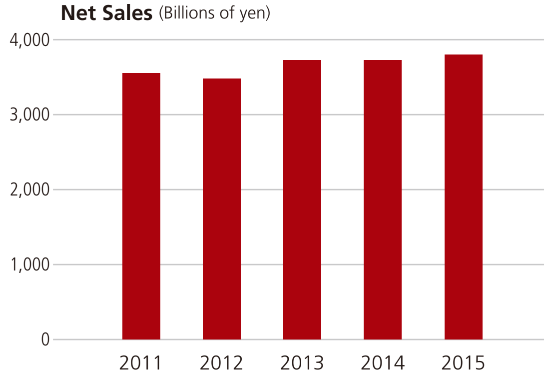
Cover Photo:
Canon's network cameras installed in British Library's St. Pancras Reading Room
Canon answers the call to protect cultural collections and the safety of visitors with the technological capabilities of its network cameras.

FINANCIAL HIGHLIGHTS

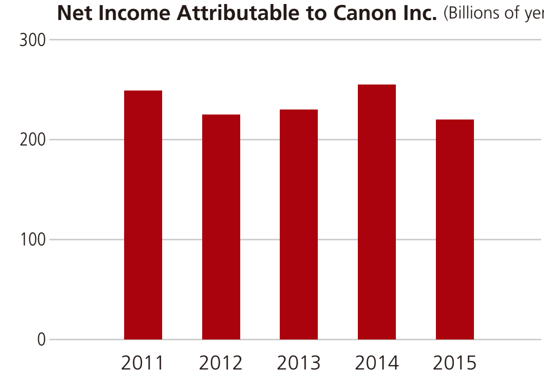
	Millions of yen (except per share amounts)			Thousands of U.S. dollars (except per share amounts)
	2015	2014	**Change (%)**	**2015**
Net sales	**¥3,800,271**	¥3,727,252	**+2.0**	**$31,407,198**
Operating profit	**355,210**	363,489	**-2.3**	**2,935,620**
Income before income taxes	**347,438**	383,239	**-9.3**	**2,871,388**
Net income attributable to Canon Inc.	**220,209**	254,797	**-13.6**	**1,819, 909**
Net income attributable to Canon Inc. shareholders per share:				
—Basic	**¥ 201.65**	¥ 229.03	**-12.0**	**$ 1.67**
—Diluted	**201.65**	229.03	**-12.0**	**1.67**
Total assets	**¥4,427,773**	¥4,460,618	**-0.7**	**$36,593,165**
Canon Inc. shareholders' equity	**¥2,966,415**	¥2,978,184	**-0.4**	**$24,515,826**

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 JPY121=U.S.$1, the approximate exchange rate on the Tokyo Foreign Exchange Market as of December 30, 2015, solely for the convenience of the reader.

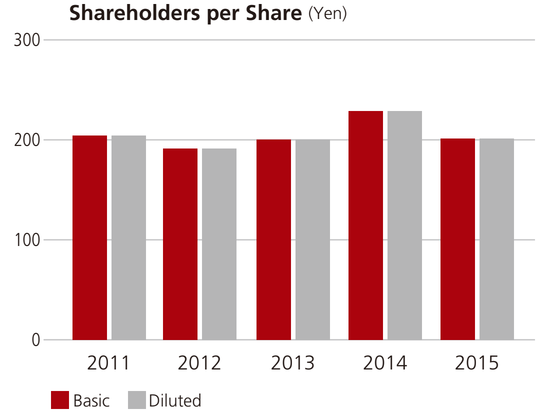
Net Sales (Billions of yen)



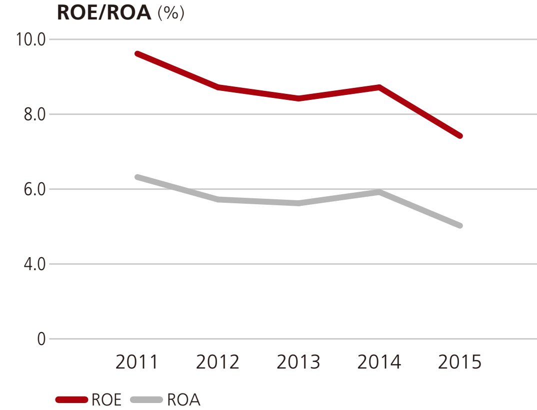
Net Income Attributable to Canon Inc. (Billions of yen)



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



ROE/ROA (%)



TO OUR SHAREHOLDERS

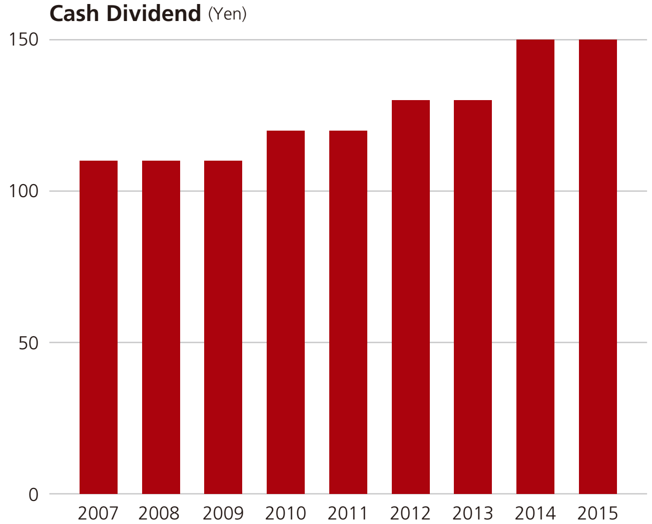
Canon will embrace the challenge of new growth through a grand strategic transformation under Phase V of its Excellent Global Corporation Plan.

Performance in 2015

Despite expectations at the beginning of 2015 that the global economy would realize a modest recovery led by the United States, the Chinese economy faced a slowdown in the second half of the year, which was followed by deceleration in emerging economies. As a result, the global economy overall realized its lowest level of growth since the financial crisis triggered by the 2008 collapse of Lehman Brothers.

Faced with these circumstances, in 2015, the final year of Phase IV of our Excellent Global Corporation Plan (2011–2015), we actively tackled such key challenges as revitalizing existing businesses and expanding new and future businesses. In line with these efforts, we welcomed into the Canon Group Axis, the global leader in network cameras.

Cash Dividend (Yen)



Looking at sales of our main products, digital cameras and inkjet printers continued to face harsh market conditions, mainly in China and emerging Asian countries, while color office multifunction devices (MFDs) and color light-production printing systems recorded sales growth. Semiconductor lithography equipment and flat panel display (FPD) lithography equipment also achieved significant year-on-year sales growth thanks to favorable market conditions. Consequently, benefiting from the boost provided by the acquisition of Axis and the positive effects of favorable currency exchange rates, consolidated net sales for 2015 increased 2.0% year on year to ¥3,800.3 billion, and the gross profit ratio rose 1.0 point year on year to 50.9%. Income before income taxes, however, declined 9.3% year on year to ¥347.4 billion, mainly due to the impact of a rise in investment in development aimed at reinforcing new businesses, higher expenses associated with consolidating Axis, and an increase in other deductions resulting from foreign currency exchange losses.

Among our accomplishments in 2015, we should highlight the fact that we recorded our highest-ever gross profit ratio despite the harsh business conditions we faced. This achievement, the result of ongoing cost-cutting activities and other efforts, is a testament to Canon's unwavering manufacturing prowess, even under adverse circumstances. Furthermore, seeking to actively return profits to shareholders, we declared an annual cash dividend of ¥150.00 per share, which remains unchanged from the record-high dividend we paid in 2014.

Excellent Global Corporation Plan Phases I to IV (1996–2015)

Canon launched the Excellent Global Corporation Plan in 1996 and, through four five-year phases of the Plan (Phases I through IV), we have reinforced our business foundation. During Phase I, we stressed thorough cash-flow management and significantly boosted productivity through the introduction of the cell production system and other measures. In Phase II, we fully digitalized our copying machine and camera offerings and became an essentially debt-free company. During Phase III, we effectively expanded business in the printing and medical equipment sectors while actively carrying out M&A activities.

And, in 2011, we embarked on Phase IV with the aim of achieving sound growth. During this period, however, the global economy faced a series of serious challenges, such as economic stagnation in Europe in the wake of Greece's sovereign debt crisis and slowdowns in China and other emerging markets. In response, we altered our original policy targeting scale expansion and focused instead on building up a strong financial structure capable of withstanding serious recessions. At the same time, we implemented two major measures to reorient our businesses with a view to the future. The first of these was ensuring new growth potential through the lateral expansion of existing businesses while the second was successfully acquiring new growth businesses through active M&A activities.

The first example of such lateral expansion of existing businesses is the Cinema EOS System. Following its launch in 2012, the lineup has revolutionized the motion picture production industry and captured an overwhelming share of the market with further growth expected in the eras of 4K and 8K. As for our Inkjet Product Operations, we launched a commercial photo printer and, through it, have developed a photo book service that encompasses editing, processing and bookbinding. Additional R&D achievements include the creation of businesses in such fields as the machine vision and professional-use display segments, which have highly promising futures.

As for M&A activity, we made successful acquisitions in three new growth sectors, the first of which was commercial printing. Océ was made a wholly owned subsidiary in 2013, thus opening the door to a new world of commercial and package printing through high-speed printing systems. The second was our entry into the network camera system

The Excellent Global Corporation Plan

Phase I 1996–2000	Phase II 2001–2005	Phase III 2006–2010	Phase IV 2011–2015
Strengthened our financial structure by thoroughly eliminating wastefulness, with production reforms playing a major role, based on changing our mindset with a focus on total optimization and profitability.	Recognized the need for digitalization and raised product competitiveness by enhancing our development infrastructure and reinforcing key components.	Strove to achieve "Sound Growth," seeking high growth levels by establishing new businesses while raising the profitability of existing businesses. With the global economy plunging into the global recession, shifted direction towards "improving the quality of management."	Tackled again the challenge of achieving "Sound Growth" through timely change in advance of changes in the times. **Slogan:** "Aiming for the Summit: Speed & Sound Growth"

Next step

Phase V
2016–2020

Continued on page 6

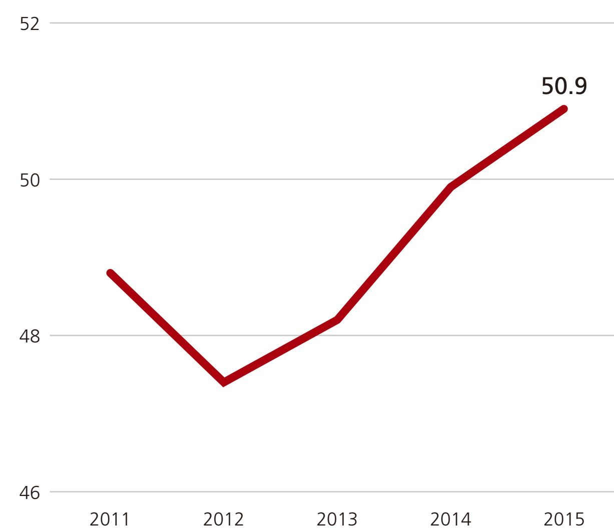
segment. Canon leaped to the top of the industry by welcoming Milestone Systems and Axis into the Canon Group. The third was making Molecular Imprints a wholly owned subsidiary and accelerating the development of nanoimprint technology that will enable both the miniaturization of electronic features and cost reductions.

In these ways, Canon has initiated a shift from B2C to B2B, adding new business segments to such maturing core businesses as cameras and office equipment.

As part of our effort to strengthen Canon's manufacturing capabilities, we have promoted production automation. In the area of camera production in particular, we have made steady progress in expanding the scope and variety of automation, following the introduction of automated assembly systems for EF lens focus units with automated systems capable of handling basic assembly processes for single-lens reflex (SLR) camera bodies. These achievements are clearly reflected in our gross profit ratio, which marked a record high of 50.9% in 2015. As a result, net income remained at a high level, recording a five-year average of over ¥230.0 billion per year. Moreover, using this income as capital for M&A activities, we have laid the foundation for an engine of future growth. Through rigorous cash flow management, we achieved a shareholders' equity ratio of 67.0% at the end of 2015, which enabled us to maintain our top-ten ranking for this management indicator among FORTUNE Global 500 companies.

Based on the above, it is clear that Phase IV was an important period during which Canon's business structure began undergoing significant changes as a result of efforts to cultivate new businesses and strengthen our manufacturing capabilities.

Gross Profit of Sales (%)



The Cinema EOS System combines a compact, lightweight body with easy-to-use functions and an attractive low price is widely used in motion picture production.

CEO Fujio Mitarai with the Board of Directors at Axis

Phase V (2016–2020)

2016 marks the start of Phase V, our latest five-year initiative within the Excellent Global Corporation Plan. As for the economic conditions on which Phase V is based, while developed countries are expected to perform generally well, due to the likelihood of a continued economic slowdown in China, we anticipate only moderate growth overall. Meanwhile, we believe two new tides will bring about significant changes to the structure of industry, as well as to the economy and society.

One of these is the Internet of Things (IoT) which, through the interconnectivity of all manner of "things" across the Internet, from appliances and automobiles to factory equipment, creates new value. Responding to this change means that, even as a manufacturer, we must stop thinking in terms of individual items and discard the notion that as long as we develop excellent products we will have no trouble selling them. Rather, we need to transform our business model to combine hardware, software and services, and consider the value offered by the system as a whole.

The other tide is the rise of emerging countries. With advances in the digitalization and modularization of products, many companies in emerging countries are entering the market and further accelerating the product commoditization process, which is expected to result in competition becoming even more intense.

It is amid this business environment that we have launched Phase V. During Phase V, under the basic policy "Embracing the challenge of new growth through a grand strategic transformation," we seek to further expand the reforms that we promoted in Phase IV. In 2020, the final year of Phase V, Canon aims to achieve net sales of ¥5 trillion, a cost-to-sales ratio of 45% or less, an operating profit ratio of 15% or more, a net income ratio of 10% or more, and a shareholders' equity ratio of 70% or more.

In accordance with this basic policy, we will pursue the following five specific strategies.

Strategy 1
Establish a new production system to achieve a cost-to-sales ratio of 45%

As a result of continuous production reforms, we were able to improve our cost-to-sales ratio to 49.1% in 2015. During Phase V, we aim to do even better, targeting a cost-to-sales ratio of 45%.

A key initiative toward this goal will be promoting a higher ratio of production in Japan. This shift offers the advantage of integrating design, R&D and manufacturing functions, allowing us to put together a competitive cost structure from the design stage, in addition to facilitating cost reductions

Key Strategies

1. Establish a new production system to achieve a cost-to-sales ratio of 45%
2. Reinforce and expand new businesses while creating future businesses
3. Restructure global sales network in accordance with market changes
4. Enhance R&D capabilities through open innovation
5. Complete the Three Regional Headquarters management system capturing world dynamism

2020 Management Targets

Net sales
¥5 trillion

***Cost-to-sales ratio**
45% or less

Operating profit ratio
15% or more

Net income ratio
10% or more

Shareholders' equity ratio
70% or more

(Based on exchange rates of US$1=¥125, €1=¥135)

*Cost-to-sales ratio refers to the cost of goods sold as a ratio of consolidated sales.

through the use of common parts and in-house production. Leveraging these advantages, we will position our production bases in Japan as "mother factories" that mainly manufacture high-end models and further adopt automation and other advanced production engineering technologies. In addition to boosting productivity through automated production systems and adopting such next-generation technologies as the IoT and artificial intelligence, we are establishing new production systems through the combination of such powerful Canon manufacturing tools as Mixed Reality (MR) systems, 3D printers and machine vision. Meanwhile, our overseas production bases will be responsible for the mass production of mid- and low-priced products, and we will review the earnings structure of these bases and adapt accordingly to changes in such factors as labor costs, currency trends and corporate taxes in pursuit of comprehensive cost reductions.

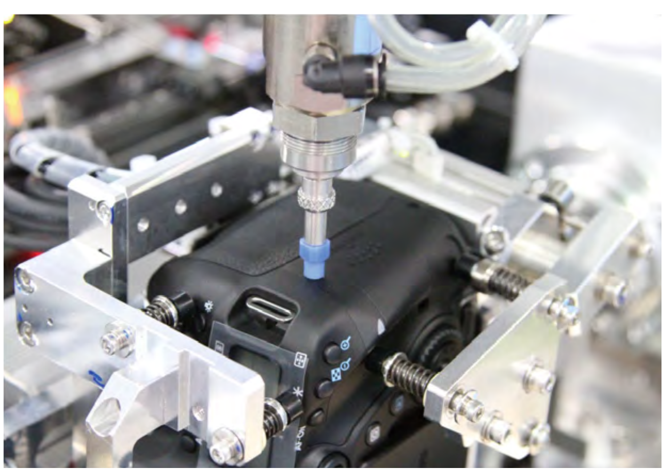
Strategy 2
Reinforce and expand new businesses while creating future businesses

At Canon, in order to achieve sustainable growth, we are shifting our focus to fields in which we can achieve greater growth. As one of the initiatives we are undertaking toward this end, we are creating and expanding new businesses by accelerating the lateral expansion of existing businesses. We are also focusing our energies on strengthening and expanding the new growth engines that we acquired through M&A activities in such areas as commercial printing and network camera systems. In the life sciences field, we seek to commercialize DNA diagnostic equipment. In this way, we are concentrating management resources in promising growth areas and will supplement these with M&A activities aimed at accelerating business expansion.

Strategy 3
Restructure global sales network in accordance with market changes

We are working to expand sales in response to the major changes that distribution markets are undergoing in the current age of IT. We plan to review existing sales organizations and accelerate a shift to omni-channel marketing that utilizes the strengths of both online and brick-and-mortar sales routes while reinforcing direct communication with customers. Furthermore, to get ahead in the IoT era, we are focused on strengthening and expanding solutions-driven businesses with the aim of solving issues faced by customers.

Meanwhile, with regard to regional expansion, we will swiftly develop sales networks not only in China and India, but also in other areas with future growth potential, such as ASEAN countries and Africa, while continuing our efforts to cultivate markets in emerging countries.



Automated processes for digital camera production have been adopted at Oita Canon Inc. (Japan)

Digital printed packaging suitable for flexible, small-lot production runs of varied products with rapid turnaround times (Canon EXPO 2015 Tokyo exhibition)

Strategy 4
Enhance R&D capabilities through open innovation

The pace of technological advancement gets faster with each passing day and, in the process, is becoming more sophisticated and complex. Additionally, we are seeing increased diversity in the needs of our customers, which has made it necessary to integrate technologies from different fields. We are therefore building a more open R&D structure, harvesting information on state-of-the-art technologies from around the world and applying it with the aim of accelerating development processes and generating effective results. Also, particularly in the field of basic research, we are promoting collaborative and sponsored research, forming a wide-reaching network through collaborations with universities, research institutions and business ventures in Japan and abroad.

Strategy 5
Complete the Three Regional Headquarters management system capturing world dynamism

During Phase IV, we made strides toward realizing the Three Regional Headquarters management system, which spans Japan, the United States and Europe. In terms of scale and volume, however, we still have a long way to go. We will therefore newly acquire multiple promising businesses via M&A activities focused on Japan, the United States and Europe while leveraging the distinctive features unique to each region to accelerate diversification. In this way, we will complete the Three Regional Headquarters management system under which Japan, the United States and Europe will each roll out businesses globally.

Additionally, we are working to establish a structure that will enable us to more effectively discover and cultivate competent human resources capable of managing and executing their duties from a global perspective. We also aim to re-instill the entrepreneurial spirit and *San-ji* (Three Selfs)* Spirit that have been passed down since the Company's inception as a foundation for new growth.

In these ways, we will work in Phase V to reform all aspects of development, production and sales to boost profitability while further promoting diversification and the cultivation of new businesses. In doing so, we will overcome changes in the market environment and transform ourselves into an all-new Canon to realize new growth.

**San-ji,* or the Three Selfs, are: self-motivation (taking the initiative and being proactive in all things), self-management (conducting oneself with responsibility and accountability), and self-awareness (understanding one's situation and role in all situations).

New Canon ecommerce sites in Europe allow customers to purchase products and access services direct from Canon online.

Research on ultra-miniature endoscopes at Healthcare Optics Research Lab. (Massachusetts, United States)

Key Challenges for 2016

Under the theme "Taking a decisive first step toward transformation," we will pursue six key challenges in 2016, the inaugural year of Phase V.

The first of these is to **draft and implement plans to revitalize existing businesses**. We will again carry out drastic cost-cutting while working to revitalize businesses, swiftly launching future products that were exhibited at Canon EXPO 2015.*

The second is to **rapidly expand new businesses**. In the large-scale business segments on which Canon's future will rely, such as commercial printing and network cameras, we will work to speed up their expansion and deployment.

Our third challenge is to **accelerate efforts aimed at reducing the cost-to-sales ratio**. We will continue to investigate optimal locations for production bases taking into account such various factors as currency exchange rates, taxation systems, workforce and logistics while working to accelerate cost reductions at every step, including the product-development stage.

The fourth is to **boost sales productivity through marketing reforms**. We will accelerate efforts to address global growth in e-commerce and work to reinforce our solutions business.

The fifth is to **improve R&D productivity through selection and concentration**. Through a process of decisive selection and concentration applied to development themes, we will boost R&D productivity, particularly software development.

Lastly, we will **promote the cultivation of global human resources**. Creating a structure that will enable us to discover talented individuals throughout the Canon Group, we will cultivate globally competent human resources capable of performing their duties while maintaining a global perspective.

*A traveling private exhibition held in four countries once every five years that showcases Canon Group products and technologies.

In Conclusion

We live in a constantly changing world and will likely encounter unexpected events. At Canon, however, we are already steadily laying the groundwork for our leading-edge industries. We will carry out Phase V of our Excellent Global Corporation Plan with firm resolve, undaunted by the speed or power of any waves of change we may face, in order to realize new growth for Canon as a global corporate group.

We look forward to your continued understanding and support.

Fujio Mitarai
Chairman & CEO
Canon Inc.

Canon network cameras play an important role in ensuring safety at the aircraft maintenance centers of airlines. (JAL Engineering Co., Ltd., Japan)

New growth engines acquired through M&A activities are entering a full-scale growth phase with a focus on B2B businesses.

Canon is working to nurture new businesses, along with revitalizing existing ones. With a focus on B2B businesses, where market growth is highly anticipated and stable profits can be expected, we have directed our efforts to new business fields where we can make use of Canon's optical and image processing technologies to maintain competitiveness after market entry, along with M&A activities. The drivers of Canon's growth strategy are the commercial printing business, which has stepped up cooperation with Océ, and the network camera business, where Milestone and Axis have joined the Group.

Commercial Printing Business

In office equipment, Canon aims for stable growth in the medium term, having identified a shift to color models as a growth driver. Yet we also recognize a risk of market shrinkage in the long term, and so we have worked to cultivate new businesses where Canon's technologies can be used to full advantage.

Offset printing has traditionally dominated the commercial printing market for publications such as books, newspapers, catalogues, and posters. However, digital printing, with its advantages in terms of lead time and cost, is growing year by year amid an increasing trend toward flexible, low-volume printing on varied materials. In addition, we can expect demand for consumables to be generated by the enormous volume of printing. Canon therefore added Océ to the Group in 2010, an acquisition that brought with it Océ's more than 130 years of history as well as industry-leading technologies including ultra-fast printing technology and software to keep productivity high. Integration of Océ has enabled Canon to prepare a lineup ranging from copying machines, laser printers, and inkjet printers to commercial printing equipment.

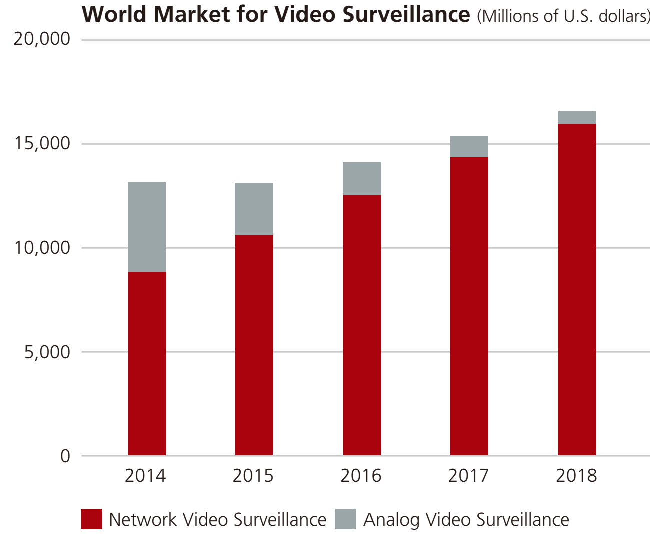
Amid accelerating growth in digital commercial printing, Canon will take aggressive action in growth fields through measures such as enhancing its lineup of printers capable of handling a wide range of materials including plastic and metal.

Network Camera Business

Amid growing needs for security and safety globally, the network camera market is undergoing a rapid shift from analog to digital in concert with advancement in digital technology and the network environment. The market including solution is projected to grow at a rate of nearly 20% per year and reach ¥3 trillion by 2018, propelled by the spread of cloud services and advances in big data processing, along with expected expansion in software and solutions. Canon, with its strengths in optical, sensor, and image-processing technologies, has set its sights on the network camera market, welcoming two top firms in this space to the Group through M&A activities. Milestone, the world's foremost provider of video management software, was the first, joining the Group in 2014. It was followed in 2015 by Axis, the market leader in network camera with outstanding communication technologies and more than 80,000 business partners worldwide. Canon, Axis, and Milestone will work together to generate synergies and forge the market's strongest lineup while working to create products in new business segments. In addition, we will fully harness the management resources of all three companies to accelerate business growth.

A high-speed continuous feed printer at Océ Customer Experience Center. (Poing, Germany)

World Market for Video Surveillance (Millions of U.S. dollars)



Source: IHS Technology

AT A GLANCE

Business Units | **Main Products**

OFFICE BUSINESS UNIT

Office Multifunction Devices (MFDs)

Digital Production Printing Systems

Laser Multifunction Printers (MFPs)

High Speed Continuous Feed Printers

- Office Multifunction Devices (MFDs)
- Laser Multifunction Printers (MFPs)
- Laser Printers
- Digital Production Printing Systems
- High Speed Continuous Feed Printers
- Wide-Format Printers
- Document Solutions

IMAGING SYSTEM BUSINESS UNIT

Interchangeable Lens Digital Cameras

Digital Cinema Cameras

Inkjet Printers

Multimedia Projectors

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

INDUSTRY AND OTHERS BUSINESS UNIT

Semiconductor Lithography Equipment

Digital Radiography Systems

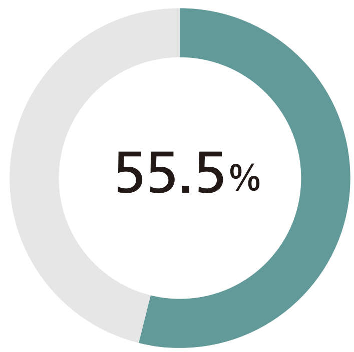
Flat Panel Display (FPD) Lithography Equipment

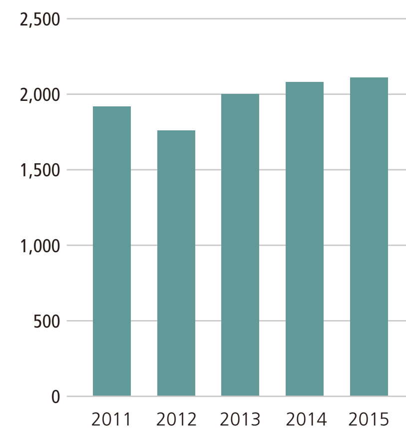
Network Cameras

- Semiconductor Lithography Equipment
- Flat Panel Display (FPD) Lithography Equipment
- Digital Radiography Systems
- Ophthalmic Equipment
- Vacuum Thin-Film Deposition Equipment
- Organic LED (OLED) Panel Manufacturing Equipment
- Die Bonders
- Micromotors
- Network Cameras
- Handy Terminals
- Document Scanners

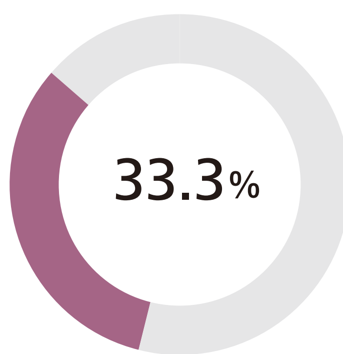
Outline | **Composition of Sales** (%) | **Net Sales** (Billions of yen)

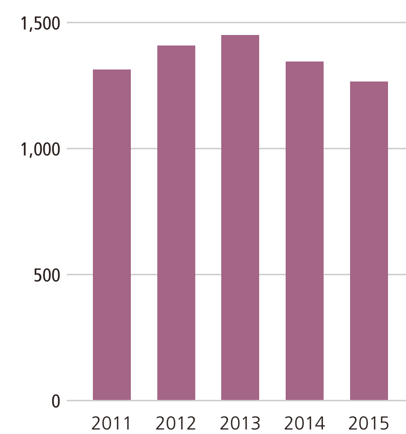
In this segment, Canon offers a comprehensive range of multifunction devices (MFDs), printers, and other equipment featuring high image quality, high resolution, and high speed. Leveraging these products, Canon works in close collaboration with various Group companies and alliance partners to deliver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



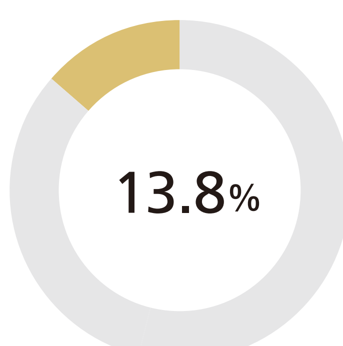


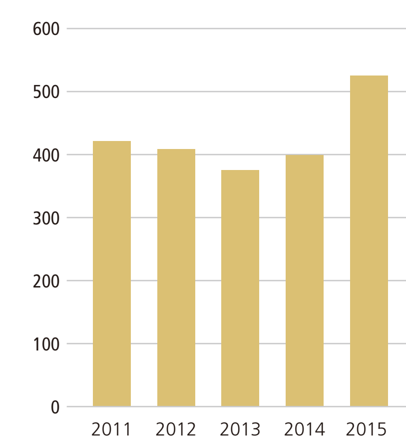
Canon's offerings in this segment include digital cameras, digital camcorders, digital cinema cameras, interchangeable lenses, inkjet printers, and calculators. Canon's digital cameras, digital camcorders and digital cinema cameras, designed to deliver unparalleled image quality, have earned particularly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





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





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

OFFICE BUSINESS UNIT

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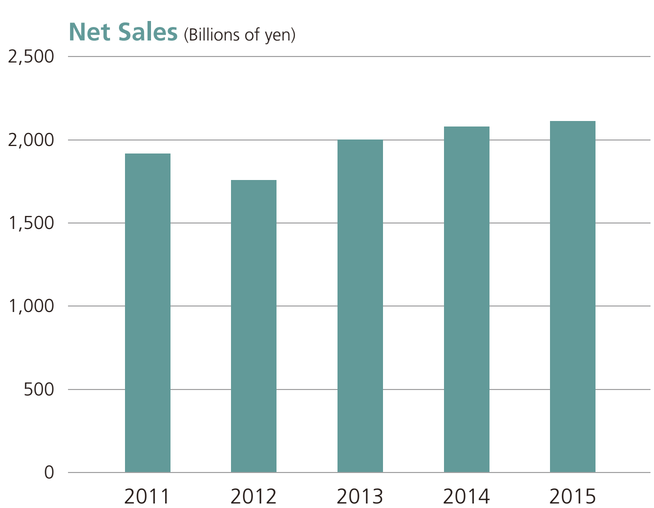
Canon has expanded the functions of its office multifunction devices, which realize enhanced coordination with IT systems and are compatible with various types of system application software, offering an optimal usage environment for all sorts of document-related tasks.



Digital production printing system
imagePRESS C800/C700

2015 Review

With regard to office multifunction devices (MFDs), sales of monochrome models decreased in China and other regions, as the recent ongoing shift in demand from monochrome to color models progressed further. Meanwhile, in color models, Canon launched the compact-body imageRUNNER ADVANCE C3300 series, which features well-balanced image quality, user-friendliness, productivity, and cost-performance. The new models saw steady sales growth around the world, especially in Japan, Europe, and the United States. Also in color models, sales of the imageRUNNER ADVANCE C5200 series were steady, mainly in Europe and the United States. As a result, sales of office MFDs, an aggregate that combines monochrome and color models, were up slightly from 2014.

In digital production printing systems, the imagePRESS C800/C700 series sold well worldwide, significantly boosting Canon's share of unit sales in the light production market targeted by the series. In addition, in the high-end market, the Océ VarioPrint 6000 series performed steadily, particularly in Europe, and sales of the Océ VarioPrint i300, Océ's first high-speed, sheet-fed color inkjet press, got off to a favorable start. Overall sales for digital production printing systems surpassed 2014 results.

With regard to laser multifunction printers (MFPs) and laser printers, sales fell below 2014 levels, due to the impact of various factors, including shrinking markets in emerging countries such as China and Russia, as well as a global decrease in demand for monochrome devices.

These factors, combined with the positive effect of favorable currency exchange rates, resulted in consolidated sales for the business unit totaling ¥2,110.8 billion, up 1.5% from the previous year.

2016 Initiatives

While sales of office MFDs are growing due to augmentation of its color model lineup amid the increasing shift to color machines, Canon will also actively introduce strategic new products in its monochrome models in 2016. At the same time, we will focus on products for which demand for consumables is anticipated, such as high-speed MFDs that meet the need for high-volume output and printers that can provide high-speed business form output from core systems. Regarding solutions, we will roll out services we have built up in each region through M&A activities to the rest of the world, thereby increasing sales for the entire business.

Canon will further strengthen its lineup of laser printers. For example, we will work to recover sales by enhancing our lineup of single-function printers (SFPs) aimed at emerging markets.

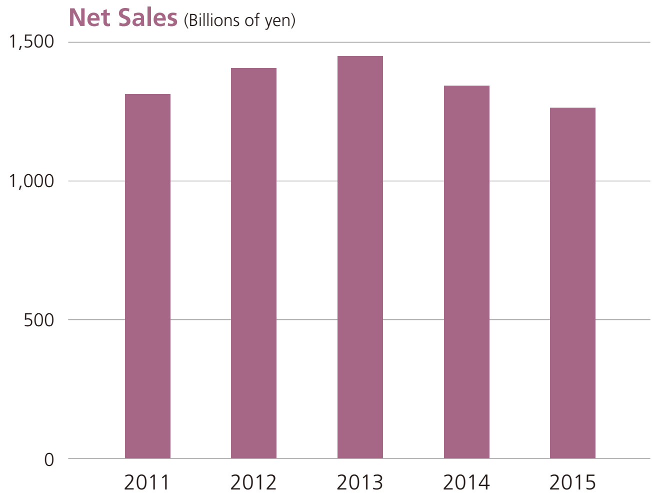
Continued growth is expected in the commercial printing market. Canon will strive to expand sales of new products, as well as traditional continuous-feed printers and wide-format printers, aiming for an increase in consumables generated by enormous printing volume.

Office multifunction device
imageRUNNER ADVANCE C3300 series

Digital production printing system Océ VarioPrint i300

IMAGING SYSTEM BUSINESS UNIT

The Cinema EOS System revolutionized the motion picture production industry and has a strong presence. Through high resolution and an expressive color gamut, Canon is developing 8K cameras and lenses that can create images so vivid they seem to come alive on screen.



Interchangeable lens digital camera
EOS 5DS/5DS R

2015 Review

Although overall unit sales of interchangeable lens digital cameras declined due to the impact of the economic slowdowns in China and Russia, signs of recovery began to appear in Japan and the United States. Amid such circumstances, Canon launched the EOS 5DS and EOS 5DS R digital SLR cameras, which boast the highest-ever resolution for EOS models, as well as the EOS M3 and EOS M10 non-reflex cameras, thereby maintaining the No. 1 share in unit sales worldwide of interchangeable lens digital cameras.

As for digital compact cameras, unit sales declined as the market continued to contract amid the growing proliferation of smartphones. However, Canon raised its sales ratio for high-end products such as the PowerShot G5 X.

The Cinema EOS System of digital cinema cameras, which are aimed at the motion picture production industry, sold well, particularly the new EOS C300 Mark II.

Sales of broadcasting equipment were solid, backed by continuing demand for models designed for sports broadcasting and for HDTV format equipment in China and other countries. The CN20x50 IAS H, a new zoom lens for 4K cameras equipped with large-format sensors, was also well received.

As for inkjet printers, although Canon has been working to expand sales through its broad product lineup, which ranges from home-use printers to MAXIFY-series business models, unit sales were lower than in 2014 due to shrinking markets, primarily in Asia. In contrast, sales of consumables enjoyed solid demand.

Unit sales of large-format inkjet printers remained at the same level as the previous year, and sales of consumables grew steadily with an increase in the number of units in operation.

As a result, consolidated sales in this business unit stood at ¥1,263.8 billion, down 5.9% from the previous year.

2016 Initiatives

In interchangeable lens digital cameras, Canon will strengthen its high-end models through technological evolution befitting an Olympic year, in order to stimulate replacement demand among professionals and advanced amateurs. In digital compact cameras, we will concentrate on the high-end models that are performing well, in an effort to improve profitability. We will also expand our business domains, not only in the consumer camera market, but also in the B2B field, as exemplified by the Cinema EOS System.

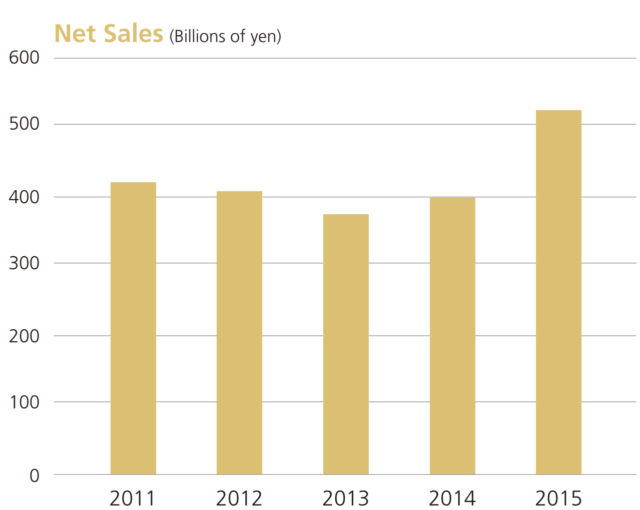
In inkjet printers, we will expand sales by augmenting our product lineup for emerging countries, such as the large-capacity ink tank models launched at the end of last year, to meet the diversified needs of emerging markets in Asia and elsewhere. In addition, we will bolster sales of business products such as the MAXIFY series and large-format inkjet printers, as well as the imagePROGRAF PRO-1000, a new product aimed at professional photographers that offers advanced image quality and high productivity. This will also lead to an increase in the sales of consumables.

Interchangeable EF lenses for Canon EOS-series

Inkjet printer
imagePROGRAF PRO-1000

INDUSTRY AND OTHERS BUSINESS UNIT

Canon has accelerated development of next-generation semiconductor lithography equipment using nanoimprint technology with sub-20-nanometer high-resolution processes. With the aim of a commercial launch soon, Canon seeks to solidify its position in the field of semiconductor lithography equipment.



Semiconductor lithography equipment FPA-5550iZ

2015 Review

In the business of semiconductor lithography equipment, sales were steady for the FPA-5550iZ i-line steppers and for FPA-6300ES6a KrF scanners, which feature high productivity. This reflects strong capital investment for the manufacturing of memory devices in response to growing demand for mobile devices such as smartphones and for cloud servers. Furthermore, lithography equipment designed for manufacturing power semiconductors and LEDs also saw considerable sales growth. As for flat panel display (FPD) lithography equipment, sales grew significantly for equipment used in the fabrication of large-sized panels such as the MPAsp-H800 series on a boost from growth in capital investment for manufacturing large-sized panels.

In the medical equipment field, our digital radiography business faced price pressure by competition, but the release of high-value-added software bolstered its competitiveness, and new non-mydriatic fundus cameras supported ophthalmic equipment sales.

In network cameras, sales significantly increased compared to 2014 as a result of major reinforcements to Canon's product lineup in response to rising concerns about security and safety and diversification of use. The business was further strengthened by the addition to the Group of Axis, the global leader in the network camera market. Sales of document scanners manufactured by Canon Electronics Inc. remained at the same level as the previous year overall, as sales growth in Europe and Asia offset a drop in the United States. Sales of semiconductor film deposition equipment manufactured by Canon ANELVA Corporation, organic LED (OLED) panel manufacturing equipment made by Canon Tokki Corporation, and factory automation (FA) systems and semiconductor manufacturing equipment made by Canon Machinery Inc. grew as a result of increased capital investments by customers.

As a result of these factors, along with the impact of the new consolidation of Axis, consolidated sales for this business unit increased 31.6% year on year, to ¥524.7 billion.

2016 Initiatives

In the lithography equipment market, capital investment is expected to remain strong. In semiconductor lithography equipment, unit sales are expected to surpass those of the previous year, backed by a continued high market share for i-line steppers and an expanded share for KrF scanners, which feature the industry's highest levels of productivity and overlay accuracy. FPD lithography equipment sales are expected to grow sharply on further growth in unit sales of high-definition mid- and small-size panels, and OLED panel manufacturing equipment sales are also expected to expand rapidly. Canon will continue to promote the development of next-generation semiconductor lithography equipments employing nanoimprint technology, which was acquired through M&A in 2014, targeted at the leading-edge high-resolution patterning segment in semiconductors.

Growth is also expected to continue in the network camera market. Through a fusion of Canon's imaging technology, Axis's network technology, and Milestone's video management software, we aim at further business expansion by providing the most advanced network video solutions.

Network cameras
VB-R11, VB-M741LE, and VB-M641VE

Organic LED (OLED) panel manufacturing equipment

CORPORATE GOVERNANCE

At a monthly meeting of all company executives, the CEO provides updates on earnings progress and important matters to implement in the future as a way to share crucial information.

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

Basic Policy

In order to establish a sound corporate governance structure and continuously raise corporate value, Canon believes that it is essential to improve management transparency and strengthen functions to supervise and monitor management. In this respect, a sense of ethics and mission held by each executive director and employee is very important for the Company.

Representative Directors, Directors, and Board of Directors

The Board of Directors makes decisions on matters prescribed in the Companies Act, including a policy for establishing systems necessary to ensure the properness of operations (a basic policy for an internal control system) and other important management matters. Furthermore, the Board receives reports on a regular basis and otherwise as necessary on the execution of operations by representative directors and executive officers under the direction of the representative directors and it oversees the execution of these operations.

As of fiscal 2015, the Board of Directors consisted of 17 directors. However, it was resolved at the 115th Ordinary General Meeting of Shareholders held on March 30, 2016 to change to a structure with a total of six directors, comprising four directors from Canon career veterans and two outside directors who are independent directors*.

Executive officers are responsible for the execution of operations as a group executive or chief executive in charge of one or more of the Company's main operations. Meanwhile, the Board of Directors consists of representative directors with years of experience at the Company who manage multiple divisions and functions, along with independent outside directors who have impartial perspectives on management that would differ from those of Canon career veterans. With this compact Board, Canon aims to speed up its management via a rigorous system centered on decision-making from a high-level, all-around perspective and oversight of execution of operations.

The responsibilities of the four representative directors are divided as follows. The Chief Executive Officer (CEO) is responsible for overall management of the Group as a whole, while the Chief Operating Officer (COO) manages the Group's businesses under the policies set by the CEO and serves as the president of the Company. The Chief Financial Officer (CFO) oversees the Group's financial matters, and the Chief Technical Officer (CTO) oversees technology and R&D.

As of April 1, 2016, there will be 37 Executive Officers, including two women and two with foreign citizenship.

*Independent directors: Stock exchanges in Japan require listed companies to appoint outside directors and/or outside Audit & Supervisory Board members and to report their name. Outside directors and Audit & Supervisory Board members should have no possible conflict of interests with regular shareholders. People related to the parent company or major business partners, consultants who receive large remunerations from the company, and their close relatives cannot be selected as independent directors.

Corporate Strategy Committee, Risk Management Committee, and Disclosure Committee

The Corporate Strategy Committee, consisting of Representative Directors and some Executive Officers, functions as an advisory body to the CEO. Among items to be decided by the CEO, the Committee undertakes prior deliberations on important matters pertaining to Canon Group strategies. Outside directors and outside Audit & Supervisory Board members attend the Corporate Strategy Committee meetings and proffer their opinions.

Based on its policy on establishment of an internal control system, the Company set up the Risk Management Committee,

Directors and Audit & Supervisory Board Members (as of April 1, 2016)

Representative Director
Chairman & CEO
Fujio Mitarai

Representative Director
President & COO
Masaya Maeda

Representative Director
Executive Vice President & CFO
Toshizo Tanaka
Group Executive of Human Resources Management & Organization Headquarters

Representative Director
Senior Managing Director & CTO
Shigeyuki Matsumoto
Group Executive of R&D Headquarters

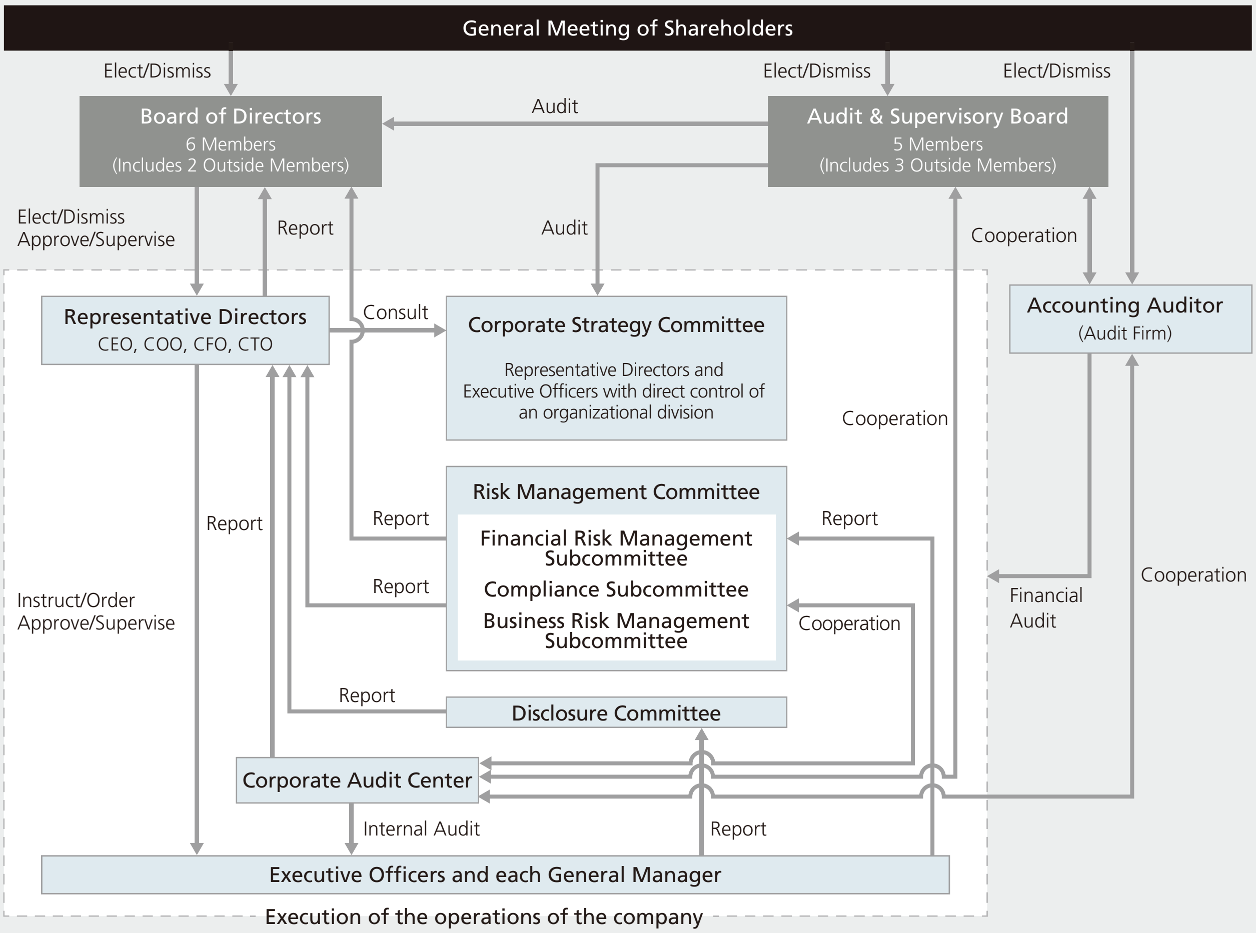
Directors
Kunitaro Saida *(Outside)*
Attorney

Haruhiko Kato *(Outside)*
President & CEO of Japan Securities Depository Center, Incorporated

Audit & Supervisory Board Members
Makoto Araki
Kazuto Ono
Tadashi Ohe *(Outside)*
Osami Yoshida *(Outside)*
Kuniyoshi Kitamura *(Outside)*

Note: Although this annual report is for FY2015, the above list of Directors and Audit & Supervisory Board members is as of April 1, 2016.

Governance Structure (as of March 30, 2016)



which formulates policy and action proposals for improvement of the risk management system in the Canon Group under decisions of the Board of Directors. The Risk Management Committee consists of three entities: the Financial Risk Management Subcommittee, which improves systems on the credibility of financial reporting; the Compliance Subcommittee, which ensures thorough implementation of corporate ethics and improves legal compliance systems; the Business Risk Management Subcommittee, which improves systems prepared for overall business risks, including insufficient product quality and information leakage. The Risk Management Committee verifies the risk management system and reports the status to the CEO and the Board of Directors.

In addition, the Disclosure Committee undertakes deliberations on information disclosure, including content and timing, to ensure timely and accurate disclosure of important company information.

Audit & Supervisory Board

Canon is a "Company with an Audit & Supervisory Board." The Board consists of five members, three of which are independent outside Audit & Supervisory Board members. In accordance with auditing policies and plans decided at Audit & Supervisory Board meetings, members of the Audit & Supervisory Board attend Board of Directors meetings, Corporate Strategy Committee meetings, and other relevant meetings, while receiving verbal reports from directors, reviewing important approval documents, and examining the business and financial asset statuses of the Company and its subsidiaries. In these ways, the Audit & Supervisory Board meticulously checks directors' and others' execution of the company operations, including establishment and operation of the internal control system, thus is fulfilling a management oversight function. The Board also works in close alliance with the Internal Audit Division and the accounting auditors to improve the efficacy of monitoring.

Internal Audit Division

The Corporate Audit Center, with about 70 members, is the Company's internal auditing arm. It conducts audits and evaluations and provides guidance on all operations and sectors without exception, including those of Group companies, from various perspectives, such as business efficacy and efficiency, compliance, and information security. Audit results are reported to the CEO and Audit & Supervisory Board and complement audits conducted by members of that board.

Accounting Auditor

The Company has an auditing service contract with its independent auditor, Ernst & Young ShinNihon LLC, to audit its financial statements. To check the validity of the audits, the Company's Audit & Supervisory Board members receive detailed explanations from the accounting auditors about the quality management system regarding audits.

With the aim of monitoring the independence of the accounting auditors, the Company introduced a prior approval system by the Audit & Supervisory Board for contents of auditing and other service contracts and relevant fees. Based on "policies and procedures of the prior approval for both auditing and non-auditing services," each contract is closely reviewed for prior approval.

Compliance

Shortly after its founding, Canon established the *San-Ji* or the Three Selfs, are: self-motivation (taking the initiative and being proactive in all things), self-management (conducting oneself with responsibility and accountability), and self-awareness (understanding one's situation and role in all situations), or understanding one's situation and role in it. In 2001, Canon established the Canon Group Code of Conduct, inspired by the above Three Selfs, and each Group company makes efforts to enforce the Code.

Countering Antisocial Forces

Canon has a basic policy prohibiting relationships of any kind with antisocial forces that represent a threat to social order and security. To uphold this basic policy, Canon has established a department dedicated to activities aimed at countering such parties while reinforcing cooperative ties with applicable public authorities. In addition, Canon's Employment Regulations include a clause prohibiting such relationships, and the Company continues to step up efforts to ensure strict employee adherence.

Risk Management

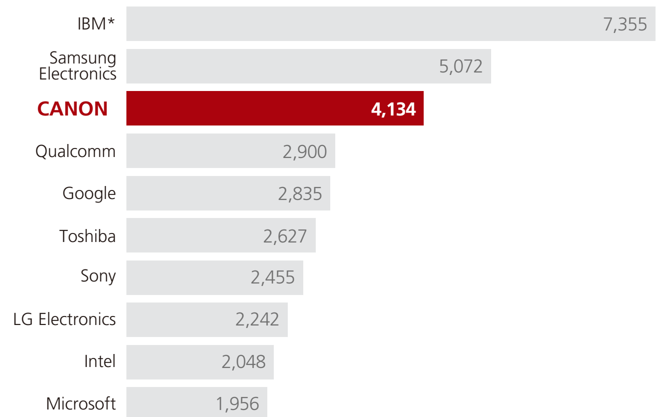
As Canon expands its business on a global scale, business and other risks to which it may be exposed continue to diversify. In accordance with policies of its Risk Management Committee, Canon calculates and investigates conceivable risks across the entire Group. Canon also strives to prevent or minimize the emergence of risk by formulating company regulations and other rules and conducting employee education.

San-ji, or the Three Selfs, are: self-motivation (taking the initiative and being proactive in all things), self-management (conducting oneself with responsibility and accountability), and self-awareness (understanding one's situation and role in all situations). (calligraphy by Canon's first president, Takeshi Mitarai)

Driving new dye ink R&D with a database of over 10,000 dye varieties, Canon pursues molecular structures that improve dye ink durability (light stability) via original designs.

Seeking to create a new Canon, the Company is reinforcing an R&D structure spanning Japan, the United States, and Europe under the Three Regional Headquarters management system.

2015 Top Ten U.S. Patent Holders by Company



*IBM is an abbreviation for International Business Machines Corporation.
Source: Preliminary data released by IFI CLAIMS Patent Services, a U.S. research company specialized in patent information

Strengthening Our Global R&D Structure

Pursuing globalized diversification of its operations in the field of R&D, Canon has established the foundation of the Three Regional Headquarters management system that leads to new businesses emerging from Japan, the United States, and Europe.

For example, in the United States, Canon U.S. Life Sciences, Inc. is making steady progress in genetic testing systems, while Healthcare Optics Research Laboratory is steadily advancing research on ultra-miniature endoscopes and medical robotics. In Europe, we are reinforcing R&D in business fields mainly in printing solutions centered on Océ, as well as making further use of existing R&D centers to advance R&D in new fields.

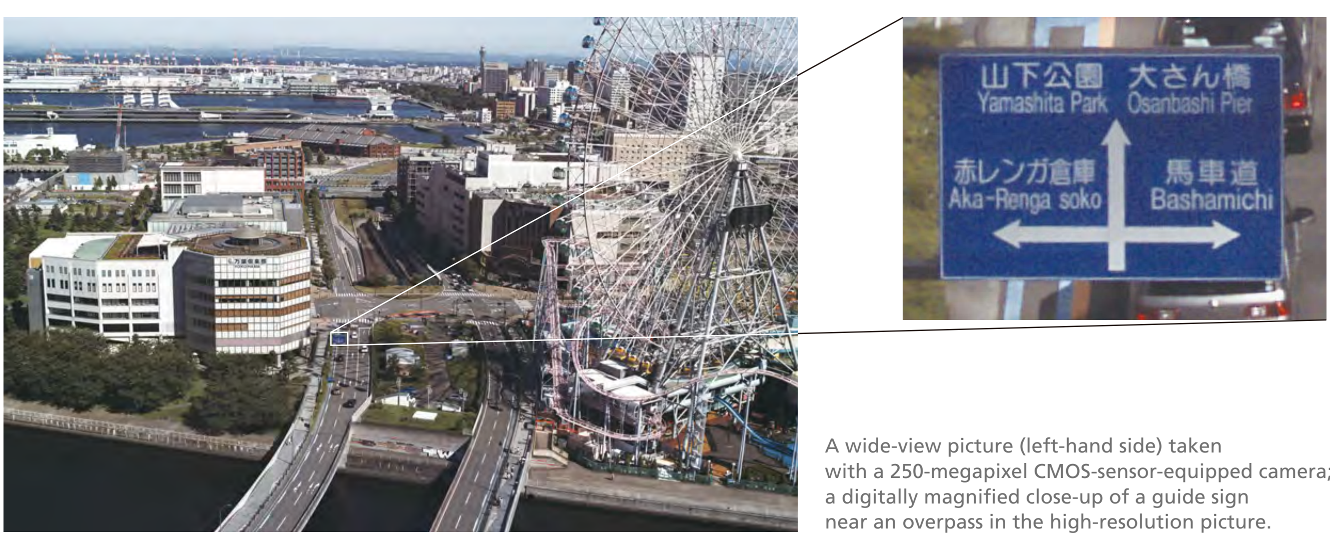
R&D Expenses and Patents

Canon is bolstering R&D activities to enable the ongoing development of innovative products and services. In the year under review, R&D expenses amounted to ¥328.5 billion, up 6.3%, or ¥19.5 billion, from the previous year. The ratio of R&D expenses to net sales was 8.6%. This focus on R&D activities has cemented Canon's high status in the field of intellectual property. In 2015, Canon was granted 4,134 patents in the United States, ranking it third in the world and the top ranked Japanese company for an eleventh consecutive year.

Initiatives to Establish New Businesses

Taking a long-term standpoint, Canon is concentrating on pre-competitive fields where the seeds of new technologies for the future are discovered. At the same time, the Company is continually bolstering R&D activities centered on key parts and key devices in order to enhance the competitiveness of its products. With regard to CMOS sensors employed in interchangeable lens digital cameras and digital cinema cameras, in 2015, a prototype camera equipped with a newly developed approximately 250-megapixel sensor succeeded in capturing images of the lettering printed on the body of an aircraft flying roughly 18 kilometers away. By raising the performance levels of CMOS sensors to their fullest extent, we are developing sensors applicable to functions in such areas as astronomical and nature observation, medical research, aviation, and surveillance and security. We are also promoting businesses of CMOS sensor components.

In addition, by integrating Canon's material appearance acquisition and image-processing technologies with Océ's elevated printing technology using UV-curable printers, Canon is working on the development of technology to faithfully reproduce material appearance characteristics of the original object, such as glossiness, surface contours, and transparency, with a printer. We will aim to expand its application in such areas as wallpaper and other interior design materials, and product packaging.



A wide-view picture (left-hand side) taken with a 250-megapixel CMOS-sensor-equipped camera; a digitally magnified close-up of a guide sign near an overpass in the high-resolution picture.

PRODUCTION

At Canon, employees with exceptional work skills are certified as a "Meister" (a multi-skilled worker). As participants in developing production equipment and reviewing designs, they are indispensible to advancing productivity improvement efforts in Japan. An S-grade Meister assembles a digital production system. (Toride Plant, Japan)

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

Belief in "Internal Production"

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

Establishing a Globally Optimized Production System

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

As one of its specific efforts in that regard, Canon will make its Japanese production sites "mother plants" that produce mainly high-end models, harnessing the full-suite of strengths in Japan from R&D and procurement operations to production engineering technologies and manufacturing facilities. As we are bringing production back to Japan, the ratio of manufacturing in Japan will increase to 60% over the next three years or so. At home, Canon will further improve productivity by enhancing its production engineering technology through initiatives such as "man-machine cell" production systems that integrate manual and automated processes; in-house production, where Canon develops and produces its own parts and materials as well as manufacturing equipment; and expansion of the fields where automation technologies such as the Canon-developed Super Machine Vision are employed. Such efforts will accelerate the return of production to Japan.

Meanwhile, we are moving ahead with functional specialization between Japan and Asia, allocating mass production of mid-range and low-priced products to our Asian production sites in China, Thailand, the Philippines and other countries.

In the Americas and Europe, Canon is making use of automated production systems to implement localized production mainly of consumables such as toner cartridges, with the aim of shortening distances to markets in order to deliver products in a timely manner, while reducing transportation costs and inventory in transit.

Environmental Friendly Manufacturing; Enhanced Product Quality

Canon actively seeks to prioritize purchases of environmentally conscious parts and materials as well as shift to transportation modes that have minimal environmental impact. We also focus on manufacturing initiatives that are friendly to the global environment.

The consolidation of the Quality Management Headquarters, which had been split across five sites, in the Tamagawa Office as a way to improve quality was completed in 2015. With this, we have centralized the contact points dealing with consultations and requests related to quality, and this is expected to increase the processing speed of support for businesses. In conjunction with this, we put into place an even stronger quality system by introducing cutting-edge facilities and facilities to handle large products.

In-house production: Canon-developed fixing belts for copiers are produced in Japan. (Toride Plant)

Semi-anechoic chamber: the new large-scale semi-anechoic chamber is for measuring electromagnetic waves emitted by products. (Tamagawa Office, Japan)

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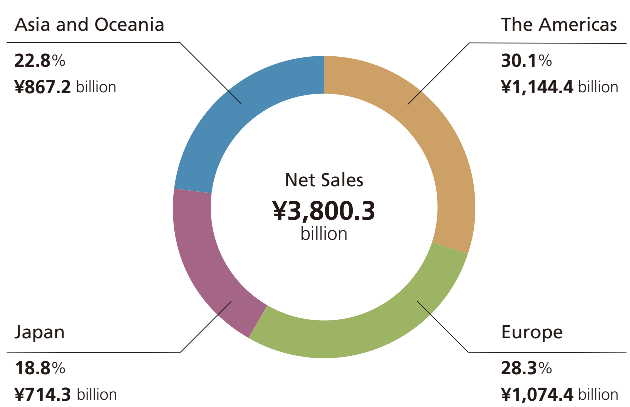
Canon EXPO exhibitions introducing the Group's vision and values for the future were held in New York, Paris, and Tokyo in 2015. (Giant photo prints of Yankee Stadium were stitched together to recreate a baseball stadium backdrop for Canon EXPO 2015 New York.)

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

Composition of Sales by Region



Japan

Sales in Japan amounted to ¥714.3 billion, or 18.8% of consolidated net sales.

In the market for consumer products, challenging conditions carried over from the previous year amid a prolonged slump in personal consumption. Nevertheless, Canon maintained top market shares in both camera products and inkjet printers, by introducing various new products and implementing various sales promotion activities.

As for the B2B field, within the IT solutions segment, Canon's main business of individual system development performed strongly amid strong investment, mainly among financial institutions. In addition, growing demand for security led to greater investment by companies, resulting in an increase in sales in the fields of computer software and peripherals, and surveillance cameras.

The Americas

Sales in the Americas amounted to ¥1,144.4 billion, or 30.1% of consolidated net sales.

Canon Americas is making steady progress toward a regional headquarters with development, manufacturing, and sales functions under our Three Regional Headquarters management system. In particular, Canon BioMedical, Inc., established in 2015 as a crucial first step in that endeavor, is the first new business launched at Canon Americas since it assumed headquarters functions. Canon BioMedical is responsible for development, manufacturing, and marketing of genetic testing systems based on life science technologies cultivated in the United States.

Canon EXPO 2015 in New York, featuring the common slogan, "Canon See Impossible," received high marks from many stakeholders.

Europe (Europe, Middle East, Africa)

Sales in Europe amounted to ¥1,074.4 billion, or 28.3% of consolidated net sales.

Canon increased market share while focusing on developing new opportunities for growth, including entering the 3D printing market. Strategic acquisitions of Integra Document Management in Italy and Lifecake in UK also drove growth in solutions and services for both businesses and consumers. Canon strengthened its sales and marketing through a very successful Canon EXPO 2015 in Paris, launching new Canon ecommerce sites for consumer products and forming a new sales organization in Central and North Africa.

Asia and Oceania

Sales in Asia and Oceania amounted to ¥867.2 billion or 22.8% of consolidated net sales.

In China, Canon added a Northwest branch and a Northeast branch, creating a six-branch system that is able to respond more swiftly and precisely to market needs. In India, we opened a technical training center and worked to train and develop sales personnel in the production printing systems business. Furthermore, we hold a unique photo contest called the Canon PhotoMarathon every year in the region, with the aim of promoting the culture of photography and increasing the number of camera users.

In Australia, Harbour IT Pty. Ltd., a leading IT managed services provider acquired by Canon in 2014, contributed to an increase in overall sales.

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Canon acquired Lifecake, the U.K. company behind the popular Lifecake photo-sharing app for families to store, organize, and share memories of their children.

Canon PhotoMarathon Singapore 2015 welcomed 2,600 participants, many of them photo enthusiasts in their twenties.

The "Silk Road Intangible Heritage Culture Protection Project" that Canon (China) Co., Ltd. has led since 2014 has striven to preserve that era's cultural heritage using Canon imaging technologies. (A Buddhist priest prepares for spring amid falling snow at Da Xingshan Shrine, near the birthplace of Chinese Esoteric Buddhism.)

Guided by its *kyosei* ("living and working together for the common good") philosophy, Canon is promoting CSR activities with the aim of becoming a truly excellent corporation that is admired and respected the world over.

Closed-loop Recycling

Canon's Basic Approach to CSR

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

Environmental Activities

Renewed Automated Toner Cartridge Recycling System Starts Operations

Canon has been promoting its toner cartridge recycling program since 1990, as it pursues ideal recycling for resource circulation. We also began the closed-loop recycling process* in 1992, and new toner cartridges using recycled parts and plastics are being sold worldwide. Furthermore, our CARS-T** system commenced operations in 2015 at Canon Ecology Industry Inc., our recycling hub in Japan, as a completely retooled system with an automated toner cartridge recycling process.

*Materials obtained from Canon products collected from the market are reused repeatedly in Canon products and parts with the same quality standards as new products.

**CARS-T: Canon Automated Recycling System for Toner Cartridge

Conservation Activities at National Parks in the United States

Canon U.S.A. continues to provide support for environmental protection activities in U.S. national parks. The company began supporting Yellowstone National Park in 1995 and Acadia National Park in 2013. Canon imaging equipment is used to observe wildlife, create video libraries and support communication activities.

Social Contribution Activities

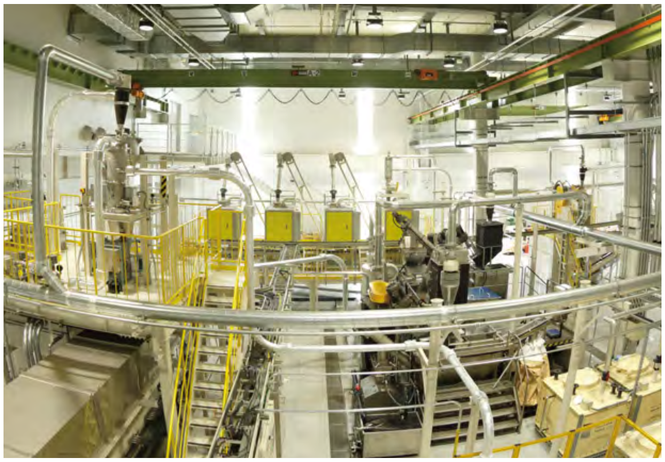
Canon conducts wide-ranging social contribution activities in various parts of the world to help create a better society.

Canon Foundation Announces Sixth Grant Program Recipients

The Canon Foundation aims to contribute to the ongoing prosperity and well-being of mankind. It has offered two research grant programs, known as the Creation of Industrial Infrastructure grant and Pursuit of Ideals grant. In 2015, 15 projects were selected for the sixth research grant program.

The Tsuzuri Project

Canon and the non-profit organization Kyoto Culture Association jointly promote a project called the "Tsuzuri Project" (Official title: Cultural Heritage Inheritance Project). The aim of the project is to preserve original cultural assets while maximizing the effective use of high-resolution facsimiles of cultural assets. These facsimiles are created by blending Canon's latest digital technology and traditional Japanese crafts, such as gold leaf craftwork. As a result of the project, original cultural assets can be kept in the more favorable environment of museums while facsimiles can be used



CARS-T realizes a much higher throughput in recycled plastic volumes and a higher degree of purity in recycled plastics.

A high-resolution reproduction of the "Dragon and Clouds" (Unryu Zu) painting has been donated to Japan's Tenryuji Temple; the original is housed in the collection at the Museum of Fine Arts, Boston.

for educational purposes and public exhibits. Since the program began in 2007, the cumulative total of reproduced and donated items has reached 33 (as of March 2016).

The Silk Road Intangible Heritage Culture Protection Project

Cultural charity events in Gansu Province, China are the latest stops in the "Silk Road Intangible Heritage Culture Protection Project" organized by Canon China. Commencing in 2014 with events in Shanxi and Henan provinces, the project aims to protect intangible heritage culture along the Silk Road by harnessing Canon's imaging technologies and promoting Chinese and foreign cultural exchanges and cooperation. It also collects photos from the public. In 2015, one of the programs organized under the project photographed scenes from everyday life in the Gansu Province cities of Tianshui, Zhangye, Wuwei, Jiayuguan, and Dunhuang.

Beyond the Horizon

Since 2014, Canon Middle East FZ-LLC has supported a photography project for young people. Sponsored by Mathare Foundation, a non-profit organization, the aim of the project is to create an environment where the talents of economically underprivileged children can be nurtured. The children attending the Beyond the Horizon workshops held in 2015 studied the basics of photography using cameras donated by Canon.

Addressing the Issue of Conflict Minerals

Seeking to ensure that customers can use Canon products with peace of mind, the Canon Group addresses the issue of conflict minerals.

Canon has been conducting full-scale investigations targeting products produced at manufacturing bases across the entire Canon Group. As of February 2016, no specific parts or materials have been found to have contributed to funding armed groups in conflict regions as defined by U.S. legislation.

Canon Inc., a U.S. listed company, files a report at the end of May every year regarding the Company's status on this issue with the U.S. Securities and Exchange Commission. The Company plans to undergo independent private sector audits of the report beginning in 2016. This report is also made available on Canon's website.

In 2015 Canon joined the Conflict Free Sourcing Initiative (CFSI), an international program that plays the leading role in response to the conflict minerals, and continues to support industry activities.

Cultivating Diverse Human Resources

Canon is committed to diversity of human resources. We welcome people of all types—irrespective of race, gender, age, customs, and value perceptions—and deploy such differences to foster our growth as an organization. Since 2012, we have engaged in in-house projects with top priority on helping maximize the potential of women in the workplace. In 2015, Akiko Tanaka, President & CEO of Canon BioMedical became the first female Executive Officer at Canon.

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Canon Middle East sponsored "Beyond the Horizon," a three-month photography project in Kenya that commenced in September 2015.

Akiko Tanaka, president of Canon BioMedical is Canon's first female executive officer.

FINANCIAL SECTION

TABLE OF CONTENTS

FINANCIAL OVERVIEW

GENERAL

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

OVERVIEW

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

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

Economic environment

Looking back at the global economy in 2015, the U.S. economy continued to grow steadily as employment conditions and consumer spending progressively improved. In Europe, developed countries such as the U.K. led a moderate economic recovery. In contrast, the growth of China's economy continued to decline, weighed down by excessive investments, and the economies of emerging countries, including those of Southeast Asia and India, slowed due to such factors as the recession in China and a decline in resource prices. As for the Japanese economy, improvements were seen in both corporate earnings and employment conditions during the year. Despite expectations at the beginning of 2015 that the global economy would realize a modest recovery led by the U.S. economy, during the second half, as the slowdown in China's economy became evident, emerging economies also grew weaker. As a result, the global economy overall experienced its lowest level of growth since the financial crisis precipitated by Lehman Brothers' bankruptcy in 2008.

Market environment

As for the markets in which Canon operates amid these conditions, demand for office MFDs remained firm, mainly for color models. As for cameras, the interchangeable-lens digital camera market continued to face harsh conditions owing to currency depreciations in emerging countries and the slowing growth in China. Likewise, demand for digital compact cameras also declined amid the shrinking market. Additionally, demand for inkjet printers decreased in emerging countries, mainly in Asia, due to the depreciations of emerging country currencies and the slowdown in China. In the industrial equipment market, ongoing strong investment by manufacturers led to healthy demand for semiconductor lithography systems for memory devices, image sensors and power semiconductor devices. Additionally, demand for lithography equipment used in the production of flat panel displays ("FPDs") increased for large-size panels as device manufacturers boost capital investment for larger-size LCD panels that offer higher levels of resolution.

The average value of the yen during the year was ¥121.13 against the U.S. dollar, a year-on-year depreciation of approximately ¥15, and ¥134.20 against the euro, a year-on-year appreciation of approximately ¥6.

Summary of operations

Sales of digital cameras and inkjet printers declined in the face of continued harsh conditions, mainly in China and emerging Asian countries. By contrast, sales of color-model office MFDs and color-model light-production printing systems increased steadily. Sales of semiconductor lithography equipment and FPD lithography equipment also largely exceeded those for the previous year thanks to favorable market conditions. Consequently, benefitting from the boost provided by the acquisition of Axis and the positive effect of favorable currency exchange rates, net sales for the year increased 2.0% year on year to ¥3,800,271 million. The gross profit ratio for the year rose 1.0 point year on year to 50.9% thanks to ongoing cost-cutting activities and highly profitable new products. Operating expenses increased 5.4% year on year to ¥1,579,174 million owing to such factors as the increase in foreign-currency-denominated operating expenses after conversion into yen due to the depreciation of the yen, along with the impact of the acquisition of Axis and an increase in R&D expenses related to new products. As a result, operating profit decreased by 2.3% to ¥355,210 million. Other income (deductions) decreased by ¥27,522 million due to foreign currency exchange losses, leading to a year-on-year decline in income before income taxes of 9.3% to ¥347,438 million, and a decrease in net income attributable to Canon Inc. of 13.6% to ¥220,209 million.

Key performance indicators

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

Revenues

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

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

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

Operating profit ratio (ratio of operating profit to net sales) and R&D expense to net sales ratio are considered to be KPIs by Canon. Canon is focusing on two areas for improvement. Canon is striving to control and reduce its selling, general and administrative expenses as its first key point. Secondly, Canon's R&D policy is designed to maintain 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.

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

Canon Inc. 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 the company 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

	2015	2014	2013	2012	2011
Net sales (Millions of yen)	**¥3,800,271**	¥3,727,252	¥3,731,380	¥3,479,788	¥3,557,433
Gross profit to net sales ratio	**50.9%**	49.9%	48.2%	47.4%	48.8%
R&D expense to net sales ratio	**8.6%**	8.3%	8.2%	8.5%	8.7%
Operating profit to net sales ratio	**9.3%**	9.8%	9.0%	9.3%	10.6%
Inventory turnover measured in days	**47 days**	50 days	52 days	57 days	46 days
Debt to total assets ratio	**0.0%**	0.0%	0.1%	0.1%	0.3%
Canon Inc. shareholders' equity to total assets ratio	**67.0%**	66.8%	68.6%	65.7%	64.9%

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

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

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

Revenue recognition

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

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

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

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

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

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

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

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

Allowance for doubtful receivables

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

Valuation of inventories

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

Impairment of long-lived assets

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

Property, plant and equipment

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

Goodwill and other intangible assets

Goodwill and other intangible assets with indefinite useful lives are not amortized, but are instead tested for impairment annually in the fourth quarter of each year, or more frequently if indicators of potential impairment exist. Canon performs its impairment test of goodwill using the two-step approach at the reporting unit level, which is one level below the operating segment level. All goodwill is assigned to the reporting unit or units that benefit from the synergies arising from each business combination. If the carrying amount assigned to the reporting unit exceeds the fair value of the reporting unit, Canon performs the second step to measure an impairment charge in the amount by which the carrying amount of a reporting unit's goodwill exceeds its implied fair value. 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 2015 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 exceeded its respective carrying amount. 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 5 years, trademarks are 15 years, patents and developed technology are from 7 years to 16 years, license fees are 7 years, and customer relationships are from 8 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 restructuring activities and other factors. Any changes in these factors may require possible recognition of significant valuation allowances to reduce the net carrying value of these deferred tax asset balances. When Canon determines that certain deferred tax assets may not be recoverable, the amounts, which may not be realized, are charged to income tax expense and will adversely affect net income.

Employee retirement and severance benefit plans

Canon has significant employee retirement and severance benefit obligations that are recognized based on actuarial valuations. Inherent in these valuations are key assumptions, including discount rates and expected return on plan assets. Management must consider current market conditions, including changes in interest rates, in selecting these assumptions. Other assumptions include assumed rate of increase in compensation levels, mortality rate, and withdrawal rate. Changes in 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 2015, Canon estimated a weighted-average discount rate used to determine benefit obligations of 1.1% for Japanese plans and 3.0% for foreign plans and a weighted-average expected long-term rate of return on plan assets of 3.1% for Japanese plans and 5.6% 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 2015, a decrease of 50 basis points in the discount rate increases the projected benefit obligation by approximately ¥92,006 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 2015, a change of 50 basis points in the expected long-term rate of return on plan assets would cause a change of approximately ¥4,222 million in net periodic benefit cost. Canon multiplies management's expected long-term rate of return on plan assets by the value of its plan assets to arrive at the expected return on plan assets that is included in pension expense. Canon defers recognition of the difference between this expected return on plan assets and the actual return on plan assets. The net deferral affects future pension expense.

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

CONSOLIDATED RESULTS OF OPERATIONS

SUMMARY OF OPERATIONS

	Millions of yen				
	2015	change	2014	change	2013
Net sales	**¥3,800,271**	**+2.0%**	¥3,727,252	-0.1%	¥3,731,380
Operating profit	**355,210**	**-2.3%**	363,489	+7.8%	337,277
Income before income taxes	**347,438**	**-9.3%**	383,239	+10.3%	347,604
Net income attributable to Canon Inc.	**220,209**	**-13.6%**	254,797	+10.5%	230,483

Sales

The shrinking market for digital compact cameras and the slowing growth of China's economy led to a major decline in net sales in Imaging System Business Unit. However, due to steady demand for color-model office MFDs and color-model light-production printing systems, benefitting from the boost provided by the acquisition of Axis and the positive effect of favorable currency exchange rates, Canon's consolidated net sales in 2015 totaled ¥3,800,271 million, an increase of 2.0% from the previous year.

Overseas operations are significant to Canon's operating results and generated 81.2% of total net sales in 2015. Such sales are denominated in the applicable local currency 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 ¥121.13 against the U.S. dollar, a year-on-year depreciation of approximately ¥15, and ¥134.20 against the euro, a year-on-year appreciation of approximately ¥6. The effects of foreign exchange rate fluctuations positively affected net sales by approximately ¥146,800 million in 2015. This favorable impact consisted of approximately ¥44,800 million of unfavorable impact for the euro denominated sales and favorable impact of ¥170,500 million for the U.S. dollar denominated sales, and ¥21,100 million for other foreign currency denominated sales.

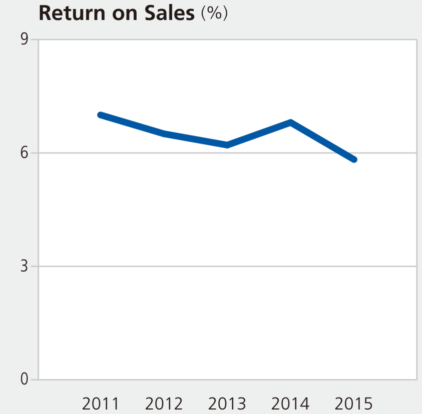
Cost of sales

Cost of sales principally reflects the cost of raw materials, parts and labor used by Canon in the manufacture of its products. A portion of the raw materials used by Canon is imported or includes imported materials. Many of these raw materials are subject to fluctuations in world market prices accompanied by fluctuations in foreign exchange rates that may affect Canon's cost of sales. Other components of cost of sales include depreciation expenses, maintenance expenses, light and fuel expenses, and rent expenses. The ratio of cost of sales to net sales for 2015 and 2014 was 49.1% and 50.1%, respectively.

Gross profit

Canon's gross profit in 2015 increased by 3.9% to ¥1,934,384 million from 2014. The gross profit ratio also increased by 1.0 points year on year to 50.9%. The increase in the gross profit ratio reflects ongoing cost-cutting activities and highly profitable new products.

Return on Sales (%)



Operating expenses
The major components of operating expenses are payroll, R&D, advertising expenses and other marketing expenses. Operating expenses increased 5.4% year on year to ¥1,579,174 million owing to such factors as the increase in foreign-currency-denominated operating expenses after conversion into yen due to the depreciation of the yen, additional operating expenses after the acquisition of Axis and an increase in R&D expenses related to new products.

Operating profit
Operating profit in 2015 decreased 2.3% from 2014 to a total of ¥355,210 million. The ratio of operating profit to net sales decreased 0.5% to 9.3% from 2014.

Other income (deductions)
Other income (deductions) for 2015 decreased ¥27,522 million, mainly due to foreign currency exchange losses.

Income before income taxes
Income before income taxes in 2015 was ¥347,438 million, a decrease of 9.3% from 2014, and constituted 9.1% of net sales.

Income taxes
Provision for income taxes in 2015 decreased by ¥1,895 million from 2014. The effective tax rate for 2015 was 33.4%, which was lower than the statutory tax rate in Japan. This was mainly due to the tax credit for R&D expenses.

Net income attributable to Canon Inc.
As a result, net income attributable to Canon Inc. in 2015 decreased by 13.6% to ¥220,209 million, which represents 5.8% of net sales.

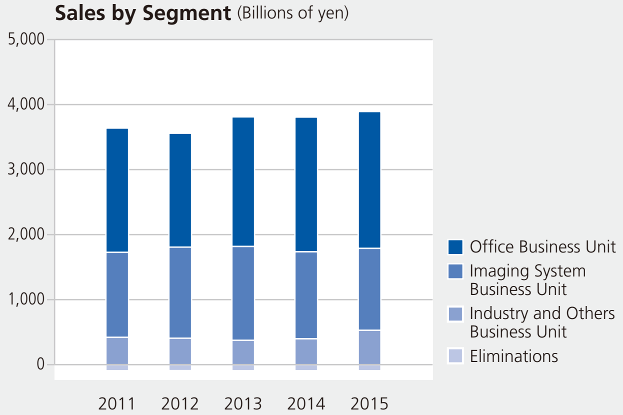
Segment information
Canon divides its businesses into three segments: the Office Business Unit, the Imaging System Business Unit and the Industry and Others Business Unit.

The Office Business Unit mainly includes Office multifunction devices ("MFDs") / Laser multifunction printers ("MFPs") / Laser printers / Digital production printing systems / High speed continuous feed printers / Wide-format printers / Document solutions

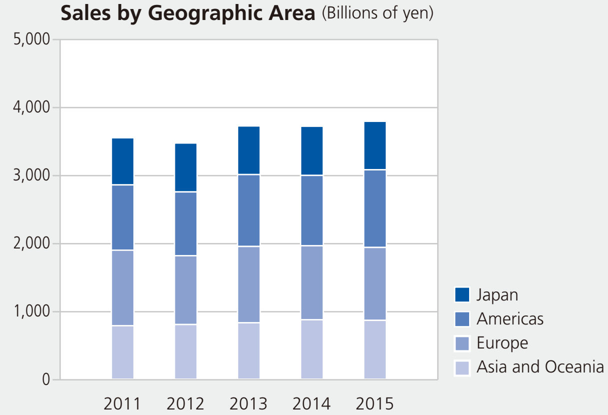
The Imaging System Business Unit mainly includes Interchangeable lens digital cameras / Digital compact cameras / Digital camcorders / Digital cinema cameras / Interchangeable lenses / Compact photo printers / Inkjet printers / Large-format inkjet printers / Commercial photo printers / Image scanners / Multimedia projectors / Broadcast equipment / Calculators

The Industry and Others Business Unit mainly includes Semiconductor lithography equipment / FPD (Flat panel display) lithography equipment / Digital radiography systems / Ophthalmic equipment / Vacuum thin-film deposition equipment / Organic LED ("OLED") panel manufacturing equipment / Die bonders / Micromotors / Network cameras / Handy terminals / Document scanners

Sales by Segment (Billions of yen)



Sales by Geographic Area (Billions of yen)



Sales by segment

SALES BY SEGMENT

	Millions of yen				
	2015	change	2014	change	2013
Office	**¥2,110,816**	**+1.5%**	¥2,078,732	+3.9%	¥2,000,073
Imaging System	**1,263,835**	**-5.9%**	1,343,194	-7.3%	1,448,938
Industry and Others	**524,651**	**+31.6%**	398,765	+6.4%	374,870
Eliminations	**(99,031)**	**—**	(93,439)	—	(92,501)
Total	**¥3,800,271**	**+2.0%**	¥3,727,252	-0.1%	¥3,731,380

Within the Office Business Unit, as for office MFDs, thanks to strong sales of color models led by new small-office/home-office color A3 (12”x18”) imageRUNNER ADVANCE C3300-series models and imagePRESS C800/700-series color digital presses targeting the light production market, unit sales of color models increased compared with the previous year, as did unit sales for the segment overall, including monochrome models, which had been facing decreasing demand. Among high-speed continuous-feed printers, the new Océ-produced VarioPrint i300, Canon’s first high-speed sheet-fed color ink-jet press, gained favorable reviews. As for laser printers, total sales volume decreased due to declining demand in emerging countries. Those factors, coupled with the positive effect of favorable currency exchange rates, resulted in sales for the business unit totaling ¥2,110,816 million, a year-on-year increase of 1.5%, while operating profit totaled ¥290,586 million, a year-on-year decrease of 0.5%.

Within the Imaging System Business Unit, although total sales volume of interchangeable-lens digital cameras declined due to currency depreciations in emerging countries and the slowdown of China’s economy, there were positive signs of a recovery in sales in the U.S. and Japan. Additionally, sales have been strong for such models as the EOS 5DS and EOS 5DS R digital SLR cameras, which deliver the highest resolution of any model in the history of EOS cameras. As for digital compact cameras, while sales volume declined amid the ongoing contraction of the market, the ratio of more profitable high-added-value models increased owing to efforts to strengthen the lineup of PowerShot G-series models. As for inkjet printers, although Canon has been working to expand sales through the Company’s broad product lineup, ranging from home-use printers to MAXIFY-series business models, total sales volume declined due to the significant impact of shrinking markets, mainly in Asia. In contrast, sales of consumable supplies enjoyed solid demand. As a result, sales for the business unit totaled ¥1,263,835 million, a year-on-year decrease of 5.9%, while operating profit totaled ¥183,439 million, declining 5.7% year on year.

In the Industry and Others Business Unit, within the semiconductor lithography equipment segment, unit sales increased owing to strong capital investment in response to growing demand for memory devices used in mobile devices such as smartphones, and in cloud servers, along with increased demand for on-board automotive devices and for communication devices supporting the development of the Internet of Things (“IoT”). Unit sales of FPD lithography equipment also increased, particularly systems used in the fabrication of large-size panels. Consequently, along with the impact of the acquisition of Axis, which was consolidated in the second quarter, sales for the business unit increased 31.6% year on year to ¥524,651 million. As for operating profit, although it improved by ¥8,722 million compared with the previous year, the business unit was in the red by ¥13,079 million due to upfront investment in next-generation technologies and new businesses.

Intersegment sales of ¥99,031 million, representing 2.6% of total sales, are eliminated from total sales for the three segments, and are described as “Eliminations.”

Sales by geographic area

Please refer to the table of sales by geographic area in Note 21 of the Notes to Consolidated Financial Statements.

In Japan, net sales decreased 1.4% from the previous year due mainly to the rush in demand during the first quarter of the previous year that preceded the country’s consumption tax increase.

In the Americas, net sales increased 10.4% from the previous year owing to the positive effects of favorable currency exchange rates along with the consolidation of new businesses.

In Europe, despite the solid demand for office MFDs and laser printers along with the consolidation of new businesses, sales decreased by 1.5% from the previous year due to the negative effect of the appreciation of the yen.

In Asia and Oceania, despite the positive impact of depreciation of the yen, net sales decreased by 1.0% from the previous year owing to the economic stagnation in China and Southeast Asian countries.

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

SALES BY REGION

	Millions of yen				
	2015	change	2014	change	2013
Japan	**¥ 714,280**	**-1.4%**	¥ 724,317	+1.2%	¥ 715,863
Americas	**1,144,422**	**+10.4%**	1,036,500	-2.2%	1,059,501
Europe	**1,074,366**	**-1.5%**	1,090,484	-3.1%	1,124,929
Asia and Oceania	**867,203**	**-1.0%**	875,951	+5.4%	831,087
Total	**¥3,800,271**	**+2.0%**	¥3,727,252	-0.1%	¥3,731,380

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

Operating profit by segment

Please refer to the table of segment information in Note 21 of the Notes to Consolidated Financial Statements.

Operating profit for the Office Business Unit in 2015 decreased by 0.5% to ¥290,586 million, owing to the increase in R&D and other expenses.

Despite operating profit for the Imaging System Business Unit in 2015 decreased by 5.7% from the previous year to ¥183,439 million, in response to the sales decline, operating profit ratio remained at the same level year on year, owing to the improvement in profitability from the sales shift to high-added-value models in camera, along with the positive effects of favorable currency exchange rates.

Operating profit for the Industry and Others Business Unit in 2015, despite an improvement from the previous year resulted from sales increase, recorded a loss of ¥13,079 million due to upfront investment in next-generation technologies and new businesses.

FOREIGN OPERATIONS AND FOREIGN CURRENCY TRANSACTIONS

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

The operating profit on foreign operation sales is usually lower than that from domestic operations because foreign operations consist mainly of marketing activities. Marketing activities are generally less profitable than production activities, which are mainly conducted by the Company and its domestic subsidiaries. Please refer to the table of geographic information in Note 21 of the Notes to Consolidated Financial Statements.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents decreased by ¥210,967 million to ¥633,613 million in fiscal 2015 compared to the previous year primarily due to the acquisition of Axis. 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 decreased by ¥109,203 million to ¥474,724 million in fiscal 2015 compared to the previous year due to the decrease in profit along with the increase in working capital. 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 2015, cash inflow from cash received from customers increased thanks to sales growth. There were no significant changes in Canon's collection rates. Cash outflow for payments for parts and materials decreased due to efforts to reduce inventory level. Cash outflow for payments for selling, general and administrative expenses increased due to the translation effect on operating expenses denominated in foreign currencies that resulted from the depreciation of the yen. The increase also reflects the acquisition of Axis and other companies. Cash outflow for income taxes increased due to an increase in taxable income.

Net cash used in investing activities increased by ¥184,321 million to ¥453,619 million in fiscal 2015. This mainly reflects the acquisition of Axis to enhance Canon's network camera business.

Canon defines "free cash flow" as cash flows from operating activities less cash flows from investing activities. For fiscal 2015, free cash flow decreased by ¥293,524 million to ¥21,105 million as compared with ¥314,629 million for fiscal 2014. Canon's management recognizes that constant and intensive investment in facilities and R&D is required to maintain and strengthen the competitiveness of its products. On March 17, 2016, the Board of Directors of the Company approved an acquisition of Toshiba Medical Systems Corporation ("TMSC") from Toshiba Corporation ("Toshiba") to make TMSC a subsidiary, and concurrently it has entered into a share transfer agreement with Toshiba. The Company paid a total consideration of ¥665.5 billion for a right to acquire all the ordinary shares of TMSC, which is exercisable upon the clearance of necessary competition regulatory authorities. The Company borrowed the consideration through bank borrowing of ¥660 billion provisionally, which is due on September 30, 2016. The Company plans to make its final decision on whether to use own funds, borrowings or a combination of both, to fund the acquisition, by that time. Canon's management seeks to meet its capital requirements with generating cash flow principally from its operating activities. Therefore, its capital resources are primarily sourced from internally generated funds. Accordingly, Canon includes information with regard to free cash flow as management frequently monitors this indicator, and believes that such indicator is beneficial to an investor's understanding. Furthermore, Canon's management believes that this indicator is significant in understanding Canon's current liquidity and the alternatives of use in financing activities because it takes into consideration its operating and investing activities. Canon refers to this indicator together with relevant U.S. GAAP financial measures shown in its consolidated statements of cash flows and consolidated balance sheets for cash availability analysis.

Net cash used in financing activities totaled ¥210,202 million in fiscal 2015, mainly resulting from the dividend payout of ¥174,711 million. The Company paid dividends in fiscal 2015 of ¥160.00 per share.

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

Short-term loans (including the current portion of long-term debt) amounted to ¥688 million at December 31, 2015 compared with ¥1,018 million at December 31, 2014. Long-term debt (excluding the current portion) amounted to ¥881 million at December 31, 2015 compared with ¥1,148 million at December 31, 2014.

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

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

As of March 11, 2016, Canon's debt ratings are: Moody's: Aa1 (long-term); S&P: AA (long-term), A-1+ (short-term); and R&I: AA+ (long-term). Canon does not have any rating downgrade triggers that would accelerate the maturity of a material amount of its debt. A downgrade in Canon's credit ratings or outlook could, however, increase the cost of its borrowings.

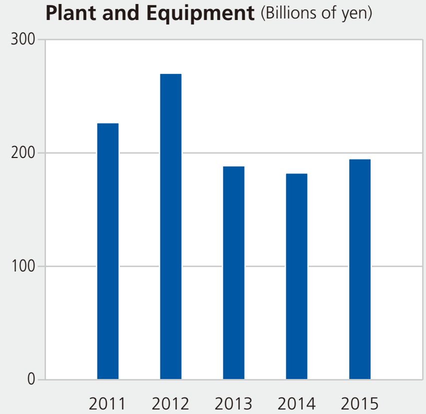
Canon's management policy in recent periods to optimize inventory levels is intended to maintain an appropriate balance among relevant imperatives, including minimizing working capital, avoiding undue exposure to the risk of inventory obsolescence, and maintaining the ability to sustain sales despite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

Reflecting the foregoing circumstances, Canon's total inventory turnover ratios were 47, 50, and 52 days at the end of the fiscal years 2015, 2014, and 2013, respectively and the improvements over the last three years are in line with Canon's expectations and its revised inventory management policy.

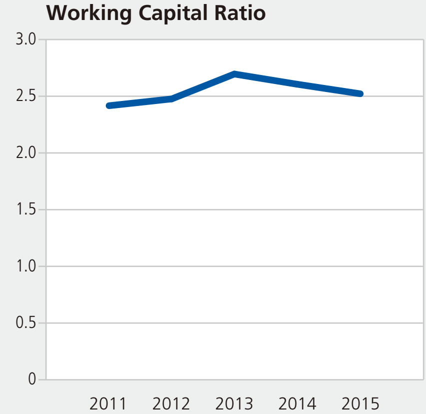
Increase in property, plant and equipment on an accrual basis in 2015 amounted to ¥195,120 million compared with ¥182,343 million in 2014 and ¥188,826 million in 2013. For 2016, Canon projects its increase in property, plant and equipment will be approximately ¥230,000 million.

Employer contributions to Canon's worldwide defined benefit pension plans were ¥19,565 million in 2015, ¥22,146

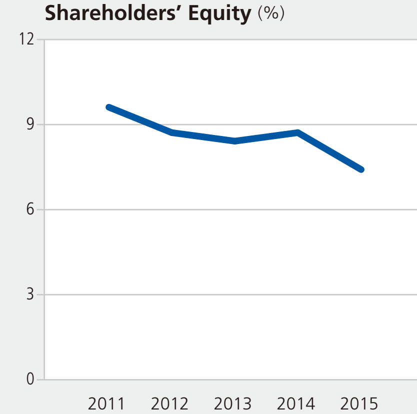
Increase in Property, Plant and Equipment (Billions of yen)



Working Capital Ratio



Return on Canon Inc. Shareholders' Equity (%)



million in 2014 and ¥48,515 million in 2013. Employer contributions to Canon's worldwide defined contribution pension plans were ¥17,277 million in 2015, ¥15,077 million in 2014, and ¥14,383 million in 2013. In addition, employer contributions to the multiemployer pension plan of certain subsidiaries were ¥3,864 million in 2015 and ¥2,815 million in 2014.

Working capital in 2015 decreased by ¥228,704 million to ¥1,241,850 million, compared with ¥1,470,554 million in 2014 and ¥1,437,635 million in 2013. 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 2015 was 2.52 compared to 2.60 for 2014 and to 2.69 for 2013.

Return on assets (net income attributable to Canon Inc. divided by the average of total assets) was 5.0% in 2015, compared to 5.9% in 2014 and 5.6% in 2013.

Return on Canon Inc. shareholders' equity (net income attributable to Canon Inc. divided by the average of total Canon Inc. shareholders' equity) was 7.4% in 2015 compared with 8.7% in 2014 and 8.4% in 2013.

The debt to total assets ratio was 0.0%, 0.0% and 0.1% as of December 31, 2015, 2014 and 2013, respectively. Canon had short-term loans and long-term debt of ¥1,569 million as of December 31, 2015, ¥2,166 million as of December 31, 2014 and ¥2,747 million as of December 31, 2013.

OFF-BALANCE SHEET ARRANGEMENTS

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

Canon provides guarantees for bank loans of its employees, affiliates and other companies. Canon will have to perform under a guarantee if the borrower defaults on a payment within the contract periods of 1 year to 30 years in the case of employees with housing loans, and 1 year to 5 years in the case of affiliates and other companies. The maximum amount of undiscounted payments Canon would have had to make in the event of default by all borrowers was ¥7,685 million at December 31, 2015. The carrying amounts of the liabilities recognized for Canon's obligations as a guarantor under those guarantees at December 31, 2015 were insignificant.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following summarizes Canon's contractual obligations at December 31, 2015.

		Payments due by period			
Millions of yen	**Total**	Less than 1 year	1-3 years	3-5 years	More than 5 years
Contractual obiligations:					
Long-term debt:					
Capital lease obligations	**¥ 1,470**	¥ 630	¥ 705	¥ 135	¥ —
Other long-term debt	**73**	32	28	13	—
Operating lease obligations	**87,592**	26,294	34,183	14,962	12,153
Purchase commitments for:					
Property, plant and equipment	**43,059**	43,059	—	—	—
Parts and raw materials	**75,439**	75,439	—	—	—
Other long-term liabilities:					
Contribution to defined benefit pension plans	**20,721**	20,721	—	—	—
Total	**¥228,354**	¥166,175	¥34,916	¥15,110	¥12,153

Note: The table does not include provisions for uncertain tax positions and related accrued interest and penalties, as the specific timing of future payments related to these obligations cannot be projected with reasonable certainty. See Note 12, Income Taxes in the Notes to Consolidated Financial Statements for further details. Contribution to defined benefit pension plans reflects the expected amount only for the next fiscal year, since contributions beyond the next fiscal year are not currently determinable due to uncertainties related to changes in actuarial assumptions, returns on plan assets and changes to plan membership.

Canon provides warranties of generally less than one year against defects in materials and workmanship on most of its consumer products. Estimated product warranty related costs are established at the time revenue are recognized and are included in selling, general and administrative expenses. Estimates for accrued product warranty costs are primarily based on historical experience, and are affected by ongoing product failure rates, specific product class failures outside of the baseline experience, material usage and service delivery costs incurred in correcting a product failure. As of December 31, 2015, accrued product warranty costs amounted to ¥14,014 million.

At December 31, 2015, commitments outstanding for the purchase of property, plant and equipment were approximately ¥43,059 million, and commitments outstanding for the purchase of parts and raw materials were approximately ¥75,439 million, both for use in the ordinary course of its business. Canon anticipates that funds needed to fulfill these commitments will be generated internally through operations.

During 2016, Canon expects to contribute ¥12,015 million to its Japanese defined benefit pension plans and ¥8,706 million to its foreign defined benefit pension plans.

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

RESEARCH AND DEVELOPMENT, PATENTS AND LICENSES

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

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

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

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

Canon is pursuing collaboration among government, industry and academia. Canon's collaboration effort can be seen in various activities such as fundamental research and development of leading-edge technologies with top universities and research institutes around the world, including Tokyo University, Kyoto University, Tokyo Institute of Technology, Tohoku University, Stanford University, and the University of Arizona, and also participation in the "ImPACT" (Impulsing Paradigm Change through Disruptive Technologies) program led by the Japanese government where Canon's physically-noninvasive and -nondestructive imaging technology is selected as one of the R&D programs. Additionally, Canon is currently working on collaborative research with Massachusetts General Hospital ("MGH") and Brigham and Women's Hospital ("BWH") to develop biomedical optical imaging and medical robotics technologies at the Healthcare Optics Research Laboratory in Cambridge, Massachusetts, founded in 2013.

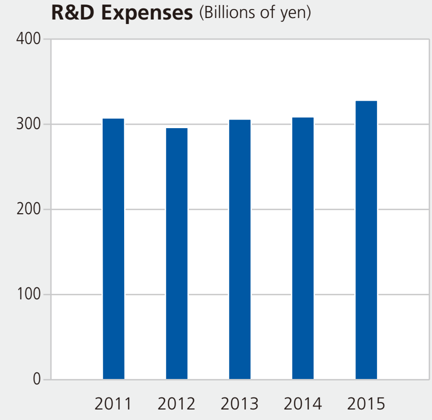
Canon has developed a comprehensive imaging simulation system covering all image formation processes including optics, mechanics, sensor, and image processing, ahead of its competitors. With the simulation system, Canon has succeeded in further reducing the need for prototypes, lowering costs and shortening product development lead times.

Canon's consolidated R&D expenses were ¥328,500 million in 2015, ¥308,979 million in 2014 and ¥306,324 million in 2013. The ratios of R&D expenses to the consolidated total net sales for 2015, 2014 and 2013 were 8.6%, 8.3% and 8.2%, respectively.

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

Canon obtained the third greatest number of private sector patents in 2015, according to the United States patent annual list, released by IFI CLAIMS® Patent Services.

R&D Expenses (Billions of yen)



MARKET RISK EXPOSURES

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

Equity price risk

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

Maturities and fair values of such marketable securities and investments with original maturities of more than three months, all of which were classified as available-for-sale securities, were as follows at December 31, 2015.

	Millions of yen	
Available-for-sale securities	Cost	Fair value
Debt securities		
Due after five years	¥ 304	¥ 488
Fund trusts	63	64
Equity securities	20,461	42,849
	¥20,828	¥43,401

Foreign currency exchange rate and interest rate risk

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

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

The following table provides information about Canon's major derivative financial instruments related to foreign currency exchange transactions existing at December 31, 2015. All of the foreign exchange contracts described in the following table have a contractual maturity date in 2016.

Millions of yen	U.S.$	Euro	Others	Total
Forwards to sell foreign currencies:				
Contract amounts	¥120,227	¥90,865	¥16,961	¥228,053
Estimated fair value	(41)	226	78	263
Forwards to buy foreign currencies:				
Contract amounts	¥ 27,553	¥ 9,623	¥ 364	¥ 37,540
Estimated fair value	318	265	15	598

All of Canon's long-term debt is fixed rate debt. Canon expects that fair value changes and cash flows resulting from reasonable near-term changes in interest rates will be immaterial. Accordingly, Canon believes interest rate risk is insignificant. See also Note 9 of the Notes to Consolidated Financial Statements.

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

The amount of the hedging ineffectiveness was not material for the years ended December 31, 2015, 2014 and 2013. The amounts of net losses excluded from the assessment of hedge effectiveness (time value component) which was recorded in other income (deductions) was ¥131 million, ¥145 million and ¥111 million for the years ended December 31, 2015, 2014 and 2013, respectively.

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

LOOKING FORWARD

As for the future of the global economy, although it is expected to be somewhat better than what it had been over the past five years, the situation remains unstable due to issues such as increased geopolitical risk in the Middle East and the economic slowdown in China. As such, global economic growth is expected to remain modest. From an industrial perspective, however, remarkable developments are being made in technologies in such areas as the IoT and artificial intelligence, which are leading to major changes in industry structure. Advancements in digital technology have made it easier for startup companies to enter markets, thus fueling increased market competition.

In the businesses in which Canon is involved, although demand for color office MFDs and production printers is expected to continue growing, a recovery in sales of products that are largely sold in emerging markets, such as entry-class cameras and single-function laser printers, is expected to take time. Within the market for semiconductor lithography equipment, capital investment is expected to remain strong while forecasts for the FPD lithography equipment market also point to further future expansion. Also expected to grow is the network camera market, a market in which Axis, which became a consolidated subsidiary in 2015, is a major player.

Under these circumstances, the Canon Group embarked on a new five-year plan, Phase V of the "Excellent Global Corporation Plan." During Phase V, under the basic policy of "Embracing the challenge of new growth through a grand strategic transformation," reforms that were promoted in Phase IV will be further expanded upon. In 2020, the final year of Phase V, Canon aims to achieve net sales of 5 trillion yen, an operating profit ratio of 15% or more, a net income ratio of 10% or more, and a shareholders' equity ratio of 70% or more. Toward this objective, Canon will undertake the following various measures.

Establish a new production system to achieve a cost-of-sales ratio of 45%

Strengthen domestic mother factories by further promoting the return of production to Japan and the integration of design, procurement, production engineering, and manufacturing technology operations. At the same time, pursue total cost reductions through the promotion of such advanced production engineering technologies as robotics and automation.

Reinforce and expand new businesses while creating future businesses

Create and expand new businesses by accelerating the horizontal expansion of existing business. Additionally, concentrate management resources and make effective use of M&A to accelerate the expansion of promising business areas such as commercial printing, network cameras and life sciences.

Restructure the global sales network in accordance with market changes
Review existing sales organizations and reinforce omni-channel marketing that integrates online and brick-and-mortar sales routes while strengthening and expanding solutions-driven businesses with the aim of solving issues faced by customers. Additionally, continue focusing energy on developing marketing in emerging countries.

Enhance R&D capabilities through open innovation
Discard the strict notion of self-sufficiency and construct an R&D system that proactively leverages external technologies and knowledge, promoting joint and contract research with various partners such as domestic and foreign universities and research institutes.

Complete the Three Regional Headquarters management system capturing world dynamism
Promote the acquisition of promising businesses through active M&A and complete the Three Regional Headquarter management system, under which Japan, the U.S. and Europe will each roll out businesses globally.

Additionally, under the theme "Taking a decisive first step toward transformation," the following key challenges will be pursued in 2016, the inaugural year of Phase V.

Draft and implement plans to revitalize existing businesses
Raise profitability through drastic cost-cutting and work to revitalize businesses, swiftly launching future products that were exhibited at Canon EXPO 2015.

Rapidly expand new businesses
Work to speed up the expansion and deployment of large-scale businesses such as commercial printing and network cameras.

Accelerate efforts aimed at reducing the cost-of-sales ratio
Continue to investigate optimal locations for production sites and work to accelerate cost reductions at all stages, including product development.

Boost sales productivity through marketing reforms
Accelerate efforts to address global growth in e-commerce and work to reinforce the solutions business.

Improve R&D productivity through selection and concentration
Apply the selection and concentration process to development themes and boost R&D productivity.

Promote the cultivation of global human resources
Build a structure to discover talented individuals from within the entire Canon Group to cultivate global competent human resources capable of performing duties while maintaining an all-encompassing perspective of the world map.

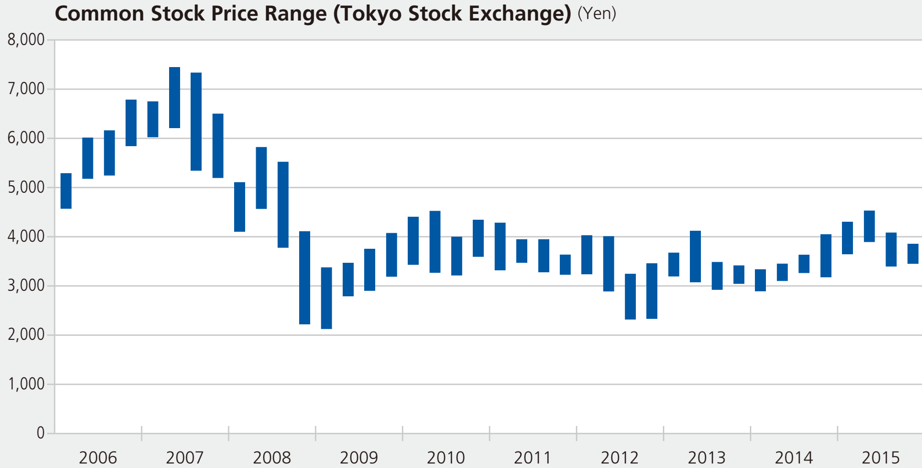
Forward looking statements

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

TEN-YEAR FINANCIAL SUMMARY

	Millions of yen (except per share amounts)			
	2015	2014	2013	2012
Net sales:				
Domestic	**¥ 714,280**	¥ 724,317	¥ 715,863	¥ 720,286
Overseas	**3,085,991**	3,002,935	3,015,517	2,759,502
Total	**3,800,271**	3,727,252	3,731,380	3,479,788
Percentage of previous year	**102.0%**	99.9%	107.2%	97.8%
Net income attributable to Canon Inc.	**220,209**	254,797	230,483	224,564
Percentage of sales	**5.8%**	6.8%	6.2%	6.5%
Advertising	**80,907**	79,765	86,398	83,134
Research and development expenses	**328,500**	308,979	306,324	296,464
Depreciation of property, plant and equipment	**223,759**	213,739	223,158	211,973
Increase in property, plant and equipment	**195,120**	182,343	188,826	270,457
Long-term debt, excluding current installments	**¥ 881**	¥ 1,148	¥ 1,448	¥ 2,117
Canon Inc. shareholders' equity	**2,966,415**	2,978,184	2,910,262	2,598,026
Total assets	**4,427,773**	4,460,618	4,242,710	3,955,503
Per share data:				
Net income attributable to Canon Inc. shareholders per share:				
Basic	**¥ 201.65**	¥ 229.03	¥ 200.78	¥ 191.34
Diluted	**201.65**	229.03	200.78	191.34
Dividend per share	**150.00**	150.00	130.00	130.00
Stock price:				
High	**4,539**	4,045	4,115	4,015
Low	**3,402**	2,889	2,913	2,308
Average number of common shares in thousands	**1,092,018**	1,112,510	1,147,934	1,173,648
Number of employees	**189,571**	191,889	194,151	196,968

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



2011	2010	2009	2008	2007	2006	Thousands of U.S. dollars (except per share amounts) 2015
¥ 694,450	¥ 695,749	¥ 702,344	¥ 868,280	¥ 947,587	¥ 932,290	**$ 5,903,140**
2,862,983	3,011,152	2,506,857	3,225,881	3,533,759	3,224,469	**25,504,058**
3,557,433	3,706,901	3,209,201	4,094,161	4,481,346	4,156,759	**31,407,198**
96.0%	115.5%	78.4%	91.4%	107.8%	110.7%	**102.0%**
248,630	246,603	131,647	309,148	488,332	455,325	**1,819,909**
7.0%	6.7%	4.1%	7.6%	10.9%	11.0%	**5.8%**
81,232	94,794	78,009	112,810	132,429	116,809	**668,653**
307,800	315,817	304,600	374,025	368,261	308,307	**2,714,876**
210,179	232,327	277,399	304,622	309,815	235,804	**1,849,248**
226,869	158,976	216,128	361,988	428,549	379,657	**1,612,562**
¥ 3,368	¥ 4,131	¥ 4,912	¥ 8,423	¥ 8,680	¥ 15,789	**$ 7,281**
2,551,132	2,645,782	2,688,109	2,659,792	2,922,336	2,986,606	**24,515,826**
3,930,727	3,983,820	3,847,557	3,969,934	4,512,625	4,521,915	**36,593,165**
¥ 204.49	¥ 199.71	¥ 106.64	¥ 246.21	¥ 377.59	¥ 341.95	**$ 1.67**
204.48	199.70	106.64	246.20	377.53	341.84	**1.67**
120.00	120.00	110.00	110.00	110.00	83.33	**1.24**
4,280	4,520	4,070	5,820	7,450	6,780	**37.51**
3,220	3,205	2,115	2,215	5,190	4,567	**28.12**
1,215,832	1,234,817	1,234,482	1,255,626	1,293,296	1,331,542	
198,307	197,386	168,879	166,980	131,352	118,499	

Notes: 1. U.S. dollar amounts are translated from yen at the rate of U.S.$1 = JPY121, the approximate exchange rate on the Tokyo Foreign Exchange Market as of December 30, 2015.

2. The Company made a three-for-two stock split on July 1, 2006. The average number of common shares and the per share data for the periods prior to the stock split have been adjusted to reflect the stock split.

CONSOLIDATED BALANCE SHEETS

Canon Inc. and Subsidiaries
December 31, 2015 and 2014

	Millions of yen	
ASSETS	**2015**	2014
Current assets:		
Cash and cash equivalents (Note 1)	**¥ 633,613**	¥ 844,580
Short-term investments (Note 2)	**20,651**	71,863
Trade receivables, net (Note 3)	**588,001**	625,675
Inventories (Note 4)	**501,895**	528,167
Prepaid expenses and other current assets (Notes 6, 12 and 17)	**313,019**	321,648
Total current assets	**2,057,179**	2,391,933
Noncurrent receivables (Note 18)	**29,476**	29,785
Investments (Note 2)	**67,862**	65,176
Property, plant and equipment, net (Notes 5 and 6)	**1,219,652**	1,269,529
Intangible assets, net (Notes 7 and 8)	**241,208**	177,288
Goodwill (Notes 7 and 8)	**478,943**	211,336
Other assets (Notes 6, 11 and 12)	**333,453**	315,571
Total assets	**¥ 4,427,773**	¥ 4,460,618

LIABILITIES AND EQUITY		
Current liabilities:		
Short-term loans and current portion of long-term debt (Note 9)	**¥ 688**	¥ 1,018
Trade payables (Note 10)	**278,255**	310,214
Accrued income taxes (Note 12)	**47,431**	57,212
Accrued expenses (Notes 11 and 18)	**317,653**	345,237
Other current liabilities (Notes 5, 12 and 17)	**171,302**	207,698
Total current liabilities	**815,329**	921,379
Long-term debt, excluding current installments (Note 9)	**881**	1,148
Accrued pension and severance cost (Note 11)	**296,262**	280,928
Other noncurrent liabilities (Notes 7 and 12)	**130,838**	116,405
Total liabilities	**1,243,310**	1,319,860
Commitments and contingent liabilities (Note 18)		
Equity:		
Canon Inc. shareholders' equity:		
Common stock		
Authorized 3,000,000,000 shares; issued 1,333,763,464 shares in 2015 and 2014	**174,762**	174,762
Additional paid-in capital	**401,358**	401,563
Legal reserve (Note 13)	**65,289**	64,599
Retained earnings (Note 13)	**3,365,158**	3,320,392
Accumulated other comprehensive income (loss) (Note 14)	**(29,742)**	28,286
Treasury stock, at cost; 241,690,840 shares in 2015 and 241,931,637 shares in 2014	**(1,010,410)**	(1,011,418)
Total Canon Inc. shareholders' equity	**2,966,415**	2,978,184
Noncontrolling interests	**218,048**	162,574
Total equity	**3,184,463**	3,140,758
Total liabilities and equity	**¥ 4,427,773**	¥ 4,460,618

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME

Canon Inc. and Subsidiaries
Years ended December 31, 2015, 2014 and 2013

	Millions of yen		
	2015	2014	2013
Net sales	**¥3,800,271**	¥3,727,252	¥3,731,380
Cost of sales (Notes 5, 8, 11 and 18)	**1,865,887**	1,865,780	1,932,959
Gross profit	**1,934,384**	1,861,472	1,798,421
Operating expenses (Notes 1, 5, 8, 11, 15 and 18):			
Selling, general and administrative expenses	**1,250,674**	1,189,004	1,154,820
Research and development expenses	**328,500**	308,979	306,324
	1,579,174	1,497,983	1,461,144
Operating profit	**355,210**	363,489	337,277
Other income (deductions):			
Interest and dividend income	**5,501**	7,906	6,579
Interest expense	**(584)**	(500)	(550)
Other, net (Notes 1, 2 and 17)	**(12,689)**	12,344	4,298
	(7,772)	19,750	10,327
Income before income taxes	**347,438**	383,239	347,604
Income taxes (Note 12)	**116,105**	118,000	108,088
Consolidated net income	**231,333**	265,239	239,516
Less: Net income attributable to noncontrolling interests	**11,124**	10,442	9,033
Net income attributable to Canon Inc.	**¥ 220,209**	¥ 254,797	¥ 230,483
	Yen		
Net income attributable to Canon Inc. shareholders per share (Note 16):			
Basic	**¥ 201.65**	¥ 229.03	¥ 200.78
Diluted	**201.65**	229.03	200.78
Cash dividends per share	**150.00**	150.00	130.00

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Canon Inc. and Subsidiaries
Years ended December 31, 2015, 2014 and 2013

	Millions of yen		
	2015	2014	2013
Consolidated net income	**¥231,333**	¥265,239	¥239,516
Other comprehensive income (loss), net of tax (Note 14):			
Foreign currency translation adjustments	**(55,504)**	143,834	251,576
Net unrealized gains and losses on securities	**2,010**	2,524	6,612
Net gains and losses on derivative instruments	**2,785**	(195)	2,056
Pension liability adjustments	**(6,543)**	(37,985)	32,669
	(57,252)	108,178	292,913
Comprehensive income	**174,081**	373,417	532,429
Less: Comprehensive income attributable to noncontrolling interests	**11,973**	9,666	14,688
Comprehensive income attributable to Canon Inc.	**¥162,108**	¥363,751	¥517,741

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF EQUITY

Canon Inc. and Subsidiaries
Years ended December 31, 2015, 2014 and 2013

	Millions of yen								
	Common stock	Additional paid-in capital	Legal reserve	Retained earnings	Accumulated other comprehensive income (loss)	Treasury stock	Total Canon Inc. shareholders' equity	Noncontrolling interests	Total equity
Balance at December 31, 2012	¥174,762	¥401,547	¥61,663	¥3,138,976	¥(367,249)	¥ (811,673)	¥2,598,026	¥156,276	¥ 2,754,302
Equity transactions with noncontrolling interests and other		489		295	(655)		129	(11,182)	(11,053)
Dividends to Canon Inc. shareholders				(155,627)			(155,627)		(155,627)
Dividends to noncontrolling interests								(3,267)	(3,267)
Transfer to legal reserve			1,428	(1,428)			—		—
Comprehensive income:									
Net income				230,483			230,483	9,033	239,516
Other comprehensive income, net of tax (Note 14):									
Foreign currency translation adjustments					249,791		249,791	1,785	251,576
Net unrealized gains and losses on securities					6,097		6,097	515	6,612
Net gains and losses on derivative instruments					2,056		2,056	—	2,056
Pension liability adjustments					29,314		29,314	3,355	32,669
Total comprehensive income							517,741	14,688	532,429
Repurchases and reissuance of treasury stock		(7)		(7)		(49,993)	(50,007)		(50,007)
Balance at December 31, 2013	174,762	402,029	63,091	3,212,692	(80,646)	(861,666)	2,910,262	156,515	3,066,777
Equity transactions with noncontrolling interests and other		(420)		216	(22)		(226)	(658)	(884)
Dividends to Canon Inc. shareholders				(145,790)			(145,790)		(145,790)
Dividends to noncontrolling interests								(2,949)	(2,949)
Transfer to legal reserve			1,508	(1,508)			—		—
Comprehensive income:									
Net income				254,797			254,797	10,442	265,239
Other comprehensive income (loss), net of tax (Note 14):									
Foreign currency translation adjustments					142,813		142,813	1,021	143,834
Net unrealized gains and losses on securities					2,301		2,301	223	2,524
Net gains and losses on derivative instruments					(195)		(195)	—	(195)
Pension liability adjustments					(35,965)		(35,965)	(2,020)	(37,985)
Total comprehensive income							363,751	9,666	373,417
Repurchases and reissuance of treasury stock		(46)		(15)		(149,752)	(149,813)		(149,813)
Balance at December 31, 2014	174,762	401,563	64,599	3,320,392	28,286	(1,011,418)	2,978,184	162,574	3,140,758
Equity transactions with noncontrolling interests and other		**(29)**			**73**		**44**	**(29,627)**	**(29,583)**
Dividends to Canon Inc. shareholders				**(174,711)**			**(174,711)**		**(174,711)**
Dividends to noncontrolling interests								**(3,958)**	**(3,958)**
Acquisition of subsidiaries								**77,086**	**77,086**
Transfer to legal reserve			**690**	**(690)**			**—**		**—**
Comprehensive income:									
Net income				**220,209**			**220,209**	**11,124**	**231,333**
Other comprehensive income (loss), net of tax (Note 14):									
Foreign currency translation adjustments					**(57,592)**		**(57,592)**	**2,088**	**(55,504)**
Net unrealized gains and losses on securities					**1,509**		**1,509**	**501**	**2,010**
Net gains and losses on derivative instruments					**2,785**		**2,785**	**—**	**2,785**
Pension liability adjustments					**(4,803)**		**(4,803)**	**(1,740)**	**(6,543)**
Total comprehensive income							**162,108**	**11,973**	**174,081**
Repurchases and reissuance of treasury stock		**(176)**		**(42)**		**1,008**	**790**		**790**
Balance at December 31, 2015	**¥174,762**	**¥401,358**	**¥65,289**	**¥3,365,158**	**¥ (29,742)**	**¥(1,010,410)**	**¥2,966,415**	**¥218,048**	**¥ 3,184,463**

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Canon Inc. and Subsidiaries
Years ended December 31, 2015, 2014 and 2013

	Millions of yen		
	2015	2014	2013
Cash flows from operating activities:			
Consolidated net income	**¥ 231,333**	¥ 265,239	¥ 239,516
Adjustments to reconcile consolidated net income to net cash provided by operating activities:			
Depreciation and amortization	**273,327**	263,480	275,173
Loss on disposal of fixed assets	**7,975**	12,429	10,638
Equity in (earnings) losses of affiliated companies	**(447)**	(478)	664
Deferred income taxes	**4,672**	8,929	16,791
Decrease in trade receivables	**22,720**	9,323	45,040
Decrease in inventories	**14,249**	59,004	85,577
Decrease in trade payables	**(17,288)**	(24,620)	(108,622)
Increase (decrease) in accrued income taxes	**(8,731)**	3,586	(9,432)
Increase (decrease) in accrued expenses	**(25,529)**	11,124	(15,635)
Increase (decrease) in accrued (prepaid) pension and severance cost	**4,622**	(6,305)	(15,568)
Other, net	**(32,179)**	(17,784)	(16,500)
Net cash provided by operating activities	**474,724**	583,927	507,642
Cash flows from investing activities:			
Purchases of fixed assets (Note 5)	**(252,948)**	(218,362)	(233,175)
Proceeds from sale of fixed assets (Note 5)	**3,824**	3,994	1,763
Purchases of available-for-sale securities	**(98)**	(311)	(5,771)
Proceeds from sale and maturity of available-for-sale securities	**804**	2,606	4,528
(Increase) decrease in time deposits, net	**47,665**	(14,223)	(12,483)
Acquisitions of businesses, net of cash acquired (Note 7)	**(251,534)**	(54,772)	(4,914)
Purchases of other investments	**(1,220)**	—	(296)
Other, net	**(112)**	11,770	136
Net cash used in investing activities	**(453,619)**	(269,298)	(250,212)
Cash flows from financing activities:			
Proceeds from issuance of long-term debt	**717**	1,377	1,483
Repayments of long-term debt	**(1,350)**	(2,152)	(2,334)
Decrease in short-term loans, net	**—**	(54)	(547)
Purchases of noncontrolling interests	**(29,570)**	—	(2,616)
Dividends paid	**(174,711)**	(145,790)	(155,627)
Repurchases and reissuance of treasury stock	**790**	(149,813)	(50,007)
Other, net	**(6,078)**	(4,454)	(12,533)
Net cash used in financing activities	**(210,202)**	(300,886)	(222,181)
Effect of exchange rate changes on cash and cash equivalents	**(21,870)**	41,928	86,982
Net change in cash and cash equivalents	**(210,967)**	55,671	122,231
Cash and cash equivalents at beginning of year	**844,580**	788,909	666,678
Cash and cash equivalents at end of year	**¥ 633,613**	¥ 844,580	¥ 788,909
Supplemental disclosure for cash flow information:			
Cash paid during the year for:			
Interest	**¥ 653**	¥ 462	¥ 500
Income taxes	**117,643**	111,819	108,950

See accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Canon Inc. and Subsidiaries

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

(a) Description of Business

Canon Inc. (the "Company") and subsidiaries (collectively "Canon") is one of the world's leading manufacturers in such fields as office products, imaging system products and industry and other products. Office products consist mainly of office multifunction devices ("MFDs"), laser multifunction printers ("MFPs"), laser printers, digital production printing systems, high speed continuous feed printers, wide-format printers and document solutions. Imaging system products consist mainly of interchangeable lens digital cameras, digital compact cameras, digital camcorders, digital cinema cameras, interchangeable lenses, compact photo printers, inkjet printers, large-format inkjet printers, commercial photo printers, image scanners, multimedia projectors, broadcast equipment and calculators. Industry and other products consist mainly of semiconductor lithography equipment, FPD (Flat panel display) lithography equipment, digital radiography systems, ophthalmic equipment, vacuum thin-film deposition equipment, organic LED ("OLED") panel manufacturing equipment, die bonders, micromotors, network cameras, handy terminals and document scanners. Canon's consolidated net sales for the years ended December 31, 2015, 2014 and 2013 were distributed as follows: the Office Business Unit 55.5%, 55.8% and 53.6%, the Imaging System Business Unit 33.3%, 36.0% and 38.8%, the Industry and Others Business Unit 13.8%, 10.7% and 10.0%, and elimination between segments 2.6%, 2.5% and 2.4%, respectively. These percentages were computed by dividing segment net sales, including intersegment sales, by consolidated net sales, based on the segment operating results described in Note 21.

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. 81.2%, 80.6% and 80.8% of consolidated net sales for the years ended December 31, 2015, 2014 and 2013 were generated outside Japan, with 30.1%, 27.8% and 28.4% in the Americas, 28.3%, 29.3% and 30.1% in Europe, and 22.8%, 23.5% and 22.3% in Asia and Oceania, respectively.

Canon sells laser printers on an OEM basis to HP Inc.; such sales constituted 17.8%, 17.4% and 17.6% of consolidated net sales for the years ended December 31, 2015, 2014 and 2013, respectively, and are included in the Office Business Unit.

Canon's manufacturing operations are conducted primarily at 28 plants in Japan and 18 overseas plants which are located in countries or 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 ("GAAP"). These adjustments were not recorded in the statutory books of account.

(c) Principles of Consolidation

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

(d) Use of Estimates

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

(e) Translation of Foreign Currencies

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

Gains and losses resulting from foreign currency transactions, including foreign exchange contracts, and translation of assets and liabilities denominated in foreign currencies are included in other income (deductions) in the consolidated statements of income. Foreign currency exchange gains and losses were a net loss of ¥22,149 million for the year ended December 31, 2015, a net gain of ¥2,628 million for the year ended December 31, 2014 and a net loss of ¥1,992 million for the year ended December 31, 2013, 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 ¥80,870 million and ¥139,240 million at December 31, 2015 and 2014, respectively, are included in cash and cash equivalents in the consolidated balance sheets.

(g) Investments

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

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

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

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

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

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

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

(h) Allowance for Doubtful Receivables

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

(i) Inventories

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

(j) Impairment of Long-Lived Assets

Long-lived assets, such as property, plant and equipment, and acquired 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 undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of by sale are reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

(k) Property, Plant and Equipment

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

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

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

(l) Goodwill and Other Intangible Assets

Goodwill and other intangible assets with indefinite useful lives are not amortized, but are instead tested for impairment annually in the fourth quarter of each year, or more frequently if indicators of potential impairment exist. Canon performs its impairment test of goodwill using the two-step approach at the reporting unit level, which is one level below the operating segment level. All goodwill is assigned to the reporting unit or units that benefit from the synergies arising from each business combination. If the carrying amount assigned to the reporting unit exceeds the fair value of the reporting unit, Canon performs the second step to measure an impairment charge in the amount by which the carrying amount of a reporting unit's goodwill exceeds its implied fair value.

Intangible assets with finite useful lives consist primarily of software, 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 5 years, trademarks are 15 years, patents and developed technology are from 7 years to 16 years, license fees are 7 years, and customer relationships are from 8 years to 15 years, respectively. Certain costs incurred in connection with developing or obtaining internal-use software are capitalized. These costs consist primarily of payments made to third parties and the salaries of employees working on such software development. Costs incurred in connection with developing internal-use software are capitalized at the application development stage. In addition, Canon develops or obtains certain software to be sold where related costs are capitalized after establishment of technological feasibility.

(m) Environmental Liabilities

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

(n) Income Taxes

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

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

(o) Stock-Based Compensation

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

(p) Net Income Attributable to Canon Inc. 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.

(q) Revenue Recognition

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

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

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

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

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

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

Canon records estimated reductions to sales at the time of sale for sales incentive programs including product discounts, customer promotions and volume-based rebates. Estimated reductions to sales are based upon historical trends and other known factors at the time of sale. Canon regularly adjusts its estimates each period in the ordinary course of establishing sales incentive program accruals based on current information. Canon also provides price protection to certain resellers of its products, and records reductions to sales for the estimated impact of price protection obligations when announced.

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

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

(r) Research and Development Costs

Research and development costs are expensed as incurred.

(s) Advertising Costs

Advertising costs are expensed as incurred. Advertising expenses were ¥80,907 million, ¥79,765 million and ¥86,398 million for the years ended December 31, 2015, 2014 and 2013, respectively.

(t) Shipping and Handling Costs

Shipping and handling costs totaled ¥52,504 million, ¥49,576 million and ¥47,460 million for the years ended December 31, 2015, 2014 and 2013, respectively, and are included in selling, general and administrative expenses in the consolidated statements of income.

(u) Derivative Financial Instruments

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

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

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

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

(v) Guarantees

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

(w) Recently Issued Accounting Guidance

In September 2015, the Financial Accounting Standards Board ("FASB") issued an amendment which requires an acquirer in a business combination to recognize the effect on earnings of any adjustments identified during the measurement period after an acquisition in the same period the adjustment is identified, as opposed to the prior guidance which required material adjustments be retrospectively adjusted. Canon adopted this amended guidance from the quarter beginning October 1, 2015. This adoption did not have a material impact on its consolidated results of operations and financial condition.

In May 2014, the FASB issued a new accounting standard related to revenue from contracts with customers. This standard requires an entity to recognize revenue when promised goods or services are transferred to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This standard was originally planned to be effective for annual reporting periods beginning after December 15, 2016, however, in August 2015, the FASB issued an accounting standard update for a one-year deferral of the effective date. Early adoption as of the original effective date is permitted. This standard may be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this standard recognized at the date of initial application. Canon has not selected a transition method and is currently evaluating the adoption date and the effect that the adoption of this standard will have on its consolidated results of operations and financial condition.

In July 2015, the FASB issued an amendment which requires an entity to measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This guidance is effective for annual reporting periods beginning after December 15, 2016, and early adoption is permitted. Canon is currently evaluating the adoption date and does not expect the adoption of this guidance to have a material impact on its consolidated results of operations and financial condition.

In November 2015, the FASB issued an amendment which requires deferred tax assets and liabilities be classified as noncurrent in the consolidated balance sheets. This guidance is effective for annual reporting periods beginning after December 15, 2016, and early adoption is permitted. Canon will early adopt this amended guidance from the quarter beginning January 1, 2016, on a prospective basis, and prior periods were not retrospectively adjusted. The adoption of this guidance will have an impact on its consolidated balance sheets as our current deferred tax assets were ¥55,108 million and current deferred tax liabilities were ¥2,682 million as of December 31, 2015.

In January 2016, the FASB issued an amendment which addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. This guidance includes the requirement that equity investments be measured at fair value with changes in the fair value recognized in net income. This guidance is effective for annual reporting periods beginning after December 15, 2017, and early adoption is permitted for certain provisions. Canon is currently evaluating the adoption date and the effect that the adoption of this guidance will have on its consolidated results of operations and financial condition.

In February 2016, the FASB issued an amendment which requires lessees to recognize most leases on their balance sheets but recognize expenses on their income statements in a manner similar to current guidance. For lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. This guidance is effective for annual reporting periods beginning after December 15, 2018, and early adoption is permitted. Canon is currently evaluating the adoption date and the effect that the adoption of this guidance will have on its consolidated results of operations and financial condition.

2. INVESTMENTS

The cost, gross unrealized holding gains, gross unrealized holding losses and fair value for available-for-sale securities included in investments by major security type at December 31, 2015 and 2014 were as follows:

December 31 Millions of yen	Cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
2015: Noncurrent:				
Government bonds	**¥ 298**	**¥ —**	**¥ 11**	**¥ 287**
Corporate bonds	**6**	**195**	**—**	**201**
Fund trusts	**63**	**1**	**—**	**64**
Equity securities	**20,461**	**23,482**	**1,094**	**42,849**
	¥20,828	**¥23,678**	**¥1,105**	**¥43,401**

Millions of yen	Cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
2014: Noncurrent:				
Government bonds	¥ 331	¥ —	¥ 6	¥ 325
Corporate bonds	512	153	29	636
Fund trusts	84	—	—	84
Equity securities	20,905	19,765	17	40,653
	¥21,832	¥19,918	¥52	¥41,698

Maturities of available-for-sale debt securities included in investments in the accompanying consolidated balance sheets were as follows at December 31, 2015:

	Millions of yen	
	Cost	Fair value
Due after five years	**¥304**	**¥488**
	¥304	**¥488**

Gross realized gains were ¥329 million, ¥2,540 million and ¥2,360 million for the years ended December 31, 2015, 2014 and 2013, respectively. Gross realized losses, including write-downs for impairments that were other-than-temporary, were ¥31 million, ¥31 million and ¥2 million for the years ended December 31, 2015, 2014 and 2013, respectively.

At December 31, 2015, substantially all of the available-for-sale securities with unrealized losses had been in a continuous unrealized loss position for less than twelve months.

Time deposits with original maturities of more than three months are ¥20,651 million and ¥71,863 million at December 31, 2015 and 2014, respectively, and are included in short-term investments in the accompanying consolidated balance sheets.

Aggregate cost of non-marketable equity securities accounted for under the cost method totaled ¥2,570 million and ¥1,164 million at December 31, 2015 and 2014, respectively. These investments were not evaluated for impairment at December 31, 2015 and 2014, respectively, because (a) Canon did not estimate the fair value of those investments as it was not practicable to estimate the fair value of the investments and (b) Canon did not identify any events or changes in circumstances that might have had significant adverse effects on the fair value of those investments.

Investments in affiliated companies accounted for by the equity method amounted to ¥20,415 million and ¥20,863 million at December 31, 2015 and 2014, respectively. Canon's share of the net earnings (losses) in affiliated companies accounted for by the equity method, included in other income (deductions), were earnings of ¥447 million and ¥478 million for the years ended December 31, 2015 and 2014, respectively, and losses of ¥664 million for the year ended December 31, 2013.

3. TRADE RECEIVABLES

Trade receivables are summarized as follows:

December 31	Millions of yen	
	2015	2014
Notes	**¥ 17,614**	¥ 18,476
Accounts	**582,464**	619,321
	600,078	637,797
Less allowance for doubtful receivables	**(12,077)**	(12,122)
	¥588,001	¥625,675

4. INVENTORIES

Inventories are summarized as follows:

December 31	Millions of yen	
	2015	2014
Finished goods	**¥357,115**	¥363,685
Work in process	**130,258**	144,394
Raw materials	**14,522**	20,088
	¥501,895	¥528,167

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	
	2015	2014
Land	**¥ 282,786**	¥ 286,336
Buildings	**1,632,604**	1,609,667
Machinery and equipment	**1,813,116**	1,822,026
Construction in progress	**61,952**	70,759
	3,790,458	3,788,788
Less accumulated depreciation	**(2,570,806)**	(2,519,259)
	¥ 1,219,652	¥ 1,269,529

Depreciation expenses for the years ended December 31, 2015, 2014 and 2013 were ¥223,759 million, ¥213,739 million and ¥223,158 million, respectively.

Amounts due for purchases of property, plant and equipment were ¥30,789 million and ¥40,483 million at December 31, 2015 and 2014, 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. FINANCE RECEIVABLES AND OPERATING LEASES

Finance receivables represent financing leases which consist of sales-type leases and direct-financing leases resulting from the sales of Canon's and complementary third-party products primarily in foreign countries. These receivables typically have terms ranging from 1 year to 6 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	
	2015	2014
Total minimum lease payments receivable	**¥318,066**	¥308,733
Unguaranteed residual values	**14,271**	13,924
Executory costs	**(888)**	(1,680)
Unearned income	**(31,920)**	(31,919)
	299,529	289,058
Less allowance for credit losses	**(2,878)**	(6,276)
	296,651	282,782
Less current portion	**(109,220)**	(102,920)
	¥187,431	¥179,862

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

Years ended December 31	Millions of yen	
	2015	2014
Balance at beginning of year	**¥ 6,276**	¥ 7,323
Charge-offs	**(1,343)**	(1,171)
Provision	**55**	154
Translation adjustments and other	**(2,110)**	(30)
Balance at end of year	**¥ 2,878**	¥ 6,276

Canon has policies in place to ensure that its products are sold to customers with an appropriate credit history, and continuously monitors its customers' credit quality based on information including length of period in arrears, macroeconomic conditions, initiation of legal proceedings against customers and bankruptcy filings. The allowance for credit losses of finance receivables are evaluated collectively based on historical experience of credit losses. An additional reserve for individual accounts is recorded when Canon becomes aware of a customer's inability to meet its financial obligations, such as in the case of bankruptcy filings. Finance receivables which are past due or individually evaluated for impairment at December 31, 2015 and 2014 are not significant.

The cost of equipment leased to customers under operating leases included in property, plant and equipment, net at December 31, 2015 and 2014 was ¥108,746 million and ¥113,997 million, respectively. Accumulated depreciation on equipment under operating leases at December 31, 2015 and 2014 was ¥82,916 million and ¥87,338 million, respectively.

The following is a schedule by year of the future minimum lease payments to be received under financing leases and noncancelable operating leases at December 31, 2015.

Year ending December 31:	Millions of yen	
	Financing leases	Operating leases
2016	¥127,714	¥ 8,709
2017	90,137	5,307
2018	57,828	3,308
2019	30,501	1,786
2020	11,165	490
Thereafter	721	206
	¥318,066	¥19,806

7. ACQUISITIONS

On April 15, 2015, the Company acquired 76.1% of the issued shares of Axis AB ("Axis"), a Sweden-based company listed on Nasdaq Stockholm, a global leader in the network video solution industry, primarily through a public cash tender offer for consideration of ¥244,725 million. In addition, the Company acquired 9.0% of the issued shares of Axis from noncontrolling shareholders primarily through an additional public cash tender offer. As a result, the Company's aggregate interest represents 85.1% of the issued shares of Axis. The fair value of the 23.9% noncontrolling interest in Axis of ¥77,086 million was measured based on Axis's common stock price on the acquisition date.

The acquisition was accounted for using the acquisition method of accounting. Acquisition-related costs were expensed as incurred and were not material.

The Company views its network surveillance camera business as a promising new business area for Canon. Canon aims to provide advanced and high-performance network solutions to its customers and improve its product competitiveness through the acquisition.

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

	Millions of yen
Current assets	¥ 31,365
Intangible assets	60,992
Goodwill	259,863
Other noncurrent assets	2,053
Non-current assets	322,908
Total assets acquired	354,273
Total liabilities assumed	32,462
Net assets acquired	¥321,811

Intangible assets acquired, which are subject to amortization, consist of trademarks of ¥42,880 million, patents and developed technology of ¥17,823 million and software of ¥289 million. Canon has estimated the amortization period for the trademarks, patents and developed technology, and software to be 15 years, 7 years and 5 years, respectively. The weighted average amortization period for all intangible assets is approximately 13 years.

Goodwill recorded is attributable primarily to expected synergies from combining operations of Axis and Canon. None of the goodwill is expected to be deductible for tax purposes. The goodwill is assigned primarily to the Industry and Others Business Unit for impairment testing.

The amounts of net sales of Axis since the acquisition date included in the Canon's consolidated statement of income for the year ended December 31, 2015 were ¥72,602 million. The amounts of net income of Axis included in the Canon's consolidated statement of income were not material.

Pro forma results of operations were not disclosed because the effect on the Canon's consolidated statement of income was not material.

Canon acquired businesses other than that described above during the year ended December 31, 2015 that were not material to its consolidated financial statements.

During the year ended December 31, 2014, Canon acquired several companies for a total cash consideration of ¥70,671 million, of which ¥30,696 million, ¥8,789 million, and ¥4,633 million was attributed to intangible assets, the related deferred tax liabilities, and other net assets acquired, respectively, and the residual amount of ¥44,131 million was recorded as goodwill. The goodwill recorded is attributable primarily to expected synergies from the combined operations of the acquired companies and Canon. None of the goodwill is expected to be deductible for tax purposes. Total acquisition-related costs were expensed as incurred and were not significant.

Intangible assets acquired, which are subject to amortization, consist of software of ¥13,290 million, customer relationships of ¥1,628 million and other intangible assets of ¥3,841 million. Canon has estimated the weighted average amortization period for the software and customer relationships to be 7 years and 6 years, respectively. The weighted average amortization period for all intangible assets is approximately 9 years. Intangible assets acquired, which are not subject to amortization, consist of in-process research and development of ¥11,937 million.

The results of operations of the acquired companies were included in Canon's consolidated financial statements from the respective acquisition dates and were not material. Pro forma results of operations have not been disclosed because the effects of these acquisitions were not material, individually and in the aggregate.

8. GOODWILL AND OTHER INTANGIBLE ASSETS

Intangible assets subject to amortization acquired during the year ended December 31, 2015, including those recorded from businesses acquired, totaled ¥113,216 million, which primarily consist of trademarks of ¥42,949 million, software of ¥39,817 million, and patents and developed technology of ¥18,083 million. The weighted average amortization periods for intangible assets in total acquired during the year ended December 31, 2015 are approximately 9 years. The weighted average amortization periods for trademarks, software, and patents and developed technology acquired during the year ended December 31, 2015 are approximately 15 years, 5 years and 7 years, respectively.

Intangible assets subject to amortization acquired during the year ended December 31, 2014, including those recorded from businesses acquired, totaled ¥62,189 million, which primarily consist of software of ¥54,686 million. The weighted average amortization periods for intangible assets in total acquired during the year ended December 31, 2014 are approximately 5 years. The weighted average amortization periods for software acquired during the year ended December 31, 2014 are approximately 4 years.

The components of intangible assets subject to amortization at December 31, 2015 and 2014 were as follows:

December 31	**2015**		2014	
Millions of yen	Gross carrying amount	Accumulated amortization	Gross carrying amount	Accumulated amortization
Software	**¥308,348**	**¥181,972**	¥312,069	¥185,885
Trademarks	**49,861**	**2,952**	10,858	6,137
Patents and developed technology	**39,685**	**16,123**	22,371	13,845
Customer relationships	**17,159**	**10,173**	53,494	46,713
License fees	**15,669**	**5,617**	11,765	7,860
Other	**17,070**	**7,690**	16,455	7,351
	¥447,792	**¥224,527**	¥427,012	¥267,791

Aggregate amortization expense for the years ended December 31, 2015, 2014 and 2013 was ¥49,568 million, ¥49,741 million and ¥52,015 million, respectively. Estimated amortization expense for intangible assets currently held for the next five years ending December 31 is ¥48,094 million in 2016, ¥38,852 million in 2017, ¥29,155 million in 2018, ¥20,589 million in 2019, and ¥15,736 million in 2020.

Intangible assets not subject to amortization other than goodwill at December 31, 2015 and 2014 were ¥17,943 million and ¥18,067 million, respectively, which primarily consist of in-process research and development recorded from businesses acquired.

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

The changes in the carrying amount of goodwill by segment for the years ended December 31, 2015 and 2014 were as follows:

Years ended December 31 Millions of yen	Office	Imaging System	Industry and Others	Total
2015: Balance at beginning of year	**¥145,335**	**¥21,780**	**¥ 44,221**	**¥211,336**
Goodwill acquired during the year	**10,373**	**31,367**	**228,827**	**270,567**
Translation adjustments and other	**(13,157)**	**327**	**9,870**	**(2,960)**
Balance at end of year	**¥142,551**	**¥53,474**	**¥282,918**	**¥478,943**

Millions of yen	Office	Imaging System	Industry and Others	Total
2014: Balance at beginning of year	¥139,412	¥13,877	¥ 8,351	¥161,640
Goodwill acquired during the year	3,971	7,424	32,736	44,131
Translation adjustments and other	1,952	479	3,134	5,565
Balance at end of year	¥145,335	¥21,780	¥44,221	¥211,336

9. SHORT-TERM LOANS AND LONG-TERM DEBT

Short-term loans consisting of bank borrowings at December 31, 2015 and 2014 were ¥26 million and ¥3 million, respectively.

Long-term debt consisted of the following:

December 31	Millions of yen	
	2015	2014
Loans, principally from banks, maturing in installments through 2020; bearing weighted average interest of 1.81% and 2.79% at December 31, 2015 and 2014, respectively	**¥ 73**	¥ 145
Capital lease obligations	**1,470**	2,018
	1,543	2,163
Less current portion	**(662)**	(1,015)
	¥ 881	¥ 1,148

The aggregate annual maturities of long-term debt outstanding at December 31, 2015 were as follows:

Year ending December 31:	Millions of yen
2016	¥ 662
2017	452
2018	281
2019	121
2020	27
Thereafter	—
	¥1,543

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

10. TRADE PAYABLES

Trade payables are summarized as follows:

December 31	Millions of yen	
	2015	2014
Notes	**¥ 16,706**	¥ 14,112
Accounts	**261,549**	296,102
	¥278,255	¥310,214

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.

Effective January 1, 2014, defined benefit pension plans of certain subsidiaries in the Netherlands were terminated, and the related plan assets and obligations were transferred to a multiemployer pension plan for the industry in which these subsidiaries operate. As a result, the Company recorded a gain on curtailments and settlements of ¥9,370 million in selling, general and administrative expenses in the consolidated statement of income for the year ended December 31, 2014.

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	Japanese plans		Foreign plans	
	Millions of yen		Millions of yen	
	2015	2014	**2015**	2014
Change in benefit obligations:				
Projected benefit obligations at beginning of year	**¥ 760,331**	¥ 684,842	**¥ 364,662**	¥ 486,572
Service cost	**30,009**	26,445	**7,760**	6,801
Interest cost	**8,008**	10,772	**10,572**	10,654
Plan participants' contributions	**—**	—	**1,830**	1,522
Actuarial (gain) loss	**7,481**	59,496	**(5,534)**	44,580
Benefits paid	**(24,479)**	(21,224)	**(6,795)**	(7,352)
Plan amendments	**—**	—	**(2,655)**	—
Curtailments and settlements	**—**	—	**—**	(191,179)
Foreign currency exchange rate changes	**—**	—	**(20,160)**	13,064
Projected benefit obligations at end of year	**781,350**	760,331	**349,680**	364,662
Change in plan assets:				
Fair value of plan assets at beginning of year	**622,121**	581,996	**221,421**	360,527
Actual return on plan assets	**17,541**	43,714	**21**	17,851
Employer contributions	**8,701**	15,676	**10,864**	6,470
Plan participants' contributions	**—**	—	**1,830**	1,522
Benefits paid	**(21,788)**	(19,265)	**(6,795)**	(7,041)
Settlements	**—**	—	**—**	(165,640)
Foreign currency exchange rate changes	**—**	—	**(9,471)**	7,732
Fair value of plan assets at end of year	**626,575**	622,121	**217,870**	221,421
Funded status at end of year	**¥(154,775)**	¥(138,210)	**¥(131,810)**	¥(143,241)

Amounts recognized in the consolidated balance sheets at December 31, 2015 and 2014 are as follows:

December 31	Japanese plans		Foreign plans	
	Millions of yen		Millions of yen	
	2015	2014	**2015**	2014
Other assets	**¥ 814**	¥ 532	**¥ 9,986**	¥ —
Accrued expenses	**—**	—	**(1,123)**	(1,055)
Accrued pension and severance cost	**(155,589)**	(138,742)	**(140,673)**	(142,186)
	¥(154,775)	¥(138,210)	**¥(131,810)**	¥(143,241)

Amounts recognized in accumulated other comprehensive income (loss) at December 31, 2015 and 2014 before the effect of income taxes are as follows:

December 31	Japanese plans		Foreign plans	
	Millions of yen		Millions of yen	
	2015	2014	**2015**	2014
Actuarial loss	**¥208,946**	¥209,829	**¥71,750**	¥69,287
Prior service credit	**(79,935)**	(92,527)	**(2,567)**	(57)
	¥129,011	¥117,302	**¥69,183**	¥69,230

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

December 31	Japanese plans		Foreign plans	
	Millions of yen		Millions of yen	
	2015	2014	**2015**	2014
Accumulated benefit obligation	**¥740,545**	¥720,034	**¥338,160**	¥343,023

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

December 31	Japanese plans		Foreign plans	
	Millions of yen		Millions of yen	
	2015	2014	**2015**	2014
Plans with projected benefit obligations in excess of plan assets:				
Projected benefit obligations	**¥777,458**	¥756,941	**¥346,749**	¥364,662
Fair value of plan assets	**621,869**	618,199	**204,953**	221,421
Plans with accumulated benefit obligations in excess of plan assets:				
Accumulated benefit obligations	**¥731,537**	¥716,940	**¥331,351**	¥339,305
Fair value of plan assets	**615,963**	618,199	**200,891**	216,560

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, 2015, 2014 and 2013 consisted of the following components:

Years ended December 31	Japanese plans			Foreign plans		
	Millions of yen			Millions of yen		
	2015	2014	2013	**2015**	2014	2013
Service cost	**¥ 30,009**	¥ 26,445	¥ 26,005	**¥ 7,760**	¥ 6,801	¥ 9,448
Interest cost	**8,008**	10,772	11,655	**10,572**	10,654	14,299
Expected return on plan assets	**(19,579)**	(18,018)	(15,273)	**(11,857)**	(10,637)	(13,949)
Amortization of prior service credit	**(12,592)**	(12,800)	(12,306)	**(145)**	(61)	(143)
Amortization of actuarial loss	**10,402**	10,023	13,546	**3,839**	1,698	2,005
(Gain) loss on curtailments and settlements	**—**	—	—	**—**	(9,370)	146
	¥ 16,248	¥ 16,422	¥ 23,627	**¥ 10,169**	¥ (915)	¥ 11,806

Other changes in plan assets and benefit obligations recognized in other comprehensive income (loss) for the years ended December 31, 2015, 2014 and 2013 are summarized as follows:

Years ended December 31	Japanese plans			Foreign plans		
	Millions of yen			Millions of yen		
	2015	2014	2013	**2015**	2014	2013
Current year actuarial (gain) loss	**¥ 9,519**	¥ 33,800	¥(54,150)	**¥ 6,302**	¥ 37,366	¥ 2,290
Current year prior service credit	**—**	—	—	**(2,655)**	—	—
Amortization of actuarial loss	**(10,402)**	(10,023)	(13,546)	**(3,839)**	(1,698)	(2,005)
Amortization of prior service credit	**12,592**	12,800	12,306	**145**	61	143
Curtailments and settlements	**—**	—	—	**—**	(16,725)	(358)
	¥ 11,709	¥ 36,577	¥(55,390)	**¥ (47)**	¥ 19,004	¥ 70

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

	Japanese plans	Foreign plans
	Millions of yen	Millions of yen
Prior service credit	¥(12,785)	¥ (132)
Actuarial loss	10,830	3,213

Assumptions

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

December 31	Japanese plans		Foreign plans	
	2015	2014	**2015**	2014
Discount rate	**1.1%**	1.1%	**3.0%**	2.9%
Assumed rate of increase in future compensation levels	**3.0%**	3.0%	**2.0%**	2.0%

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

Years ended December 31	Japanese plans			Foreign plans		
	2015	2014	2013	**2015**	2014	2013
Discount rate	**1.1%**	1.6%	1.8%	**2.9%**	3.9%	3.6%
Assumed rate of increase in future compensation levels	**3.0%**	3.0%	3.0%	**2.0%**	2.3%	2.2%
Expected long-term rate of return on plan assets	**3.1%**	3.1%	3.1%	**5.6%**	4.9%	5.2%

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 20% is invested in equity securities, approximately 55% is invested in debt securities, and approximately 25% is invested in other investment vehicles, primarily consisting of investments in life insurance company general accounts.

Outside Japan, investment policies vary by country, but the long-term investment objectives and strategies remain consistent. Canon's model portfolio for foreign plans has been developed as follows: approximately 35% is invested in equity securities, approximately 35% is invested in debt securities, and approximately 30% is invested in other investment vehicles, primarily consisting of investments in real estate assets.

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

The three levels of input used to measure fair value are more fully described in Note 20. The fair values of Canon's pension plan assets at December 31, 2015 and 2014, by asset category, are as follows:

December 31, 2015	Millions of yen							
	Japanese plans				Foreign plans			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Equity securities:								
Japanese companies (a)	¥ 49,847	¥ —	¥ —	¥ 49,847	¥ —	¥ —	¥—	¥ —
Foreign companies	3,287	—	—	3,287	18,661	—	—	18,661
Pooled funds (b)	—	125,850	—	125,850	—	66,296	—	66,296
Debt securities:								
Government bonds (c)	142,015	—	—	142,015	48	—	—	48
Municipal bonds	—	1,248	—	1,248	—	2,587	—	2,587
Corporate bonds	—	13,532	—	13,532	—	21,009	—	21,009
Pooled funds (d)	—	120,364	—	120,364	—	34,564	—	34,564
Mortgage backed securities (and other asset backed securities)	—	10,462	—	10,462	—	137	—	137
Life insurance company general accounts	—	125,759	—	125,759	—	6,190	—	6,190
Other assets	—	33,432	779	34,211	—	68,378	—	68,378
	¥195,149	¥430,647	¥779	¥626,575	¥18,709	¥199,161	¥—	¥217,870

December 31, 2014	Millions of yen							
	Japanese plans				Foreign plans			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Equity securities:								
Japanese companies (e)	¥ 51,805	¥ —	¥ —	¥ 51,805	¥ —	¥ —	¥—	¥ —
Foreign companies	10,233	—	—	10,233	31,963	—	—	31,963
Pooled funds (f)	—	124,388	—	124,388	—	74,744	—	74,744
Debt securities:								
Government bonds (g)	143,431	—	—	143,431	7,899	—	—	7,899
Municipal bonds	—	573	—	573	—	3,221	—	3,221
Corporate bonds	—	11,775	—	11,775	—	24,014	—	24,014
Poole d funds (h)	—	118,606	—	118,606	—	23,260	—	23,260
Mortgage backed securities (and other asset backed securities)	—	12,310	—	12,310	—	—	—	—
Life insurance company general accounts	—	123,575	—	123,575	—	7,049	—	7,049
Other assets	—	23,825	1,600	25,425	—	49,271	—	49,271
	¥205,469	¥415,052	¥1,600	¥622,121	¥39,862	¥181,559	¥—	¥221,421

(a) The plan's equity securities include common stock of the Company and certain of its subsidiaries in the amounts of ¥325 million.

(b) These funds invest in listed equity securities consisting of approximately 25% Japanese companies and 75% foreign companies for Japanese plans, and mainly foreign companies for foreign plans.

(c) This class includes approximately 85% Japanese government bonds and 15% foreign government bonds for Japanese plans, and mainly foreign government bonds for foreign plans.

(d) These funds invest in approximately 25% Japanese government bonds, 50% foreign government bonds, 5% Japanese municipal bonds, and 20% corporate bonds for Japanese plans. These funds invest in approximately 75% foreign government bonds and 25% corporate bonds for foreign plans.

(e) The plan's equity securities include common stock of the Company and certain of its subsidiaries in the amounts of ¥197 million.

(f) These funds invest in listed equity securities consisting of approximately 25% Japanese companies and 75% 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, 50% foreign government bonds, 5% Japanese municipal bonds, and 20% corporate bonds for Japanese plans. These funds invest in approximately 85% foreign government bonds and 15% corporate bonds for foreign plans.

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

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

The fair value of Level 3 assets, consisting of hedge funds, was ¥779 million and ¥1,600 million at December 31, 2015 and 2014, respectively. Amounts of actual returns on, and purchases and sales of, these assets during the years ended December 31, 2015 and 2014 were not significant.

Contributions

Canon expects to contribute ¥12,015 million to its Japanese defined benefit pension plans and ¥8,706 million to its foreign defined benefit pension plans for the year ending December 31, 2016.

Estimated future benefit payments

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

Year ending December 31:	Japanese plans	Foreign plans
	Millions of yen	Millions of yen
2016	¥ 20,023	¥ 9,836
2017	21,351	10,165
2018	23,280	9,843
2019	23,359	11,036
2020	27,886	11,686
2021–2025	170,161	67,899

Multiemployer pension plans

The amounts of cost recognized for the multiemployer pension plans primarily in the Netherlands for the years ended December 31, 2015 and 2014 were ¥3,864 million and ¥2,815 million, respectively. The multiemployer pension plan in which the subsidiaries in the Netherlands participated was 102% funded as of December 31, 2014. The collective bargaining agreements have no expiration date. 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, 2015, 2014 and 2013 were ¥17,277 million, ¥15,077 million and ¥14,383 million, respectively.

12. INCOME TAXES

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

Years ended December 31	Millions of yen		
	Japanese	Foreign	Total
2015: Income before income taxes	**¥228,871**	**¥118,567**	**¥347,438**
Income taxes:			
Current	**¥ 80,020**	**¥ 31,413**	**¥111,433**
Deferred	**3,414**	**1,258**	**4,672**
	¥ 83,434	**¥ 32,671**	**¥116,105**

Years ended December 31	Millions of yen		
	Japanese	Foreign	Total
2014: Income before income taxes	¥277,041	¥106,198	¥383,239
Income taxes:			
Current	¥ 83,221	¥ 25,850	¥109,071
Deferred	6,796	2,133	8,929
	¥ 90,017	¥ 27,983	¥118,000
2013: Income before income taxes	¥251,351	¥96,253	¥347,604
Income taxes:			
Current	¥ 75,134	¥16,163	¥ 91,297
Deferred	4,005	12,786	16,791
	¥ 79,139	¥28,949	¥108,088

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 35% for the year ended December 31, 2015 and approximately 38% for the years ended December 31, 2014 and 2013, respectively.

Amendments to the Japanese tax regulations were enacted into law on March 31, 2015. As a result of these amendments, the statutory income tax rate will be reduced from approximately 35% to 33% effective from the year beginning January 1, 2016, and to approximately 32% effective from the year beginning January 1, 2017 thereafter. Consequently, the statutory income tax rate utilized for deferred tax assets and liabilities expected to be settled or realized in the period from January 1, 2016 to December 31, 2016 is approximately 33% and for periods subsequent to December 31, 2016 the rate is approximately 32%. The adjustments of deferred tax assets and liabilities for this change in the tax rate amounted to ¥6,456 million and have been reflected in income taxes in the consolidated statement of income for the year ended December 31, 2015.

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	**2015**	2014	2013
Japanese statutory income tax rate	**35.0%**	38.0%	38.0%
Increase (reduction) in income taxes resulting from:			
Expenses not deductible for tax purposes	**0.8**	0.7	0.9
Income of foreign subsidiaries taxed at lower than Japanese statutory tax rate	**(2.9)**	(3.7)	(3.3)
Tax credit for research and development expenses	**(4.8)**	(5.0)	(5.4)
Change in valuation allowance	**(0.4)**	(0.5)	0.2
Effect of enacted changes in tax laws and rates on Japanese tax	**1.9**	0.8	—
Other	**3.8**	0.5	0.7
Effective income tax rate	**33.4%**	30.8%	31.1%

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

December 31	Millions of yen	
	2015	2014
Prepaid expenses and other current assets	**¥ 55,108**	¥ 61,943
Other assets	**113,687**	117,636
Other current liabilities	**(2,682)**	(3,456)
Other noncurrent liabilities	**(96,243)**	(80,459)
	¥ 69,870	¥ 95,664

The tax effects of temporary differences that give rise to the deferred tax assets and deferred tax liabilities at December 31, 2015 and 2014 are presented below:

December 31	Millions of yen	
	2015	2014
Deferred tax assets:		
Inventories	**¥ 15,298**	¥ 16,085
Accrued business tax	**3,293**	3,951
Accrued pension and severance cost	**77,420**	79,392
Research and development—costs capitalized for tax purposes	**6,906**	8,616
Property, plant and equipment	**24,281**	29,558
Accrued expenses	**39,881**	43,706
Net operating losses carried forward	**33,526**	38,351
Other	**33,808**	34,673
	234,413	254,332
Less valuation allowance	**(32,931)**	(37,498)
Total deferred tax assets	**201,482**	216,834
Deferred tax liabilities:		
Undistributed earnings of foreign subsidiaries	**(10,400)**	(10,368)
Net unrealized gains on securities	**(7,354)**	(6,801)
Tax deductible reserve	**(4,974)**	(5,696)
Financing lease revenue	**(54,280)**	(58,958)
Prepaid pension and severance cost	**(1,104)**	(1,671)
Intangible assets	**(21,106)**	(7,283)
Other	**(32,394)**	(30,393)
Total deferred tax liabilities	**(131,612)**	(121,170)
Net deferred tax assets	**¥ 69,870**	¥ 95,664

The net changes in the total valuation allowance were a decrease of ¥4,567 million for the year ended December 31, 2015, and increases of ¥2,443 million and ¥2,888 million for the years ended December 31, 2014 and 2013, respectively.

Based upon the level of historical taxable income and projections for future taxable income over the periods which the net deductible temporary differences are expected to reverse, management believes it is more likely than not that Canon will realize the benefits of these deferred tax assets, net of the existing valuation allowance, at December 31, 2015.

At December 31, 2015, Canon had net operating losses which can be carried forward for income tax purposes of ¥200,994 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	¥ 6,138
After one year through five years	36,317
After five years through ten years	58,462
After ten years through twenty years	62,270
Indefinite period	37,807
Total	¥200,994

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 ¥28,500 million for a portion of undistributed earnings of foreign subsidiaries that arose for the year ended December 31, 2015 and prior years because Canon currently does not expect to have such amounts distributed or paid as dividends to the Company in the foreseeable future. Deferred tax liabilities will be recognized when Canon expects that it will realize those undistributed earnings in a taxable manner, such as through receipt of dividends or sale of the investments. At December 31, 2015, such undistributed earnings of these subsidiaries were ¥940,931 million.

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

Years ended December 31	Millions of yen		
	2015	2014	2013
Balance at beginning of year	**¥ 6,431**	¥ 6,201	¥ 7,711
Additions for tax positions of the current year	**2,174**	1,649	312
Additions for tax positions of prior years	**165**	216	388
Reductions for tax positions of prior years	**(1,180)**	(114)	(3,141)
Settlements with tax authorities	**(505)**	(1,808)	(347)
Other	**(1,029)**	287	1,278
Balance at end of year	**¥ 6,056**	¥ 6,431	¥ 6,201

The total amounts of unrecognized tax benefits that would reduce the effective tax rate, if recognized, are ¥6,056 million and ¥6,431 million at December 31, 2015 and 2014, respectively.

Although Canon believes its estimates and assumptions of unrecognized tax benefits are reasonable, uncertainty regarding the final determination of tax audit settlements and any related litigation could affect the effective tax rate in a future period. Based on each of the items of which Canon is aware at December 31, 2015, 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, 2015 and 2014, and interest and penalties included in income taxes for the years ended December 31, 2015, 2014 and 2013 are 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 2015. Canon is also no longer subject to a transfer pricing examination by the tax authority for years before 2015. 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 2007 with few exceptions. The tax authorities are currently conducting income tax examinations of Canon's income tax returns for years after 2006 in major foreign tax jurisdictions.

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, 2015, 2014 and 2013 represent dividends paid out during those years and the related appropriations to the legal reserve. Retained earnings at December 31, 2015 did not reflect current year-end dividends in the amount of ¥81,905 million which were approved by the shareholders in March 2016.

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 ¥970,771 million at December 31, 2015.

Retained earnings at December 31, 2015 included Canon's equity in undistributed earnings of affiliated companies accounted for by the equity method in the amount of ¥17,129 million.

14. OTHER COMPREHENSIVE INCOME (LOSS)

Changes in accumulated other comprehensive income (loss) for the years ended December 31, 2015, 2014 and 2013 are as follows:

Millions of yen	Foreign currency translation adjustments	Unrealized gains and losses on securities	Gains and losses on derivative instruments	Pension liability adjustments	Total
Balance at December 31, 2012	¥(247,734)	¥ 4,146	¥(4,462)	¥(119,199)	¥(367,249)
Equity transactions with noncontrolling interests and other	(323)	(1)	(2)	(329)	(655)
Other comprehensive income (loss) before reclassifications	249,791	7,449	(7,551)	27,153	276,842
Amounts reclassified from accumulated other comprehensive income (loss)	—	(1,352)	9,607	2,161	10,416
Net change during the year	249,468	6,096	2,054	28,985	286,603
Balance at December 31, 2013	1,734	10,242	(2,408)	(90,214)	(80,646)
Equity transactions with noncontrolling interests and other	10	3	—	(35)	(22)
Other comprehensive income (loss) before reclassifications	142,813	3,933	(2,204)	(47,840)	96,702
Amounts reclassified from accumulated other comprehensive income (loss)	—	(1,632)	2,009	11,875	12,252
Net change during the year	142,823	2,304	(195)	(36,000)	108,932
Balance at December 31, 2014	**144,557**	**12,546**	**(2,603)**	**(126,214)**	**28,286**
Equity transactions with noncontrolling interests and other	**73**	**—**	**—**	**—**	**73**
Other comprehensive income (loss) before reclassifications	**(57,592)**	**1,691**	**(256)**	**(6,155)**	**(62,312)**
Amounts reclassified from accumulated other comprehensive income (loss)	**—**	**(182)**	**3,041**	**1,352**	**4,211**
Net change during the year	**(57,519)**	**1,509**	**2,785**	**(4,803)**	**(58,028)**
Balance at December 31, 2015	**¥ 87,038**	**¥14,055**	**¥ 182**	**¥(131,017)**	**¥ (29,742)**

Reclassifications out of accumulated other comprehensive income (loss) for the years ended December 31, 2015, 2014 and 2013 are as follows:

Years ended December 31	Amount reclassified from accumulated other comprehensive income (loss)*1			Affected line items in consolidated statements of income
	Millions of yen			
	2015	2014	2013	
Unrealized gains and losses on securities	**¥ (298)**	¥ (2,509)	¥ (2,358)	Other, net
	104	879	613	Income taxes
	(194)	(1,630)	(1,745)	Consolidated net income
	12	(2)	393	Net income attributable to noncontrolling interests
	(182)	(1,632)	(1,352)	Net income attributable to Canon Inc.
Gains and losses on derivative instruments	**4,217**	3,260	15,387	Other, net
	(1,180)	(1,248)	(5,780)	Income taxes
	3,037	2,012	9,607	Consolidated net income
	4	(3)	—	Net income attributable to noncontrolling interests
	3,041	2,009	9,607	Net income attributable to Canon Inc.
Pension liability adjustments	**1,504**	15,585	3,460	See Note 11
	(175)	(3,710)	(1,037)	Income taxes
	1,329	11,875	2,423	Consolidated net income
	23	—	(262)	Net income attributable to noncontrolling interests
	1,352	11,875	2,161	Net income attributable to Canon Inc.
Total amount reclassified, net of tax and noncontrolling interests	**¥4,211**	¥12,252	¥10,416	

*1 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
2015:			
Foreign currency translation adjustments	**¥ (56,054)**	**¥ 550**	**¥ (55,504)**
Net unrealized gains and losses on securities:			
Amount arising during the year	**3,249**	**(1,045)**	**2,204**
Reclassification adjustments for gains and losses realized in net income	**(298)**	**104**	**(194)**
Net change during the year	**2,951**	**(941)**	**2,010**
Net gains and losses on derivative instruments:			
Amount arising during the year	**52**	**(304)**	**(252)**
Reclassification adjustments for gains and losses realized in net income	**4,217**	**(1,180)**	**3,037**
Net change during the year	**4,269**	**(1,484)**	**2,785**
Pension liability adjustments:			
Amount arising during the year	**(13,166)**	**5,294**	**(7,872)**
Reclassification adjustments for gains and losses realized in net income	**1,504**	**(175)**	**1,329**
Net change during the year	**(11,662)**	**5,119**	**(6,543)**
Other comprehensive income (loss)	**¥ (60,496)**	**¥ 3,244**	**¥ (57,252)**
2014:			
Foreign currency translation adjustments	¥144,826	¥ (992)	¥143,834
Net unrealized gains and losses on securities:			
Amount arising during the year	6,379	(2,225)	4,154
Reclassification adjustments for gains and losses realized in net income	(2,509)	879	(1,630)
Net change during the year	3,870	(1,346)	2,524
Net gains and losses on derivative instruments:			
Amount arising during the year	(3,309)	1,102	(2,207)
Reclassification adjustments for gains and losses realized in net income	3,260	(1,248)	2,012
Net change during the year	(49)	(146)	(195)
Pension liability adjustments:			
Amount arising during the year	(71,166)	21,306	(49,860)
Reclassification adjustments for gains and losses realized in net income	15,585	(3,710)	11,875
Net change during the year	(55,581)	17,596	(37,985)
Other comprehensive income (loss)	¥ 93,066	¥ 15,112	¥108,178
2013:			
Foreign currency translation adjustments	¥253,707	¥ (2,131)	¥251,576
Net unrealized gains and losses on securities:			
Amount arising during the year	12,669	(4,312)	8,357
Reclassification adjustments for gains and losses realized in net income	(2,358)	613	(1,745)
Net change during the year	10,311	(3,699)	6,612
Net gains and losses on derivative instruments:			
Amount arising during the year	(12,145)	4,594	(7,551)
Reclassification adjustments for gains and losses realized in net income	15,387	(5,780)	9,607
Net change during the year	3,242	(1,186)	2,056
Pension liability adjustments:			
Amount arising during the year	51,860	(21,614)	30,246
Reclassification adjustments for gains and losses realized in net income	3,460	(1,037)	2,423
Net change during the year	55,320	(22,651)	32,669
Other comprehensive income (loss)	¥322,580	¥ (29,667)	¥292,913

15. STOCK-BASED COMPENSATION

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

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

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

The compensation cost recognized for these stock options for the years ended December 31, 2015 and 2014 was nil and 2013 was ¥95 million, and is included in selling, general and administrative expenses in the consolidated statements of income.

A summary of option activity under the stock option plans as of and for the years ended December 31, 2015, 2014 and 2013 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, 2013	2,726,400	¥4,247	1.6	¥ 37
Exercised	(8,600)	3,287		
Forfeited	(60,400)	4,461		
Outstanding at December 31, 2013	2,657,400	4,245	1.0	28
Exercised	(67,200)	3,287		
Forfeited/Expired	(728,400)	4,869		
Outstanding at December 31, 2014	1,861,800	4,036	0.7	248
Exercised	**(249,600)**	**3,311**		
Forfeited/Expired	**(316,200)**	**3,678**		
Outstanding at December 31, 2015	**1,296,000**	**¥4,263**	**0.4**	**¥ —**
Exercisable at December 31, 2015	**1,296,000**	**¥4,263**	**0.4**	**¥ —**

At December 31, 2015, all outstanding option awards were vested.

The total fair value of shares vested during the years ended December 31, 2015 and 2014 was nil and 2013 was ¥570 million. Cash received from the exercise of stock options for the years ended December 31, 2015, 2014 and 2013 was ¥826 million, ¥221 million and ¥28 million, respectively.

16. 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		
	2015	2014	2013
Net income attributable to Canon Inc.	**¥220,209**	¥254,797	¥230,483

	Number of shares		
Average common shares outstanding	**1,092,017,955**	1,112,509,931	1,147,933,835
Effect of dilutive securities:			
Stock options	**34,931**	4,393	8,466
Diluted common shares outstanding	**1,092,052,886**	1,112,514,324	1,147,942,301

	Yen		
Net income attributable to Canon Inc. shareholders per share:			
Basic	**¥201.65**	¥229.03	¥200.78
Diluted	**201.65**	229.03	200.78

The computation of diluted net income attributable to Canon Inc. shareholders per share for the years ended December 31, 2015, 2014 and 2013 excludes certain outstanding stock options because the effect would be anti-dilutive.

17. DERIVATIVES AND HEDGING ACTIVITIES

Risk management policy

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

Foreign currency exchange rate risk management

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

Cash flow hedge

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

Derivatives not designated as hedges

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

Contract amounts of foreign exchange contracts at December 31, 2015 and 2014 are set forth below:

December 31	Millions of yen	
	2015	2014
To sell foreign currencies	**¥228,053**	¥358,862
To buy foreign currencies	**37,540**	21,365

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, 2015 and 2014.

Derivatives designated as hedging instruments

December 31		Fair value	
		Millions of yen	
	Balance sheet location	**2015**	2014
Assets:			
Foreign exchange contracts	Prepaid expenses and other current assets	**¥373**	¥ 8
Liabilities:			
Foreign exchange contracts	Other current liabilities	**534**	1,597

Derivatives not designated as hedging instruments

December 31		Fair value	
		Millions of yen	
	Balance sheet location	**2015**	2014
Assets:			
Foreign exchange contracts	Prepaid expenses and other current assets	**¥1,112**	¥ 257
Liabilities:			
Foreign exchange contracts	Other current liabilities	**90**	9,570

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, 2015, 2014 and 2013.

Derivatives in cash flow hedging relationships

Years ended December 31	Gain (loss) recognized in OCI (effective portion)	Gain (loss) reclassified from accumulated OCI into income (effective portion)		Gain (loss) recognized in income (ineffective portion and amount excluded from effectiveness testing)	
Millions of yen	Amount	Location	Amount	Location	Amount
2015: Foreign exchange contracts	**¥ 52**	Other, net	**¥ (4,217)**	Other, net	**¥(131)**
2014: Foreign exchange contracts	(3,309)	Other, net	(3,260)	Other, net	(145)
2013: Foreign exchange contracts	(12,145)	Other, net	(15,387)	Other, net	(111)

Derivatives not designated as hedging instruments

Years ended December 31		Gain (loss) recognized in income on derivative		
		Millions of yen		
	Location	**2015**	2014	2013
Foreign exchange contracts	Other, net	**¥1,099**	¥(21,728)	¥(61,787)

18. COMMITMENTS AND CONTINGENT LIABILITIES

Commitments

At December 31, 2015, commitments outstanding for the purchase of property, plant and equipment approximated ¥43,059 million, and commitments outstanding for the purchase of parts and raw materials approximated ¥75,439 million.

Canon occupies sales offices and other facilities under lease arrangements accounted for as operating leases. Deposits made under such arrangements aggregated ¥13,561 million and ¥13,847 million at December 31, 2015 and 2014, respectively, and are included in noncurrent receivables in the accompanying consolidated balance sheets. Rental expenses under such operating lease arrangements amounted to ¥46,483 million, ¥43,215 million and ¥44,562 million for the years ended December 31, 2015, 2014 and 2013, respectively.

Future minimum lease payments required under noncancelable operating leases that have initial or remaining lease terms in excess of one year at December 31, 2015 are as follows:

Year ending December 31:	Millions of yen
2016	¥26,294
2017	20,328
2018	13,855
2019	8,847
2020	6,115
Thereafter	12,153
Total future minimum lease payments	¥87,592

Guarantees

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

For each guarantee provided, Canon would have to perform under a guarantee if the borrower defaults on a payment within the contract periods of 1 year to 30 years, in the case of employees with housing loans, and 1 year to 5 years, in the case of affiliates and other companies. The maximum amount of undiscounted payments Canon would have had to make in the event of default is ¥7,685 million at December 31, 2015. The carrying amounts of the liabilities recognized for Canon's obligations as a guarantor under those guarantees at December 31, 2015 were not significant.

Canon also issues contractual product warranties under which it generally guarantees the performance of products delivered and services rendered for a certain period or term. Changes in accrued product warranty costs for the years ended December 31, 2015 and 2014 are summarized as follows:

Years ended December 31	Millions of yen	
	2015	2014
Balance at beginning of year	**¥ 11,564**	¥ 10,890
Additions	**18,942**	15,699
Utilization	**(12,404)**	(12,039)
Other	**(4,088)**	(2,986)
Balance at end of year	**¥ 14,014**	¥ 11,564

Legal proceedings

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

19. 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, 2015 and 2014 are set forth below. The following summary excludes cash and cash equivalents, trade receivables, finance receivables, noncurrent receivables, short-term loans, trade payables and accrued expenses for which fair values approximate their carrying amounts. The summary also excludes investments and derivative instruments which are disclosed in Note 2 and Note 17, respectively.

December 31	Millions of yen			
	2015		2014	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Long-term debt, including current installments	**¥(1,543)**	**¥(1,507)**	¥(2,163)	¥(2,146)

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 20.

Limitations of fair value estimates

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

Concentrations of credit risk

At December 31, 2015 and 2014, one customer accounted for approximately 15% and 16% of consolidated trade receivables, respectively. Although Canon does not expect that the customer will fail to meet its obligations, Canon is potentially exposed to concentrations of credit risk if the customer failed to perform according to the terms of the contracts.

20. 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, 2015 and 2014.

December 31 Millions of yen	Level 1	Level 2	Level 3	Total
2015: Assets:				
Cash and cash equivalents	¥ —	¥80,870	¥—	¥ 80,870
Available-for-sale (noncurrent):				
Government bonds	287	—	—	287
Corporate bonds	—	201	—	201
Fund trusts	12	52	—	64
Equity securities	42,849	—	—	42,849
Derivatives	—	1,485	—	1,485
Total assets	¥43,148	¥82,608	¥—	¥125,756
Liabilities:				
Derivatives	¥ —	¥ 624	¥—	¥ 624
Total liabilities	¥ —	¥ 624	¥—	¥ 624

Millions of yen	Level 1	Level 2	Level 3	Total
2014: Assets:				
Cash and cash equivalents	¥ —	¥139,240	¥ —	¥139,240
Available-for-sale (noncurrent):				
Government bonds	325	—	—	325
Corporate bonds	—	162	474	636
Fund trusts	12	72	—	84
Equity securities	40,653	—	—	40,653
Derivatives	—	265	—	265
Total assets	¥40,990	¥139,739	¥474	¥181,203
Liabilities:				
Derivatives	¥ —	¥ 11,167	¥ —	¥ 11,167
Total liabilities	¥ —	¥ 11,167	¥ —	¥ 11,167

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

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

The following table presents the changes in Level 3 assets measured on a recurring basis, consisting primarily of corporate bonds, for the years ended December 31, 2015 and 2014.

Years ended December 31	Millions of yen	
	2015	2014
Balance at beginning of year	**¥ 474**	¥340
Total gains or losses (realized or unrealized):		
Included in earnings	**—**	—
Included in other comprehensive income (loss)	**22**	(18)
Purchases, issuances, and settlements	**(496)**	152
Balance at end of year	**¥ —**	¥474

Assets and liabilities measured at fair value on a nonrecurring basis

During the years ended December 31, 2015 and 2014, there were no circumstances that required any significant assets or liabilities to be measured at fair value on a nonrecurring basis.

21. SEGMENT INFORMATION

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

The primary products included in each segment are as follows:

Office Business Unit:

Office multifunction devices (MFDs) / Laser multifunction printers / Laser printers / Digital production printing systems / High speed continuous feed printers / Wide-format printers / Document solutions

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

Industry and Others Business Unit:
Semiconductor lithography equipment / FPD (Flat panel display) lithography equipment / Digital radiography systems / Ophthalmic equipment / Vacuum thin-film deposition equipment / Organic LED (OLED) panel manufacturing equipment / Die bonders / Micromotors / Network cameras / 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 evaluates performance of, and allocates resources to, each segment based on operating profit.

Information about operating results and assets for each segment as of and for the years ended December 31, 2015, 2014 and 2013 is as follows:

Millions of yen	Office	Imaging System	Industry and Others	Corporate and eliminations	Consolidated
2015: Net sales:					
External customers	**¥2,108,246**	**¥1,262,667**	**¥429,358**	**¥ —**	**¥3,800,271**
Intersegment	**2,570**	**1,168**	**95,293**	**(99,031)**	**—**
Total	**2,110,816**	**1,263,835**	**524,651**	**(99,031)**	**3,800,271**
Operating cost and expenses	**1,820,230**	**1,080,396**	**537,730**	**6,705**	**3,445,061**
Operating profit	**¥ 290,586**	**¥ 183,439**	**¥ (13,079)**	**¥ (105,736)**	**¥ 355,210**
Total assets	**¥1,020,758**	**¥ 452,283**	**¥332,252**	**¥2,622,480**	**¥4,427,773**
Depreciation and amortization	**86,206**	**52,070**	**45,064**	**89,987**	**273,327**
Capital expenditures	**73,819**	**38,337**	**24,241**	**106,733**	**243,130**
2014: Net sales:					
External customers	¥2,075,788	¥1,342,501	¥308,963	¥ —	¥3,727,252
Intersegment	2,944	693	89,802	(93,439)	—
Total	2,078,732	1,343,194	398,765	(93,439)	3,727,252
Operating cost and expenses	1,786,675	1,148,593	420,566	7,929	3,363,763
Operating profit	¥ 292,057	¥ 194,601	¥ (21,801)	¥ (101,368)	¥ 363,489
Total assets	¥1,025,499	¥ 517,524	¥342,695	¥2,574,900	¥4,460,618
Depreciation and amortization	87,058	53,912	37,544	84,966	263,480
Capital expenditures	69,704	31,124	15,976	107,956	224,760
2013: Net sales:					
External customers	¥1,993,898	¥1,448,186	¥289,296	¥ —	¥3,731,380
Intersegment	6,175	752	85,574	(92,501)	—
Total	2,000,073	1,448,938	374,870	(92,501)	3,731,380
Operating cost and expenses	1,733,165	1,245,144	400,201	15,593	3,394,103
Operating profit	¥ 266,908	¥ 203,794	¥ (25,331)	¥ (108,094)	¥ 337,277
Total assets	¥ 954,803	¥ 584,856	¥328,202	¥2,374,849	¥4,242,710
Depreciation and amortization	88,344	56,564	37,072	93,193	275,173
Capital expenditures	54,644	44,112	27,040	101,682	227,478

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

Information about product sales to external customers by business unit for the years ended December 31, 2015, 2014 and 2013 is as follows:

Years ended December 31	Millions of yen		
	2015	2014	2013
Office			
Monochrome copiers	**¥ 328,061**	¥ 322,398	¥ 312,973
Color copiers	**421,209**	401,447	381,848
Printers	**857,369**	862,000	841,436
Others	**501,607**	489,943	457,641
Total	**2,108,246**	2,075,788	1,993,898
Imaging System			
Cameras	**782,623**	861,196	973,517
Inkjet printers	**362,663**	366,946	363,070
Others	**117,381**	114,359	111,599
Total	**1,262,667**	1,342,501	1,448,186
Industry and Others			
Lithography equipment	**123,887**	90,395	62,116
Others	**305,471**	218,568	227,180
Total	**429,358**	308,963	289,296
Consolidated	**¥3,800,271**	¥3,727,252	¥3,731,380

Information by major geographic area as of and for the years ended December 31, 2015, 2014 and 2013 is as follows:

	Millions of yen		
	2015	2014	2013
Net sales:			
Japan	**¥ 714,280**	¥ 724,317	¥ 715,863
Americas	**1,144,422**	1,036,500	1,059,501
Europe	**1,074,366**	1,090,484	1,124,929
Asia and Oceania	**867,203**	875,951	831,087
Total	**¥3,800,271**	¥3,727,252	¥3,731,380
Long-lived assets:			
Japan	**¥ 937,716**	¥ 950,719	¥ 984,231
Americas	**150,105**	157,748	131,660
Europe	**183,451**	127,700	111,609
Asia and Oceania	**189,588**	210,650	196,305
Total	**¥1,460,860**	¥1,446,817	¥1,423,805

Net sales are attributed to areas based on the location where the product is shipped to the customers. Other than in Japan and the United States, Canon does not conduct business in any individual country in which its sales in that country exceed 10% of consolidated net sales. Net sales in the United States were ¥1,047,838 million, ¥938,411 million and ¥960,213 million for the years ended December 31, 2015, 2014 and 2013, respectively.

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

The following information is based on the location of the Company and its subsidiaries as of and for the years ended December 31, 2015, 2014 and 2013. In addition to the disclosure requirements under U.S. GAAP, Canon discloses this information in order to provide financial statements users with useful information.

Millions of yen	Japan	Americas	Europe	Asia and Oceania	Corporate and eliminations	Consolidated
2015: Net sales:						
External customers	**¥ 847,669**	**¥1,138,830**	**¥1,077,033**	**¥ 736,739**	**¥ —**	**¥3,800,271**
Intersegment	**1,765,840**	**21,069**	**106,675**	**911,395**	**(2,804,979)**	**—**
Total	**2,613,509**	**1,159,899**	**1,183,708**	**1,648,134**	**(2,804,979)**	**3,800,271**
Operating cost and expenses	**2,285,780**	**1,130,099**	**1,165,218**	**1,582,113**	**(2,718,149)**	**3,445,061**
Operating profit	**¥ 327,729**	**¥ 29,800**	**¥ 18,490**	**¥ 66,021**	**¥ (86,830)**	**¥ 355,210**
Total assets	**¥ 969,805**	**¥ 544,395**	**¥ 409,357**	**¥ 620,090**	**¥ 1,884,126**	**¥4,427,773**
2014: Net sales:						
External customers	¥ 836,801	¥1,033,797	¥1,088,293	¥ 768,361	¥ —	¥3,727,252
Intersegment	1,752,378	8,738	59,493	821,600	(2,642,209)	—
Total	2,589,179	1,042,535	1,147,786	1,589,961	(2,642,209)	3,727,252
Operating cost and expenses	2,245,930	1,018,661	1,135,515	1,522,244	(2,558,587)	3,363,763
Operating profit	¥ 343,249	¥ 23,874	¥ 12,271	¥ 67,717	¥ (83,622)	¥ 363,489
Total assets	¥1,134,484	¥ 531,122	¥ 484,858	¥ 674,672	¥ 1,635,482	¥4,460,618
2013: Net sales:						
External customers	¥ 797,501	¥1,056,096	¥1,124,603	¥ 753,180	¥ —	¥3,731,380
Intersegment	1,855,181	11,774	53,281	881,765	(2,802,001)	—
Total	2,652,682	1,067,870	1,177,884	1,634,945	(2,802,001)	3,731,380
Operating cost and expenses	2,326,351	1,043,487	1,171,357	1,574,125	(2,721,217)	3,394,103
Operating profit	¥ 326,331	¥ 24,383	¥ 6,527	¥ 60,820	¥ (80,784)	¥ 337,277
Total assets	¥1,152,398	¥ 447,039	¥ 496,549	¥ 631,827	¥ 1,514,897	¥4,242,710

22. SUBSEQUENT EVENT

On March 17, 2016, the Board of Directors of the Company approved an acquisition of Toshiba Medical Systems Corporation ("TMSC") from Toshiba Corporation ("Toshiba") to make TMSC a subsidiary, and concurrently it has entered into a share transfer agreement with Toshiba. The Company paid a total consideration of ¥665.5 billion for a right to acquire all the ordinary shares of TMSC, which is exercisable upon the clearance of necessary competition regulatory authorities. The Company borrowed the consideration through bank borrowing of ¥660 billion provisionally, which is due on September 30, 2016. The Company plans to make its final decision on whether to use own funds, borrowings or a combination of both, to fund the acquisition, by that time.

Until the clearance of necessary competition regulatory authorities is obtained, the Company does not expect to consolidate TMSC since it does not currently hold power over TMSC including voting rights in the shareholders meeting of TMSC.

Under Phase V of its Excellent Global Corporation Plan, a five-year initiative launched in 2016, the Company aims to embrace the challenge of new growth through a grand strategic transformation. With regard to reinforcing and expanding new businesses in particular, which represents one of the important strategies to be carried out during this phase, the Company intends to cultivate its health care business within the safety and security sector as a next-generation pillar of growth.

TMSC is one of the leading global companies in the medical equipment industry. Within the field of medical X-ray computed tomography (CT) systems in particular, TMSC is the overwhelming market share leader in Japan and has been steadily increasing its global market share. Through the agreement, TMSC, with its world-class technological capabilities and global platform, will be welcomed into the Canon Group. By maximizing the combination of both companies' management resources, the Company aims to solidify its business foundation for health care that can contribute to the world.

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
2015: Allowance for doubtful receivables					
Trade receivables	**¥12,122**	**¥2,180**	**¥(1,745)**	**¥ (480)**	**¥12,077**
Finance receivables	**6,276**	**55**	**(1,343)**	**(2,110)**	**2,878**
2014: Allowance for doubtful receivables					
Trade receivables	¥12,730	¥ 878	¥(2,236)	¥ 750	¥12,122
Finance receivables	7,323	154	(1,171)	(30)	6,276
2013: Allowance for doubtful receivables					
Trade receivables	¥12,970	¥1,235	¥(4,173)	¥ 2,698	¥12,730
Finance receivables	6,908	212	(1,278)	1,481	7,323

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

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

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

Canon's management assessed the effectiveness of internal control over financial reporting as of December 31, 2015. In making this assessment, management used the criteria established in internal Control –Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the "COSO criteria").

Based on its assessment, management concluded that, as of December 31, 2015, Canon's internal control over financial reporting was effective based on the COSO criteria.

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

Fujio Mitarai
Chairman & CEO

Toshizo Tanaka
Executive Vice President & CFO

March 30, 2016

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

EY
Building a better working world

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The Board of Directors and Shareholders of
Canon Inc.

We have audited the accompanying consolidated balance sheets of Canon Inc. and subsidiaries as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2015. Our audits also included the schedule of valuation and qualifying accounts (the "schedule"). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Canon Inc. and subsidiaries at December 31, 2015 and 2014, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2015, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Canon Inc. and subsidiaries' internal control over financial reporting as of December 31, 2015, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 30, 2016 expressed an unqualified opinion thereon.

Ernst & Young ShinNihon LLC

March 30, 2016

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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The Board of Directors and Shareholders of
Canon Inc.

We have audited Canon Inc. and subsidiaries' internal control over financial reporting as of December 31, 2015, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). Canon Inc. and subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, Canon Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2015, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Canon Inc. and subsidiaries as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2015, and our report dated March 30, 2016 expressed an unqualified opinion thereon.

Ernst & Young ShinNihon LLC

March 30, 2016

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.
2-1, Yaesu 1-chome, Chuo-ku, Tokyo 103-8670, Japan

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

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

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 30, 2016, in Tokyo

Further Information:

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

MAJOR CONSOLIDATED SUBSIDIARIES

(As of December 31, 2015)

Manufacturing

Canon Precision Inc.
Fukushima Canon Inc.
Canon Chemicals Inc.
Canon Components, Inc.
Canon Electronics Inc.
Canon Finetech Inc.
Nisca Corporation
Canon Tokki Corporation
Canon ANELVA Corporation
Nagahama Canon Inc.
Canon Machinery Inc.
Oita Canon Materials Inc.
Oita Canon Inc.
Nagasaki Canon Inc.
Canon Virginia, Inc.
Canon Bretagne S.A.S.
Axis Communications AB
Océ-Technologies B.V.
Océ Printing Systems G.m.b.H.
Canon Dalian Business Machines, Inc.
Canon (Suzhou) Inc.
Canon Zhongshan Business Machines Co., Ltd.
Canon Zhuhai, Inc.
Canon Inc., Taiwan
Canon Vietnam Co., Ltd.
Canon Hi-Tech (Thailand) Ltd.
Canon Prachinburi (Thailand) Ltd.
Canon Business Machines (Philippines), Inc.
Canon Opto (Malaysia) Sdn. Bhd.

Research & Development

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

Marketing & Other

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

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