

Sumitomo Heavy Industries, Ltd.

SECOND QUARTER CONSOLIDATED FINANCIAL REPORT

For the Six-Month Period from April 1 to September 30, 2018

All financial information has been prepared in accordance with generally accepted accounting principles in Japan. This document has been translated from the Japanese original as a guide to non-Japanese investors and contains forward-looking statements that are based on management's estimates, assumptions, and projections at the time of publication. A number of factors could cause actual results to differ materially from expectations. Amounts shown in this financial statement have been rounded to the nearest million yen.

Summary of Consolidated Financial Results
For the Second Quarter Ended September 30, 2018
 Presented October 31, 2018

Sumitomo Heavy Industries, Ltd.

Listed exchanges	Tokyo Stock Exchange
Stock code	6302
Head office	Tokyo
President	Shunsuke Betsukawa
URL	www.shi.co.jp
Inquiries	Michiko Watanabe General Manager, Corporate Communications Dept.
Telephone	+81 3 6737 2331
Scheduled reporting date for quarterly report	November 8, 2018
Scheduled date of payment of cash dividends	December 3, 2018
Availability of supplementary explanations for quarterly financial statement	Yes
Holding of meeting to explain quarterly financial statement	Yes (for analysts)

1. FY 2018 Second Quarter Consolidated Results (April 1, 2018, to September 30, 2018)

(1) Business Results

(Units: millions of yen)

	Second Quarter April 1 to September 30, 2018		Previous Second Quarter April 1 to September 30, 2017	
		% change		% change
Net sales	423,661	19.2	355,319	11.8
Operating income	34,086	17.6	28,982	55.6
Ordinary income	33,050	14.3	28,925	58.6
Net income attributed to shareholders of the parent company	21,362	8.1	19,769	50.9
Net income per share (yen)	174.34		161.31	
Fully diluted net income per share (yen)	—		—	

Note: Comprehensive income

Fiscal quarter ended September 30, 2018: 14,818 million yen, (26.9%)

Fiscal quarter ended September 30, 2017: 20,271 million yen, —%

(Note) The Company carried out a 5-to-1 reverse stock split for its common shares with an effective date of October 1, 2017. The quarterly net income per share was calculated, under the assumption that such share consolidation was conducted at the beginning of the previous consolidated fiscal year.

(2) Financial Position

(Units: millions of yen)

	End of Second Quarter As of September 30, 2018	End of Previous Full Year As of March 31, 2018
Total assets	929,630	894,835
Total net assets	453,628	444,964
Equity ratio (%)	47.2	48.2

Reference: Equity

Fiscal quarter ended September 30, 2018: 438,712 million yen

Fiscal year ended March 31, 2018: 431,008 million yen

2. Dividends

(Units: yen)

	Year Ended March 31, 2018	Year Ending March 31, 2019	Year Ending March 31, 2019 (forecast)
Annual dividends per share			
First quarter	—	—	
Second quarter	8.00	50.00	
Third quarter	—		—
End of term	45.00		50.00
Annual dividends	—		100.00

Note 1: Changes from the most recent dividend forecast: Yes

Note 2: Because the Company carried out a 5-to-1 reverse stock split for its common shares with an effective date of October 1, 2017, the actual amount of second quarter-end dividend for the period ended March 2018 as calculated on a pre-consolidation basis is presented. The second quarter-end dividend and the total annual dividend for the period ended March 2018, taking into consideration of the share consolidation, are 40 yen and 85 yen, respectively.

3. FY 2018 Consolidated Forecasts (April 1, 2018, to March 31, 2019)

(Units: millions of yen)

	Full Year April 1, 2018, to March 31, 2019	
		% change
Net sales	890,000	12.5
Operating income	70,000	0.1
Ordinary income	67,500	0.1
Net income attributed to shareholders of the parent company	41,000	18.3
Projected net income per share (yen)	334.61	

Note 1: Changes from the most recent consolidated forecast: Yes

Additional Notes

- (1) Transfers of important subsidiaries during the fiscal period (moves of specific subsidiaries due to change in scope of consolidation): None
- Newly consolidated: None
- Excluded from consolidation: None
- (2) Special accounting measures applied in the quarterly consolidated financial report: Applicable
- (3) Changes to accounting policies, changes to accounting estimates, and restatements
- (i) Changes to accounting policies resulting from revisions to accounting standards, etc.: None
- (ii) Changes other than (i): Applicable
- (iii) Changes to accounting estimates: None
- (iv) Restatements: None
- (4) Number of shares issued (common shares)
- (i) Number of shares issued at end of fiscal period (including treasury stock):
- | | |
|--------------------------|--------------------|
| As of September 30, 2018 | 122,905,481 shares |
| As of March 31, 2018 | 122,905,481 shares |
- (ii) Amount of treasury stock at end of fiscal period
- | | |
|--------------------------|----------------|
| As of September 30, 2018 | 376,303 shares |
| As of March 31, 2018 | 367,080 shares |
- (iii) Average number of shares during fiscal period (cumulative quarterly period)
- | | |
|--------------------------|--------------------|
| As of September 30, 2018 | 122,533,932 shares |
| As of September 30, 2017 | 122,553,337 shares |
- (Note) The Company carried out a 5-to-1 reverse stock split for its common shares with an effective date of October 1, 2017. The average number of shares during the fiscal period was calculated, under the assumption that such share consolidation was conducted at the beginning of the previous consolidated fiscal year.

* The Quarterly Summary of Financial Results is not subject to the Quarterly Review

* Explanations and Other Special Items regarding the Pertinent Reasons for the Earnings Forecast

Earnings forecasts and outlooks concerning future financial results are believed to be reasonable based on information available at the time of publication. Actual financial results may vary from the above forecast and outlook because of a variety of factors. For information on the assumptions that form the basis of the earnings forecast and items to note concerning the use of earnings forecasts, please see the *Explanation of the Consolidated Earnings Forecast and Other Forward-Looking Estimates* in the *Supplementary Materials* on page 9.

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1. Qualitative Information regarding Current Quarterly Consolidated Business Performance

(1) Explanation of Business Performance

As for the business environment surrounding the Group during the second quarter of the current consolidated fiscal year under review, capital investments trended positively as a result of improvement in corporate performance in Japan, and turning to overseas markets, the recovery of the US manufacturing industry continued due to the recovery of domestic and overseas demand and the industrial production in China continued to show stable growth. Due mainly to these factors, demand for machinery was on an upward trend globally. On the other hand, the global economy is still lacking clarity in its future direction mainly due to continued concerns over trade disputes, ongoing geopolitical risks in the Korean Peninsula and other places, and the occurrence of foreign exchange and financial markets in some emerging economies.

In this business environment, the Group started the Medium-Term Management Plan 2019, proactively pursue investments to drive growth through M&A, capital spending, etc., working to further improve the operational quality, actively promoting CSR measures and moving forward with other key initiatives.

Under these conditions, orders increased across all segments of the Group with the exception of the Others segment. On a consolidated basis, the Group posted an order figure of JPY461.4 billion, a 20% increase as compared to the same period last year (hereinafter referred to as the “previous term”). Sales also increased across all segments with the exception of the Others segment. In total, the Group posted a sales figure of JPY423.7 billion, a 19% increase as compared to the previous term.

Turning to income, the drop in profits from the Machinery Components, Ships and other segments was offset by increases from the Construction Machinery, Environmental Facilities & Plants and other segments. As a result, operating income was JPY34.1 billion, an 18% increase as compared to the previous term, and ordinary income was JPY33.1 billion, a 14% increase as compared to the previous term. Quarterly net income attributable to the shareholders of the parent company also increased by 8% as compared to the previous term to finish at JPY21.4 billion.

Conditions in each business segment of the Group were as follows:

1. Machinery Components

The market for small-to-medium scale gear reducers showed positivity, along with the market for precision gear reducers for use in robots in Europe and China, and the Lafert Group (including Lafert S.p.A.) was made a consolidated subsidiary of the Company. As a result, orders and sales increased as compared to the previous term. In actual figures, the segment received orders worth JPY68.3 billion, a rise of 22% as compared to the previous term, and posted sales of JPY62.4 billion, a rise of 22% as compared to the previous term. Further, the segment posted operating income of JPY4.5 billion.

2. Precision Machinery

With respect to plastics machinery, demand from the electric and electronic sector in China continued to be strong and with respect to other product areas, there was an increase in demand for cryogenic coolers for medical uses. Due to these and other factors, orders and sales increased as compared to the previous term. In actual figures, the segment received orders worth JPY98.1 billion, a rise of 13% as compared to the previous term, and posted sales of JPY87.0 billion, a rise of 13% as compared to the previous term. Further, the segment posted operating income of JPY7.7 billion.

3. Construction Machinery

With regard to the hydraulic excavator business, both orders and sales increased as compared to the previous term due to a rise in demand from the China and other overseas markets. As for the mobile crane business, both orders and sales increased as compared to the previous term mainly due to continued signs of recovery in the North American market and strong demand from the domestic market. In actual figures, the segment received orders worth JPY152.4 billion, a rise of 24% as compared to the previous term, and posted sales of JPY144.2 billion, a rise of 15% as compared to the previous term. Further, the segment posted operating income of JPY13.1 billion.

4. Industrial Machinery

Orders increased as compared to the previous term as the drop in orders for industrial turbines compared with the previous term was offset by increases mainly from the material handling business where demand from steel manufacturers was strong. On the other hand, sales increased as compared to the previous term due to growth in the industrial machinery business driven mainly by an increase in sales of forging presses for which there is a substantial backlog of orders, although sales of industrial turbines dropped as with the case of orders. In actual figures, the segment received orders worth JPY43.2 billion, a rise of 8% as compared to the previous term, and posted sales of JPY41.6 billion, a rise of 8% as compared to the previous term. Further, the segment posted operating income of JPY3.0 billion.

5. Ships

The slowdown in market conditions continued in the Ships segment which meant that no orders for new vessels were secured during the current quarter under review, equaling the total from the previous term, although the Company was requested to repair a ship. On the other hand, two vessels were delivered during the current quarter under review as compared to three vessels handed over in the previous term. In actual figures, the segment received orders worth JPY12.1 billion, a rise of 53% as compared to the previous term, and posted sales of JPY19.0 billion, a rise of 4% as compared to the previous term. Further, the segment posted operating income of JPY1.1 billion.

6. Environmental Facilities & Plants

Orders and sales in the energy plant business increased as compared to the previous term due to the subsidiarization of Sumitomo SHI FW Energie B.V. although orders for biomass-fueled power generation plants decreased from the previous term. On the other hand, in the water treatment plant business, orders increased as compared to the previous term, but sales dropped as compared to the previous term. In actual figures, the segment received orders worth JPY83.6 billion, a rise of 21% as compared to the previous term, and posted sales of JPY66.0 billion, a rise of 61% as compared to the previous term. Further, the segment posted an operating income of JPY3.6 billion.

7. Other

The Other segment received orders worth JPY3.7 billion, a fall of 4% as compared to the previous term, and posted sales of JPY3.4 billion, a fall of 11% as compared to the previous term. Further, the segment posted operating income of JPY1.2 billion.

(2) Explanation of the Group's Consolidated Financial Position

1. Condition of Assets, Liabilities, and Net Assets

Total assets at the end of the second quarter of the current consolidated fiscal year under review (ended September 30, 2018) amounted to JPY929.6 billion, an increase of JPY34.8 billion as compared to the end of the previous consolidated fiscal year. This was mainly due to increases of JPY21.2 billion in inventory assets and JPY15.3 billion in intangible assets offsetting a decrease of JPY15.6 billion in trade notes and accounts receivable.

Total liabilities rose to JPY476.0 billion, an increase of JPY26.1 billion as compared to the end of the previous consolidated fiscal year. This was mainly due to increases of JPY8.4 billion in notes and accounts payable and offsetting the increase of JPY3.7 billion in the balance of interest-bearing liabilities.

Net assets to JPY453.6 billion, an increase of JPY8.7 billion as compared to the end of the previous consolidated fiscal year. This was mainly due to increase of JPY15.9 billion in retained earnings.

As a result of the above, the shareholders' equity ratio fell by 0.9 points from the end of the previous consolidated fiscal year to finish at 47.2%.

2. Cash Flow Condition

The increase in cash flow from operating activities was JPY51.8 billion (as compared to an increase in cash flow of JPY45.0 billion in the previous term). When broken down, the main components of the proceeds were JPY32.8 billion in quarterly net income before tax and other adjustments, and the JPY27.8 billion reduction in trade receivables. The main sources of the outflow of cash were the JPY20.3 billion increase in inventory assets and the JPY8.5 billion payment of corporate and other taxes.

The decrease in cash flow as a result of investing activities was JPY34.7 billion (as compared to a decrease in cash flow of JPY25.2 billion in the previous term). The main reason for the cash outflow was the JPY20.6 billion used to acquire the shares of, and money invested in, a subsidiary, which results in a change in the scope of consolidation.

The decrease in cash flow as a result of financing activities was JPY7.9 billion (as compared to a decrease in cash flow of JPY18.7 billion in the previous term). The main reasons are the JPY5.5 billion used to pay dividends.

As a result of the foregoing, the balance of cash and cash equivalents at the end of the second quarter of the current consolidated fiscal year under review totaled JPY93.1 billion, an increase of JPY32.0 billion as compared to the end of the previous consolidated fiscal year.

(3) Explanation of the Consolidated Earnings Forecast and Other Forward-Looking Estimates

The consolidated earnings forecast for the fiscal year ending March 2019 that was announced in the Summary of Consolidated Financial Results dated May 8, 2018 has been revised as follows.

(Fiscal year ending March 2019; full year)

	Net sales (millions of yen)	Operating income (millions of yen)	Ordinary income (millions of yen)	Net income attributed to shareholders of the parent company (millions of yen)	Net income per share (yen)
Previous forecast (A)	850,000	64,000	61,800	38,000	310.11
Revised forecast (B)	890,000	70,000	67,500	41,000	334.61
Difference (B-A)	40,000	6,000	5,700	3,000	—
% Change	4.7	9.4	9.2	7.9	—
(Reference) Results for previous fiscal year	791,025	69,921	67,466	34,660	282.83

Due to the consolidation of the newly acquired motor business in addition to strong performance in the hydraulic excavator business where demand from overseas is growing, the Company has decided to revise up the consolidated earnings forecast for the fiscal year ending March 2019 that was announced on May 8, 2018 with regard to net sales, operating income, ordinary income and net income attributed to shareholders of the parent company.

Please note that from the third quarter of the current consolidated fiscal year, the main exchange rates are assumed to be USD1 = JPY110 and EUR1 = JPY125.

2. Quarterly Consolidated Financial Statements and Key Explanatory Notes

(1) Quarterly Consolidated Balance Sheets

(Units: millions of yen)

	End of Previous Fiscal Year As of March 31, 2018	End of Second Quarter As of September 30, 2018
	Amount	Amount
Assets		
Cash and deposits	88,233	95,396
Notes and accounts receivable	269,409	253,802
Inventory assets	167,400	188,568
Other	30,597	31,826
Allowance for doubtful accounts	(4,055)	(3,782)
Current assets	551,584	565,811
Land	107,826	107,557
Other (net)	131,770	136,591
Total tangible assets	239,596	244,148
Goodwill	18,030	33,442
Other	32,319	32,253
Total intangible assets	50,349	65,695
Other	58,830	59,287
Allowance for doubtful accounts	(5,524)	(5,312)
Investments and other assets	53,306	53,975
Fixed assets	343,251	363,818
Total assets	894,835	929,630

(Units: millions of yen)

	End of Previous Fiscal Year As of March 31, 2018	End of Second Quarter As of September 30, 2018
	Amount	Amount
Liabilities		
Notes and accounts payable	184,227	192,603
Short-term bank loans	33,516	34,081
Long-term loans due within one year	7,801	2,908
Allowance for guaranteed construction	13,478	14,412
Other allowance amount	5,679	5,098
Other	102,984	117,537
Current liabilities	347,684	366,638
Bonds	20,000	20,000
Long-term debt due after one year	2,864	10,927
Allowance	155	154
Defined benefit liability	40,466	40,741
Deferred income taxes on revaluation	20,730	20,713
Other	17,972	16,827
Total fixed liabilities	102,187	109,364
Total liabilities	449,871	476,001
Net assets		
Common stock	30,872	30,872
Capital surplus	25,267	25,267
Retained earnings	314,296	330,161
Treasury stock	(1,000)	(1,035)
Total shareholders' equity	369,434	385,265
Unrealized gains on securities	5,406	5,258
Profit (loss) on deferred hedge	925	(420)
Revaluation reserve for land	40,831	40,813
Foreign currency translation adjustments	17,565	10,754
Re-measurement of defined benefit plans	(3,153)	(2,958)
Total accumulated other comprehensive income	61,574	53,447
Non-controlling interest	13,956	14,916
Total net assets	444,964	453,628
Total liabilities and net assets	894,835	929,630

(2) Consolidated Income Statements and Consolidated Statement of Comprehensive Income
Consolidated Income Statements

(Units: millions of yen)

	Previous Second Quarter April 1, 2017, to September 30, 2017	Present Second Quarter April 1, 2018, to September 30, 2018
	Amount	Amount
Net sales	355,319	423,661
Cost of sales	268,015	323,170
Gross income	87,304	100,491
Selling, general & administrative expenses	58,322	66,406
Operating income	28,982	34,086
Non-operating income		
Interest income	245	336
Dividend income	590	517
Other	1,639	1,540
Total non-operating income	2,474	2,393
Non-operating expenses		
Interest expense	517	528
Loss on foreign currency exchange	319	1,094
Other	1,695	1,806
Total non-operating expenses	2,532	3,428
Ordinary income	28,925	33,050
Extraordinary losses		
Loss on impaired assets	114	201
Total extraordinary losses	114	201
Income before income taxes	28,811	32,849
Corporate income taxes	8,002	9,501
Net income	20,809	23,348
Net income (or loss) attributable to non-controlling interests	1,040	1,986
Net income attributed to shareholders of the parent company	19,769	21,362

Consolidated Statement of Comprehensive Income

(Units: millions of yen)

	Previous Second Quarter April 1, 2017, to September 30, 2017	Present Second Quarter April 1, 2018, to September 30, 2018
	Amount	Amount
Net income	20,809	23,348
Other comprehensive income		
Unrealized gains on securities	1,259	(150)
Profit (loss) on deferred hedge	(117)	(1,343)
Revaluation reserve for land	7	—
Foreign currency translation adjustments	(2,508)	(7,233)
Adjustment to retirement benefits	821	189
Amount applied for equity method accounting of affiliates	1	7
Total other comprehensive income	(538)	(8,530)
Comprehensive income	20,271	14,818
(Breakdown)		
Comprehensive income relating to parent company shareholdings	18,350	13,253
Quarterly comprehensive income relating to non-controlling interests	1,920	1,565

(3) Notes regarding Consolidated Quarterly Financial Statements

(Notes on Premise of a Going Concern)

There are no applicable items.

(Notes regarding Significant Fluctuations to Shareholders' Equity)

There are no applicable items.

(Application of Accounting Procedures Specific to Preparation of Quarterly Consolidated Financial Statements)

(Calculation of tax expenses)

The effective tax rate expected to be imposed on pretax net income (after tax effect accounting) applicable to the consolidated fiscal year in which the second quarter of the current consolidated fiscal year under review is included was estimated based on reasonable assumptions, and tax expenses were calculated by multiplying the quarterly pretax net income by the estimated effective tax rate.

(Change in Accounting Policy)

(Change in calculation method for tax expenses)

Previously, tax expenses of the Company and its consolidated subsidiaries were calculated based on a method that was applied as a general rule. To further streamline operations for quarterly settlement of accounts for the Company and its consolidated subsidiaries, however, starting from the first quarter of the current consolidated fiscal year under review, the calculation method for the tax expenses has been changed so that the effective tax rate expected to be imposed on pretax net income (after tax effect accounting) applicable to the consolidated fiscal year is estimated based on reasonable assumptions, and tax expenses are calculated by multiplying the quarterly pretax net income by the estimated effective tax rate.

Note that because this change only has a minimal impact, the Company has decided not to make a retrospective application.

(Additional Information)

The Company has applied the "Partial Amendment to the 'Accounting Standard on Tax Effect Accounting'" (Corporate Accounting Standard No. 28; February 16, 2018), etc. from the first quarter of the current consolidated fiscal year under review. As a result, deferred tax assets are presented in the investments and other assets section and deferred tax liabilities are presented in the fixed liabilities section.

(Subsequent Events of Significant Importance)

There are no applicable items.

3. Supplementary Information

(1) Orders, Sales and Operating Income, and Balance of Orders by Segment

Orders

(Units: millions of yen)

Segment	April 1, 2017, to September 30, 2017	April 1, 2018, to September 30, 2018	Y/Y Change	
	Amount	Amount	Amount	%
Machinery Components	56,128	68,254	12,126	21.6
Precision Machinery	86,472	98,107	11,635	13.5
Construction Machinery	122,424	152,406	29,982	24.5
Industrial Machinery	40,155	43,231	3,077	7.7
Ships	7,928	12,132	4,204	53.0
Environmental Facilities & Plants	68,847	83,591	14,744	21.4
Other	3,828	3,686	(142)	(3.7)
Total	385,781	461,406	75,624	19.6

Sales and Operating Income

(Units: millions of yen)

Segment	April 1, 2017, to September 30, 2017		April 1, 2018, to September 30, 2018		Y/Y Change	
	Sales	Operating Income	Sales	Operating Income	Sales	Operating Income
Machinery Components	51,246	5,272	62,409	4,457	11,163	(815)
Precision Machinery	76,815	7,768	87,014	7,665	10,200	(103)
Construction Machinery	125,620	8,280	144,234	13,091	18,614	4,811
Industrial Machinery	38,498	2,986	41,604	2,999	3,106	13
Ships	18,250	2,024	18,987	1,061	736	(964)
Environmental Facilities & Plants	41,034	1,590	65,987	3,625	24,953	2,035
Other	3,856	1,059	3,426	1,194	(430)	135
Adjustments	—	3	—	(7)	—	(10)
Total	355,319	28,982	423,661	34,086	68,342	5,104

Balance of Orders Received

(Units: millions of yen)

Segment	End of Previous Fiscal Year As of March 31, 2018	End of Second Quarter As of September 30, 2017	Change	
	Amount	Amount	Amount	%
Machinery Components	36,783	42,627	5,845	15.9
Precision Machinery	77,456	88,548	11,092	14.3
Construction Machinery	58,053	66,225	8,172	14.1
Industrial Machinery	98,937	100,564	1,627	1.6
Ships	49,790	42,935	(6,855)	(13.8)
Environmental Facilities & Plants	231,172	248,775	17,603	7.6
Other	1,484	1,744	260	17.5
Total	553,675	591,420	37,745	6.8

The Group's operating segments are categorized as follows:

Businesses	Main Products
Machinery Components	Power transmission and control equipment
Precision Machinery	Plastics machinery, film forming machines, semiconductor production equipment, laser processing systems, cryogenic equipment, precision positioning equipment, precision forgings, control components, defense equipment, machining tools
Construction Machinery	Hydraulic excavators, mobile cranes, road machinery
Industrial Machinery	Ion accelerators, medical machines and equipment, forging press machines, material handling systems, logistics systems, automated parking systems, turbines, pumps
Ships	Ships
Environmental Facilities & Plants	Private power generation facilities, boilers, industrial waste treatment facilities, air pollution control equipment, water and sewage treatment systems, process equipment, pressure vessels, mixing vessels, air-conditioning equipment, food processing machinery

(2) (Summary) Consolidated Cash Flows Statement

(Units: millions of yen)

	Previous Second Quarter April 1, 2017, to September 30, 2017	Present Second Quarter April 1, 2018, to September 30, 2018	Y/Y Change
Income before income taxes	28,811	32,849	4,039
Depreciation	10,696	12,557	1,861
(Increase) decrease in notes and accounts receivable	25,740	27,812	2,072
(Increase) decrease in inventories	(11,549)	(20,306)	(8,757)
Increase (decrease) in notes and accounts payable	1,176	7,129	5,952
Payments for income taxes	(9,428)	(8,489)	940
Other	(398)	212	610
Net cash provided by operating activities	45,047	51,764	6,717
Payments for purchases of property, plant, and equipment	(12,859)	(14,445)	(1,586)
Other	(12,309)	(20,246)	(7,937)
Net cash used in investing activities	(25,168)	(34,691)	(9,523)
Net increase (decrease) in short-term loans	(11,364)	(633)	10,730
Cash dividends paid	(5,509)	(5,511)	(3)
Other	(1,800)	(1,716)	83
Net cash used in financing activities	(18,672)	(7,861)	10,811
Other	(1,124)	(1,632)	(509)
Cash and cash equivalents at beginning of period	61,017	85,503	24,486
Cash and cash equivalents at end of period	61,101	93,083	31,982