\Orchestrating a brighter world NEC

Integrated Report 2020 (Financials)

Year ended March 31, 2020

Contents

Note: NEC has changed its reporting segments from the fiscal year ended March 31, 2020.
Although Public Solutions Business and Public Infrastructure Business have been consolidated into the Public Business as reportable segments until Q3 of the fiscal year ended March31, 2020, NEC has split each business unit into separate reportable segments at the year end.

Management's Discussion and Analysis

Year Ended March 31, 2020 (Fiscal 2020)
Compared With the Year Ended March 31, 2019 (Fiscal 2019)

This section contains forward-looking statements concerning the NEC Group's analysis of financial condition, business results and cash flows. These statements are based on the judgment of the NEC Group as of March 31, 2020. The preparation of financial statements 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 financial statements and the reported amount of revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimated.

1. Business Overview and Key Business Drivers

The NEC Group implemented a variety of innovative changes that included a "Reform of profit structure," an "Achievement of growth" and a "Restructuring of execution capabilities" as outlined in the "Mid-term Management Plan 2020" announced in January 2018.

In the following sections, NEC reports the business results in six main segments: Public Solutions, Public Infrastructure, Enterprise, Network Services, System Platform, and Global. In fiscal 2020, Public Solutions generated 10.5% of net sales, Public Infrastructure 20.4%, Enterprise 14.7%, Network Services 16.5%, System Platform 17.7%, and Global 16.0%. (The ratios of segment sales to total revenue were calculated based on segment revenue to external customers.)

Segment information is included in "Notes to Consolidated Financial Statements - Note 6. Segment Information".

2. Analysis of Fiscal 2020 Business Results

The worldwide economy during the fiscal year ended March 31, 2020 slowed down due to factors such as the US-China trade conflict and the effects of the novel coronavirus.

As for the Japanese economy, in addition to the slowdown of economies throughout the world and the increase in Japan's consumption tax rate, the impact of the novel coronavirus infectious disease resulted in sluggish performance.

Under these business conditions, the NEC Group implemented a variety of innovative changes that included a "Reform of profit structure," an "Achievement of growth" and a "Restructuring of execution capabilities" as outlined in the "Mid-term Management Plan 2020" announced in January 2018.

In terms of the "Reform of profit structure," as part of securing the investment necessary to return to a growth trajectory, NEC further promoted structural reforms, such as responding to problematic businesses in order to improve profitability. Specifically, in January 2020, NEC sold all common stock of Nippon Avionics Co., Ltd., and in March 2020, agreed to transfer a majority of the shares of NEC Display Solutions, Ltd., a subsidiary responsible for the video solution business, to Sharp Corporation. In the wireless solutions business, NEC implemented measures to improve profitability, such as promoting profitability-focused businesses and collaborating with Ceragon Networks Ltd. to reduce development costs.

As for the "Achievement of growth," NEC worked to create social value by promoting businesses that make use of digital technologies, such as biometrics and artificial intelligence (AI). In particular, in July 2019, NEC announced that it will collaborate with Star Alliance, the world's largest airline alliance, on the development of a personal identification platform that uses biometric technology in order to realize seamless boarding procedures for passengers. Furthermore, in August 2019, NEC participated in Lawson, Inc.'s demonstration experiment of a late night labor saving store with the provision of a store entrance management system using a face recognition AI engine and related technologies and services. Moreover, in September 2019, NEC carried out trials of a next-generation ATM system that supports face recognition identity verification and QR code settlement with Seven Bank, Ltd. This ATM was also used for trials of a system for opening bank accounts with face authentication for the first time in Japan.

In addition, NEC is beginning shipments of base station equipment and wireless slave stations to NTT DOCOMO, INC. and Rakuten Mobile, Inc. for the construction of networks for 5th generation mobile communications systems (5G), as well as full scale entry into the "local 5G" business, which provides 5G only to limited locations. This is in addition to the launch of activities for proposing total solutions, from network infrastructure to applications, to companies and local governments.

Regarding the "Restructuring of execution capabilities," NEC worked to create value for customers utilizing the latest technologies and to implement reforms that enable employees to maximize their strengths. In terms of creating value for customers utilizing the latest technologies, NEC announced its full-scale entry into the drug discovery business that specializes in advanced immunotherapy for cancer and other diseases as a part of strengthening the healthcare business. In addition to starting clinical trials of individualized neoantigen vaccines, NEC also worked on activities to put infant fingerprint authentication into practical use, which enables services that include birth certification, registration and the tracking of vaccination records for newborns in developing countries. As part of implementing reforms that enable employees to maximize their strengths, NEC deployed a performance management system for group companies that fairly evaluates employees in terms of both achievements and actions and rewards their contributions. At the same time, NEC introduced "NEC Growth Careers" as a mechanism for employees to cultivate their own careers and motivate them to grow, by internally disclosing the work history of employees and the recruitment positions of each organization to assist with job matching. In addition, NEC promoted institutional reforms and environment improvements to accelerate work style changes, such as the establishment of "BASE," a working space that promotes collaboration between organizations and enables more creative work styles, the introduction of "Super Flex" schedules without a core working time, the promotion of telework through telework week and company-wide telework day.

Condensed Consolidated Income Statements

	Billions of Yen		*YoY Change*
	2019	2020	2020/2019
Revenue	¥2,913.4	¥3,095.2	+6.2%
Operating profit	57.8	127.6	+120.9%
Income before income taxes	77.3	124.0	+60.4%
Net profit (loss) attributable to owners of the parent	39.7	100.0	+152.0%

The NEC Group recorded consolidated revenue of 3,095.2 billion JPY for the fiscal year ended March 31, 2020, an increase of 181.8 billion JPY (6.2%) year-on-year. This increase was due to increased sales in all reportable segments.

Regarding profitability, operating profit (loss) improved by 69.8 billion JPY year-on-year, to an operating profit of 127.6 billion JPY. This was mainly due to increased revenue, in addition to business structure improvement expenses recorded in the previous fiscal year. Adjusted operating profit (loss) improved by 75.9 billion JPY year-on-year, to an adjusted operating profit of 145.8 billion JPY.

Income (loss) before income taxes was an income of 124.0 billion JPY, a year-on-year improvement of 46.7 billion JPY, mainly due to improved operating profit (loss), despite the effect of gains from the sale of affiliated company shares that was recorded in the previous fiscal year.

Net profit (loss) attributable to owners of the parent for the fiscal year ended March 31, 2020 was a profit of 100.0 billion JPY, an improvement of 60.3 billion JPY year-on-year, primarily due to improved income (loss) before income taxes. Adjusted net profit (loss) attributable to owners of the parent improved by 64.2 billion JPY year-on-year, to a profit of 111.2 billion JPY.

(1) Public Solutions Business

Revenue:	324.6 billion yen	(+13.4 %)
Adjusted operating profit (loss):	18.6 billion yen	(+11.4 billion yen)

In the Public Solutions business, revenue was 324.6 billion JPY, an increase of 38.5 billion JPY (+13.4%) year-on-year, mainly due to increased sales in sectors that include public and healthcare.

Adjusted operating profit (loss) improved by 11.4 billion JPY year-on-year, to a profit of 18.6 billion JPY, mainly owing to increased sales and improved profitability.

(2) Public Infrastructure Business

Revenue	631.1billion yen	(+1.5 %)
Adjusted operating profit (loss):	53.9 billion yen	(+8.5 billion yen)

In the Public Infrastructure business, revenue was 631.1 billion JPY, an increase of 9.3 billion JPY (+1.5%) year-on-year, mainly due to increased sales in sectors that include aerospace and defense.

Adjusted operating profit (loss) improved by 8.5 billion JPY year-on-year, to a profit of 53.9 billion JPY, mainly owing to increased sales and improved profitability.

(3) Enterprise Business

Revenue	455.5 billion yen	(+5.5 %)
Adjusted operating profit (loss):	37.2 billion yen	(+1.3 billion yen)

In the Enterprise business, revenue was 455.5 billion JPY, an increase of 23.7 billion JPY (+5.5%) year-on-year, mainly due to increased sales for the finance sector.

Adjusted operating profit (loss) improved by 1.3 billion JPY year-on-year, to a profit of 37.2 billion JPY, mainly owing to increased sales.

(4) Network Services Business

Revenue	509.8 billion yen	(+10.8 %)
Adjusted operating profit (loss):	38.2 billion yen	(+17.5 billion yen)

In the Network Services business, revenue was 509.8 billion JPY, an increase of 49.5 billion JPY (+10.8%) year-on-year, mainly due to increased sales in the fixed network domain and an one-time large-scale project.

Adjusted operating profit (loss) improved by 17.5 billion JPY year-on-year, to a profit of 38.2 billion JPY, mainly owing to increased sales.

(5) System Platform Business

Revenue	548.7 billion yen	(+9.7 %)
Adjusted operating profit (loss):	48.9 billion yen	(+28.8 billion yen)

In the System Platform business, revenue was 548.7 billion JPY, an increase of 48.5 billion JPY (+9.7%) year-on-year, mainly due to increased sales in hardware, primarily business PCs.

Adjusted operating profit (loss) improved by 28.8 billion JPY year-on-year, to a profit of 48.9 billion JPY, mainly owing to the effect of restructuring as well as increased sales.

(6) Global Business

Revenue	493.8 billion yen	(+20.6 %)
Adjusted operating profit (loss):	-3.8 billion yen	(+18.8 billion yen)

In the Global business, revenue was 493.8 billion JPY, an increase of 84.4 billion JPY (+20.6%) year-on-year, mainly due to increased sales in the Safer City and submarine systems domains.

Adjusted operating profit (loss) improved by 18.8 billion JPY year-on-year, to a loss of 3.8 billion JPY, mainly owing to increased profitability in the Safer City, service provider, wireless backhaul and submarine systems domains.

(7) Others

Revenue	131.7 billion yen	(-35.4 %)
Adjusted operating profit (loss):	9.4 billion yen	(-9.6 billion yen)

In Others, revenue was 131.7 billion JPY, a decrease of 72.0 billion JPY (-35.4%) year-on-year.

Adjusted operating profit (loss) worsened by 9.6 billion JPY year-on-year, to a profit of 9.4 billion JPY.

3. Liquidity and Capital Resources

(1) Assets, Liabilities and Net Assets

Condensed Consolidated Balance Sheets

	Billions of Yen		*YoY Change*
	2019	2020	2020/2019
Assets			
Current assets	¥ 1,638.2	¥ 1,698.9	¥+60.7
Property, plant and equipment	408.8	558.1	+149.3
Investments and other assets	916.2	866.3	-49.9
Total Assets	2,963.2	3,123.3	+160.0
Liabilities			
Current liabilities	1,158.2	1,221.9	+63.7
Noncurrent liabilities	745.3	786.9	+41.5
Total liabilities	1,903.5	2,008.7	+105.2
Equity			
Total equity attributable to owners of the parent	858.9	910.7	+51.7
Non-controlling interests	200.7	203.8	+3.1
Total equity	1,059.7	1,114.5	+54.8
Total liabilities and equity	2,963.2	3,123.3	+160.0
Interest-bearing debt	552.5	675.4	+122.9
Net interest-bearing debt	274.2	316.2	+42.0
Equity attributable to owners of the parent	858.9	910.7	+51.7
Ratio of equity attributable to owners of the parent	29.0%	29.2%	+0.2
Debt equity ratio	0.64 times	0.74 times	0.10
Net debt equity ratio	0.32 times	0.35 times	0.03

Total assets were 3,123.3 billion JPY as of March 31, 2020, an increase of 160.0 billion JPY as compared with the end of the previous fiscal year. Current assets as of March 31, 2020 increased by 60.7 billion JPY compared with the end of the previous fiscal year to 1,698.9 billion JPY, mainly due to an increase in cash and cash equivalents from the collection of trade receivables and other receivables, despite a decrease in inventories due to the sales at the end of the period. Non-current assets as of March 31, 2020 increased by 99.4 billion JPY compared with the end of the previous fiscal year to 1,424.3 billion JPY, mainly due to an increase in property, plant and equipment due to the recording of right-of-use assets associated with the adoption of International Financial Reporting Standards ("IFRS") 16 "Leases" ("IFRS 16").

Total liabilities as of March 31, 2020 increased by 105.2 billion JPY compared with the end of the previous fiscal year, to 2,008.7 billion JPY, mainly due to the recording of a lease liability associated with the adoption of IFRS 16, despite a decrease in trade and other payables due to the payment of material costs. The balance of interest-bearing debt amounted to 675.4 billion JPY, an increase of 122.9 billion JPY as compared with the end of the previous fiscal year. The debt-equity ratio as of March 31, 2020 was 0.74 (a worsening of 0.10 points as compared with the end of the previous fiscal year). The balance of net interest-bearing debt as of March 31, 2020, calculated by offsetting the balance of interest-bearing debt with the balance of cash and cash equivalents, amounted to 316.2 billion JPY, an increase of 42.0 billion JPY as compared with the end of the previous fiscal year. The net debt-equity ratio as of March 31, 2020 was 0.35 (a worsening of 0.03 points as compared with the end of the previous fiscal year).

Taking into account the effects of adopting IFRS 16, changes in the balance of interest-bearing debt and the balance of net interest-bearing debt at the beginning of the fiscal year were a decrease of 52.2 billion JPY and a decrease of 133.2 billion JPY, respectively. The debt-equity ratio and the net debt-equity ratio improved 0.11 points and 0.17 points, respectively, compared to the beginning of the current fiscal year.

Total equity was 1,114.5 billion JPY as of March 31, 2020, an increase of 54.8 billion JPY as compared with the end of the previous fiscal year, mainly due to the recording of net profit attributable to owners of the parent for the fiscal year ended March 31, 2020, despite the payment of dividends and a decrease in other components of equity due to market price fluctuations of securities and the appreciation of the yen.

As a result, total equity attributable to owners of the parent (total equity less non-controlling interests) as of March 31, 2020 was 910.7 billion JPY, and the ratio of equity attributable to owners of the parent was 29.2% (an improvement of 0.2 points as compared with the end of the previous fiscal year).

(2) Cash Flows

Condensed Consolidated Cash Flows

		Billions of Yen		*YoY Change*
		2019	2020	2020/2019
I	Cash flows from operating activities	¥ 64.2	¥ 261.9	¥+197.6
II	Cash flows from investing activities	-76.7	-84.0	-7.3
I+II	Free cash flows	-12.4	+177.8	+190.3
III	Cash flows from financing activities	-50.5	-91.7	-41.2
Cash and cash equivalents at end of period		278.3	359.3	+80.9

Net cash inflows from operating activities for the fiscal year ended March 31, 2020 were 261.9 billion JPY, an improvement of 197.6 billion JPY as compared with the previous fiscal year, mainly due to improved income before income taxes as well as the impact of adopting IFRS 16 and improved working capital.

Net cash outflows from investing activities for the fiscal year ended March 31, 2020 were 84.0 billion JPY, an increase of 7.3 billion JPY as compared with the previous fiscal year, mainly due to an increase in purchase of property, plant and equipment.

As a result, free cash flows (the sum of cash flows from operating activities and investing activities) for the fiscal year ended March 31, 2020 totaled a cash inflow of 177.8 billion JPY, an improvement of 190.3 billion JPY year-on-year.

Net cash flows from financing activities for the fiscal year ended March 31, 2020 totaled a cash outflow of 91.7 billion JPY, mainly due to redemption of commercial paper as well as payment of dividends and repayment of lease liabilities.

As a result, cash and cash equivalents as of March 31, 2020 amounted to 359.3 billion JPY, an increase of 80.9 billion JPY as compared with the end of the previous fiscal year.

(3) Basic Liquidity Management Policy / Capital Resources

The NEC Group's basic policy is to maintain sufficient liquidity in hand for conducting business activities. Liquidity in hand is the sum of cash and cash equivalents and the unused portion of committed credit facilities established with multiple financial institutions. As of March 31, 2020, NEC had a sufficient amount of liquidity. Total liquidity in hand as of March 31, 2020, was 685.3 billion JPY, comprising cash and cash equivalents of 359.3 billion JPY and unused committed credit facilities of 326.0 billion JPY. Cash and cash equivalents are mainly denominated in JPY as well as other denominations that include U.S. dollars and euros.

The NEC Group maintains credit facilities that it believes are sufficient to meet its short-term and long-term financing needs. With regard to short-term financing, the NEC Group relies primarily on commercial paper ("CP") in Japan to provide for short-term financing. It has a 500.0 billion JPY CP program. To prepare for unexpected short-term funding needs or instability in fund procurement through the issue of CP, the NEC Group maintains committed short-term credit facilities of 328.0 billion JPY to ensure that funds may be borrowed from financial institutions at all times. Of this amount, 80.0 billion JPY represents a committed credit facility with a contract period effective through March 2023 that enables NEC to obtain short-term loans. For long-term financing, the NEC Group has a 300.0 billion JPY straight bond issuance program in Japan.

The NEC Group's basic policy regarding the structure of liabilities on the balance sheets is to maintain a balanced mix of fund procurement from debt and capital market instruments, while securing adequate long-term funds, from the standpoint of satisfying funding requirements in a stable manner.

The NEC Group's fund procurement status was as follows:

As of March 31,	2019	2020
Long-term fund procurement*1	71.0%	70.1%
Use of capital market instruments*2	41.5%	29.6%

*1 Long-term fund procurement is calculated by dividing the sum of bonds and long-term borrowings and others (lease obligations with maturities of more than one year) by interest-bearing debt.

*2 Use of capital market instruments is calculated by dividing the sum of bonds (including the current portion) and CPs by interest-bearing debt.

4. Capital Expenditures

Capital expenditures of NEC and its consolidated subsidiaries for fiscal 2019 and 2020 are broken down as follows (amounts do not include consumption taxes):

	Billions of Yen		*YoY Change*
	2019 *1	2020	2020/2019
Public Solutions Business	¥0.8	¥2.0	+148.3%
Public Infrastructure Business	26.7	29.2	+9.3%
Enterprise Business	1.3	1.0	-20.4%
Network Services Business	3.7	5.0	+36.4%
System Platform Business	5.7	6.2	+7.3%
Global Business	5.8	7.5	+28.6%
Others	18.7	16.5	-11.3%
Total	¥62.7	¥67.4	+7.6%

*1 From the fiscal year ended March 31, 2020, the Company's segments have been revised. In connection with this revision, capital expenditures for the fiscal year ended March 31, 2019 has been reclassified to conform to the presentation of the fiscal year ended March 31, 2020.

In the Public Solutions Business, capital expenditures included investments in R&D equipment related to smart infrastructure and production facilities.

In the Public Infrastructure Business, capital expenditures included production facilities for Japan Aviation Electronics Industry, Limited as well as R&D equipment and production facilities for defense, satellite and other systems.

In the Enterprise Business, capital expenditures included investments in equipment related to service and system development.

In the Network Services Business, capital expenditures included investment in R&D equipment and production facilities mainly for next-generation wireless communication systems.

In the System Platform Business, capital expenditures included investment in R&D equipment and production facilities for computers, such as servers and storage as well as equipment related to service development.

In the Global Business, capital expenditures included investments in related facilities for R&D equipment and production facilities for submarine cables.

In others, capital expenditures included investment in data center facilities.

NEC primarily used its own capital and borrowings to fund these capital expenditures.

5. Risk Factors

The NEC Group's business is subject to various risks. NEC's Group's management recognizes that the Group's financial condition, results of operations, and cash flow status could be materially affected by the primary risks described below, among matters related to the Group's business and management status. The forward-looking statements in this section are based on the judgement of the NEC Group as of the date of publication.

(1) Risks related to economic conditions and financial markets

a. Influence of economic conditions

The NEC Group's business is dependent, to a significant extent, on the Japanese market. The NEC Group's consolidated revenue to customers in Japan accounted for 75.7% of its total revenue in the fiscal year ended March 31, 2020. The future deterioration of economic conditions in Japan or the financial condition or performance of the Group's customer base in Japan could have a material adverse effect on the results of operations and the financial position of the NEC Group.

Moreover, the NEC Group's business is also influenced by the economic conditions of countries and regions including Asia, the United States and Europe, in which the NEC Group operates its business. Geopolitical issues and trade conflicts, including uncertainty regarding trade tensions between the United States and China and resulting trade restrictions such as tariffs, have recently contributed to increasing uncertainties in global markets, and increases in protectionist trade policies more generally may also contribute to slower global macroeconomic growth. Epidemics such as virus outbreaks, including the recent outbreak of the novel coronavirus COVID-19 described below in d. Impact of the outbreak of novel coronavirus COVID-19, may also negatively affect economic conditions in the global economy.

In addition, shifts in the policy or budgetary focus of national or local governments in Japan or internationally for economic or other reasons may also adversely affect the NEC Group's business.

Uncertainties in the economy make it difficult to forecast future levels of economic activity. Because the components of the NEC Group's planning and forecasting depend upon estimates of economic activity in the markets that the NEC Group serves, the prevailing economic uncertainty in Japan and overseas makes it more difficult than usual to estimate its future income and required expenditures. If the NEC Group is mistaken in its planning and forecasting, there is a possibility that the NEC Group will not be able to appropriately respond to the changing market conditions.

b. Fluctuations in foreign currency exchange and interest rate

The NEC Group is exposed to risks of foreign currency exchange rate fluctuations particularly for the Japanese yen against the U.S. dollar and euro. The NEC Group's consolidated financial statements, which are presented in Japanese yen, are affected by fluctuations in foreign exchange rates. Changes in exchange rates affect the yen value of the NEC Group's equity investments and monetary assets and liabilities arising from business transactions in foreign currencies. They also affect the costs and revenue of products or services that are denominated in foreign currencies. The NEC Group uses various measures to reduce, or hedge against, foreign currency exchange risks, such as offsetting of foreign currency-denominated operating receivables and payables, forward currency exchange contracts, and currency options. Despite these measures, however, foreign exchange rate fluctuations may hurt the NEC Group's business, results of operations and financial condition. Depending on the movements of particular foreign exchange rates, the NEC Group may be adversely affected at a time when the same currency movements are benefiting some of its competitors.

The NEC Group is also exposed to risks of interest rate fluctuations, which may affect its overall operational costs and the amount of its financial assets and liabilities, in particular, the burden of long-term debt. As of March 31, 2020, the NEC Group had 65,671 million JPY of long-term borrowings subject to floating interest rates. Despite measures undertaken by the NEC Group to hedge a portion of its exposure against interest rate fluctuations, such as interest rate swaps, such fluctuations may increase the NEC Group's operational costs, reduce the value of its financial assets, or increase the value of its liabilities.

c. Volatile nature of markets

The NEC Group is exposed to the risk that broader changes and trends in the ICT industry, both in Japan and overseas, may affect demand for the products and services that it provides. Demand for the NEC Group's products and services can be negatively affected by a slump in ICT market conditions, as well as obsolescence of existing products and services, excess inventories, and a decline in the NEC Group's cost competitiveness. The volatile nature of the relevant markets means that even if they recover, there may be future recurrences of downturns with similar or more adverse effects on the NEC Group's results of operations.

d. Impact of the outbreak of novel coronavirus (COVID-19)

The spread of coronavirus disease globally, including Japan, has led to the implementation of various countermeasures to prevent infection, including government-imposed travel restrictions in each country and request to people to refrain from going outside. The coronavirus and related government countermeasures may result in ongoing social, economic, financial and labor instability in the countries in which the NEC Group, its suppliers, and its customers operate. The extent to which the coronavirus will ultimately impact the NEC Group's operations and those of its suppliers and customers will depend on future developments, which are highly uncertain and cannot be predicted with confidence, including the duration of the pandemic. As the NEC Group's corporate customers as well as its Japanese national and local government customers focus on addressing the various difficulties presented by the emergency situation due to the spread of the disease, they may become more constrained in their ability to engage the NEC Group's services and purchase its products at the levels that were anticipated prior to the crisis. If the pandemic results in a decline in IT-related investments by the NEC Group's customers, its business, results of operations and financial condition would be adversely affected. In addition, disruptions in infrastructure, including communications, financial services, and supply chains, could materially and adversely disrupt the NEC Group's normal business operations.

To date, the NEC Group has transitioned a significant subset of its employee population to a remote work environment in an effort to mitigate the spread of the coronavirus, which may exacerbate certain risks to its business, including increased risk of cybersecurity attacks and increased risk of unauthorized dissemination of personal information or confidential information about the NEC Group, its customers or other third-parties, in addition to which internal control systems may not function effectively at the same level as before. Although the NEC Group has not closed any of its production facilities and has not yet experienced significant disruptions in its supply chain, the ongoing pandemic could result in facility closures by its customers or suppliers, general business shutdowns and financial difficulties. The pandemic could also result in increased prices, delays or difficulty in obtaining such components and raw materials. The NEC Group cannot presently predict the overall scope or duration of business disruptions as a result of the coronavirus, but its ability to conduct our business as previously planned could be materially and negatively impacted.

Capital markets have been affected by the pandemic, and the cost of fund procurement through corporate debt issuances, including the NEC Group's, has begun to increase. If the global economy were to deteriorate significantly such that the ordinary functioning of financial institutions is suspended, the NEC Group's ability to procure funds could be adversely affected.

Depending on the overall duration and severity of the impact of the coronavirus pandemic, the NEC Group may be required to recognize material impairments of its assets, including, but not limited to, goodwill, intangible assets and right-of-use assets. Additionally, declines in the value of the NEC Group's equity holdings in various major companies could negatively impact its financial condition. The NEC Group's equity instruments designated as measured at fair value through other comprehensive income was 167.2 billion JPY as of March 2020, and there is a possibility that this value will decrease due to the impact of the spread of the coronavirus pandemic.

The NEC Group is unable to estimate with certainty the overall impact to its business, results of operations and financial condition due to the coronavirus pandemic and any associated protective or preventative measures. While the spread of the coronavirus pandemic did not have a material adverse impact on its consolidated financial results and condition for the fiscal year ended March 31, 2020, future events and circumstances may result in the coronavirus pandemic having a more negative impact on its operations. The coronavirus-related developments have adversely affected the global economy until June 24, 2020, the approval date of the consolidated financial statements and may have a material adverse effect on the NEC Group's business, results of operations and financial condition.

(2) Risks related to the NEC Group's Management Policy

a. Mid-term management plan

In January 2018, the NEC Group launched "Mid-term Management Plan 2020" with the fiscal year ending March 31, 2021 as its final year, with the goals of 1) reforming of profit structure, 2) achievement of growth, and 3) restructuring of execution capabilities.

The NEC Group is carrying out initiatives to realize its Mid-term Management Plan, as described in "6. Management Strategy and Policy (4) Middle and Long Term Management Strategy and Challenges to be Addressed by the NEC Group". However, the NEC Group may be unable to achieve the goals stated in its mid-term management plan due to various factors discussed in more details in "5.Risk Factors".

b. Finance and profit fluctuations

The NEC Group's results of operations for any quarter or year are not necessarily indicative of results to be expected in future periods. The NEC Group's results of operations have historically been, and will continue to be, subject to quarterly and yearly fluctuations as a result of a number of factors, including:

- the introduction and market acceptance of new technologies, products, and services;
- delay or failure in development or commercialization of technologies or infrastructures to support them;
- generational technology upgrades, expiration of support services contracts for widely used software products, and technology investment cycles;
- variations in product costs, and the mix of products sold;
- seasonality of purchasing cycles of customers,
- the size and timing of customer orders, which in turn will often depend upon the success of customers' businesses or specific products or services;
- the impact of acquired businesses and technologies;
- fixed costs.

There are other trends and factors beyond the NEC Group's control that may affect its results of operations and make it difficult to predict results of operations for a particular period. These include:

- adverse changes in the market conditions for the products and services that the NEC Group offers;
- changes in conditions in the broader markets for ICT infrastructure and in the Japanese and global economies generally
- governmental decisions regarding the development and deployment of ICT and communications infrastructure, including the size and timing of governmental expenditures in these areas;
- the size and timing of capital expenditures and ICT spending by its customers;
- inventory management practices of its customers;
- changes in governmental regulation or policy affecting the ICT industry;
- adverse changes in the public and private equity and debt markets, and the ability of its customers and suppliers to obtain financing or to fund capital expenditures; and
- adverse changes in the credit conditions of its customers and suppliers.

These trends and factors could have a material adverse effect on the NEC Group's business, results of operations and financial condition.

c. Acquisitions and other business combinations and reorganizations

The NEC Group has completed and continues to seek appropriate opportunities for acquisitions and other business combinations and reorganizations in order to expand its business and strengthen its competitiveness. For example, as part of its growth strategy to expand the "NEC Safer Cities" initiative, the NEC Group acquired Northgate Public Services Limited in the United Kingdom in January 2018 and KMD Holding ApS in Denmark in February 2019. However, the NEC Group may be unable to find appropriate target companies with strengths that match the objectives of its inorganic growth strategy, and even if it is able to find such appropriate target companies, the NEC Group faces risks that could adversely affect its ability to achieve its strategic goals. For example,

- The NEC Group may be unable to realize the growth opportunities, improvement of its financial position, investment effect and other expected benefits by these acquisitions, business combinations and reorganizations in the expected time period or at all;
- The planned transactions may not be completed as scheduled or at all due to legal or regulatory requirements or contractual and other conditions to which such transactions are subject;
- Unanticipated problems could also arise in the integration process, including unanticipated restructuring or integration expenses and liabilities, as well as delays or other difficulties in coordinating, consolidating and integrating personnel, information and management systems, and customer products and services, particularly in markets outside Japan;
- The acquired, integrated, or reorganized entities may not be able to retain existing customers and strategic partners to the extent that they wish to diversify their suppliers for cost and risk management and other purposes;
- The acquired, integrated or reorganized entities may require additional financial support from the NEC Group;
- The diversion of management and key employees' attention may leave the NEC Group unable to focus on increasing revenues and minimizing costs in its existing businesses;
- The goodwill and other intangible assets arising from the acquisitions and business reorganizations are subject to impairment charges;
- NEC Group's investments in the acquired, integrated or reorganized entities are subject to valuation and other losses; and
- The transactions may result in other unanticipated adverse consequences.

Any of the foregoing and other risks may adversely affect the NEC Group's business, results of operations, financial condition and stock price.

d. Alliance with strategic partners

The NEC Group has entered into a number of long-term strategic alliances with leading industry participants, both to develop new technologies and products and to manufacture existing and new products. If the NEC Group's strategic partners encounter financial or other business difficulties, if their strategic objectives change or if they no longer perceive the NEC Group to be an attractive alliance partner, they may no longer desire or be able to participate in the NEC Group's alliances. The NEC Group's business could be hurt if the NEC Group is unable to continue one or more of its alliances. In addition, as a result of such strategic alliances, the NEC Group may become dependent on its alliance partners for product lines using co-developed technologies, leaving the NEC Group with less flexibility in expanding or diversifying its product offerings. The NEC Group participates in various projects where the NEC Group and various other companies provide services and products that are integrated into systems to meet customer requirements. If a strategic partner is unable to continue its role in the partnership due to bankruptcy or other reasons, or if any of the services or products that companies other than the NEC Group provide cause the integrated systems to malfunction, fail to meet customer requirements, or give rise to some other defect or problem, the NEC Group's reputation and business could be significantly harmed.

e. Expansion of global business

The NEC Group's strategies include expanding its business in markets outside Japan, including the promotion of NEC Safer Cities. As the NEC Group expands business, it will be exposed to risks that are unique to particular regions or markets. The NEC Group's efforts to penetrate new markets or offer new products and services may not succeed if the profitability or market growth of planned products and services develops more slowly than expected, if its new products and services are not well accepted among customers, if the profitability of opportunities is undermined by competitive pressures or regulatory limitations, or if its planned acquisitions, investments or capital alliances are not approved by regulators. The NEC Group may also lack sufficient knowledge or understanding of local business practices or legal and regulatory requirements. Moreover, depending on the market, the NEC Group may encounter difficulties in finding suitable business, joint venture and alliance partners. Furthermore, in many of these markets, the NEC Group faces entry barriers such as the existence of long-standing relationships between its potential customers and their local suppliers, and protective regulations. In addition, pursuing international growth opportunities may require the NEC Group to make significant investments long before it realizes returns on the investments, if any. Increased investments may result in expenses growing at a faster rate than revenues.

The NEC Group's overseas projects and investments could be adversely affected by:

- exchange controls;
- restrictions on foreign investment or the repatriation of income or invested capital;
- nationalization of local industries;
- changes in export or import restrictions;
- regulations in foreign markets, including with respect to licenses and permits that may be required from local authorities;
- changes in the tax system or rate of taxation in the countries where we do business; and
- economic, social, and political risks.

In addition, difficulties in foreign financial markets and economies could adversely affect demand from customers in the affected markets. Because of these factors, the NEC Group may not succeed in expanding its business in international markets, and its business growth prospects, results of operations and financial condition could be materially and adversely affected.

(3) Risks related to the NEC Group's business and operations

a. Technological advances and response to customer needs

The markets for the products and services that the NEC Group offers are characterized by rapidly changing technology, evolving technical standards, changes in customer preferences, and the frequent introduction of new products and services. The development and commercialization of new technologies and the introduction of new products and services will often make existing products and services obsolete or unmarketable. The NEC Group's competitiveness in the future will depend at least in part on its ability to:

- keep pace with rapid technological developments and maintain technological leadership, primarily in the fields of AI, IoT, biometrics and cybersecurity technology;
- enhance existing products and services;
- develop and manufacture innovative products that meet customers' needs in a timely and cost-effective manner;
- utilize or adjust to new products, services, and technologies;
- attract and retain highly capable technical and engineering personnel;
- accurately assess the demand for, and perceived market acceptance of, new products and services that the NEC Group develops;
- avoid delays in developing or shipping new products;
- address increasingly sophisticated customer requirements; and
- have the NEC Group's products integrated into its customers' products and systems.

The NEC Group may not be successful in identifying and marketing product and service enhancements, or offering and supporting new products and services, in response to rapid changes in technologies and customer preferences. Additionally, future technological changes may not advance in accordance with historical trends or predicted courses or timetables, and may differ from current forecasts. If the NEC Group fails to adequately monitor and address these technological changes and changes in customer preferences or accurately anticipate the direction of such changes, its business, results of operations and financial condition will be significantly harmed. In addition, the NEC Group may encounter difficulties in incorporating its technologies into its products in accordance with its customers' expectations, which may adversely affect its relationships with its customers, its reputation and revenues.

The NEC Group seeks to form and enhance alliances and partnerships with other companies to develop and commercialize technologies that will become industry standards for the products and services that it currently provides and plans to provide in the future. The NEC Group spends significant financial, human and other resources on developing and commercializing such technologies.

The NEC Group may not, however, succeed in developing or commercializing such standard-setting technologies if its competitors' technologies are accepted as industry standards. In such a case, the NEC Group's competitive position, reputation, results of operations and financial condition could be adversely affected.

b. Intense competition

To intense competition in many of the markets in which it operates. Competition places significant pressure on the NEC Group's ability to maintain gross margins and is particularly acute during market slowdowns. The entry of additional competitors into the markets in which the NEC Group operates increases the risk that its products and services will become subject to intense price competition. Some of the NEC Group's competitors mainly in Asian countries may have an advantage of lower production cost than the NEC Group does and may be able to compete for customers more effectively than it can in terms of price. There is also the risk that the NEC Group's competitors in the future may include multinational corporations with extensive financial resources. Multinational corporations such as these may invest significant resources into strategic pricing and research and development, and may undertake large-scale hiring of personnel. In recent years, the time between the introduction of a new product developed by the NEC Group and the production of the same or a comparable product by its competitors has become shorter. This has increased the risk that the products the NEC Group offers will become subject to intense price competition sooner than in the past.

The NEC Group has many competitors in Japan and other countries, ranging from large multinational corporations to a number of relatively small, rapidly growing, and highly specialized companies. Unlike many of the NEC Group's competitors, however, it operates in many businesses and competes with companies that specialize in one or more of its product or service lines. As a result, even if the NEC Group has more combined resources than its specialized competitors, it may not be able to fund or invest in some of its businesses as much as its competitors can and it may not be able to respond to change or take advantage of market opportunities as quickly or as well as they can.

The NEC Group's participation in competitive bidding or proposal processes for government and other large projects with demanding price and other requirements can place further downward pressure on its profitability. In order to maintain or improve profitability while meeting such demanding requirements, the NEC Group continuously strives to increase its revenue by offering and delivering innovative and unique value to customers and to reduce its costs and expenses through optimization of development and manufacturing operations, business process improvements and other measures. However, these measures may be insufficient to enable the NEC Group to maintain or improve its operating profit margin on such projects.

The NEC Group sells products and services to some of its current and potential competitors. For example, the NEC Group receives orders from, and provides solutions to, competitors that further integrate or otherwise use its solutions for large projects for which such competitors are engaged as the primary solutions provider. If these competitors cease to use the NEC Group's solutions for such large projects for competitive or other reasons, the NEC Group's business could be harmed.

c. Dependence on certain key customers

A substantial portion of the NEC Group's business portfolio consists of projects for government entities and certain large network and other infrastructure companies, such as the NTT group. Fluctuations in demand for such projects, particularly large-scale projects, or the NEC Group's potential inability to secure such projects through the applicable bidding processes, may have a significant impact on its revenue. Furthermore, government entities may reduce contract amounts or terminate contracts for funding, policy or other reasons. Similarly, corporate customers may reduce their level of capital expenditures, shift their investment focus or otherwise reduce their business with the NEC Group for business, financial or other reasons.

The NEC Group is also subject to the risk that regulatory restrictions may prevent it from participating in the bidding or proposal processes that are required for obtaining contracts with government entities. For example, in 2016 and 2017, the NEC Group was subject to a nomination stop from a significant number of Japanese government agencies and local governments after receiving notification from the Japanese Fair Trade Commission that it had violated the Japanese Act on Prohibition of Private Monopolization and Maintenance of Fair Trade. and thereby became temporarily ineligible to participate in the bidding process for projects. The NEC Group has worked to strengthen its internal control systems with a view to preventing regulatory violations; however, even if these measures are thoroughly implemented, the NEC Group is unable to completely eliminate the possibility of regulatory violations. Furthermore, if the number of projects for government entities decreases due to changes in demand, government policy, and regulations, the NEC Group's business, results of operations, and financial condition could be adversely affected.

d. Development of new business

The process of developing new products and services entails many risks. The development and manufacturing processes can be lengthy and costly and require the NEC Group to commit significant resources well in advance of actually selling or providing the product or service. For example, in 2019, the NEC Group acquired OncoImmunity AS (currently, NEC OncoImmunity AS) with a view to making a full-scale entry to the AI-driven drug discovery business. Because the NEC Group has limited experience with drug development, it anticipates that this initiative may not become profitable for an extended period and is still subject to the risk of failure. Additionally, new technologies may be launched and standards may change while new products or services are in the development stage, rendering them obsolete or uncompetitive before their introduction. Newly developed products or services may also contain undetected defects or errors that may be discovered after their introduction and distribution, resulting in liability for losses incurred by customers due to such errors and reputational harm to the NEC Group or the product or service. These could significantly and adversely affect the NEC Group's business, results of operations and financial condition.

e. Defects in products and services

The NEC Group faces risks arising from defects in its products and services. Defects in products and services provided by the NEC Group could cause serious losses to its customers, including public institutions, as well as to a large population of end users. Many of its products and services are used in customers' "mission critical" operations requiring high degree of reliability, where the NEC Group could be liable for damages incurred by its customers due to defects in product or service, or delays in their provision. Negative publicity concerning these problems could also make it more difficult to convince customers to buy the NEC Group's products and services, and the NEC Group could also be liable for recall costs. In particular, although products and services generally related to ICT solutions are exposed to customary risks of technology failure or computer viruses, many of the NEC Group's products and services are used in infrastructure that is directly related to the protection of human life, such as systems for fire rescue services, and it may be exposed to more serious liability. Products and services that use innovative technologies may also be exposed to risks that are difficult to foresee. Any reputational harm and regulatory sanctions that arise from these could harm the NEC Group's ability to sell its products and services. Furthermore, such factors may result in unprofitable projects.

In order to prevent the defects of products and services or unprofitable projects, the NEC Group takes thorough measures to control risks in projects such as system development projects from the beginning of business negotiation, through understanding of customer's confirmed system requirements or technical difficulties, and quality control measures on hardware and software of which systems consist. However, it is difficult to prevent them completely. The defects of its products or services or unprofitable projects could hurt the NEC Group's business, results of operations and financial condition.

f. Material Procurement of components, etc.

The NEC Group's business operations depend on obtaining deliveries of components, equipment, and other supplies in a timely manner. In some cases, the NEC Group purchases on a just-in-time basis. Because the components that the NEC Group purchases are often complex or specialized, it may be difficult for the NEC Group to substitute one supplier for another or one product for another. Some products are available only from a limited number of suppliers or a single supplier. Although the NEC Group believes that supplies of the components, equipment, and other supplies that the NEC Group uses are currently adequate, shortages in critical components could occur and the procurement cost of replacement parts increase, due to a delay or an interruption in supply, a change in regulatory trends, an increase in industry demand, or tariffs and other trade restrictions, which could adversely affect the NEC Group's production capacity and efficiency. In addition, a financial market disruption could pose liquidity or solvency risks for the NEC Group's suppliers, which could reduce its sources of supply or disrupt its supply chain. In addition, if the NEC Group procures components, equipment or other supplies include defects that could adversely affect the reliability and reputation of the NEC Group's products, or if it could not obtain adequate delivery of these supplies in a timely manner and at an acceptable price, the NEC Group's business, results of operations, and financial condition could be adversely affected.

g. Intellectual property rights

The NEC Group depends on its proprietary technology, and its ability to obtain patents and other intellectual property rights covering its products, services, business models, and design and manufacturing processes. The applications for patents and the maintenance of registered patents can be a time and cost consuming process. The NEC Group's patents could be challenged, invalidated, or circumvented. The fact that the NEC Group holds many patents or other intellectual property rights does not ensure that the rights granted under them will provide competitive advantages to the NEC Group. For example, the protection afforded by the NEC Group's intellectual property rights may be undermined by rapid changes in technologies in the industries in which the NEC Group operates. Similarly, there can be no assurance that claims allowed on any future patents will be broad enough to protect the NEC Group's technology. Effective patent, copyright, and trade secret protection may be unavailable or limited in some countries, and the NEC Group's trade secrets may be vulnerable to disclosure or misappropriation by employees, contractors, and other persons. Further, pirated products of inferior quality infringing the NEC Group's intellectual property rights may damage its brand and adversely affect sales of its products. Litigation, which could consume financial and management resources, may be necessary to enforce the NEC Group's patents or other intellectual property rights.

h. Intellectual property licenses owned by third parties

Many of the NEC Group's products are designed to include software or other intellectual property licenses from third parties. While it may be necessary in the future to seek or renew licenses relating to various aspects of the NEC Group's products, the NEC Group believes that, based upon experience and industry's standard practices, these licenses can be obtained on commercially reasonable terms in principle. There can be no assurance that the NEC Group will be able to obtain, on commercially reasonable terms or at all, from third parties the licenses that the NEC Group will need. In such a case, the NEC Group may be required to limit or cease operations that make use of such licenses, which could adversely affect its business, results of operations and financial condition.

i. Risks related to customers' financial difficulties

The NEC Group sometimes provides vendor financing to its customers or offer customers extended payment terms or other forms of financing to assist their purchase of the NEC Group's products and services. If the NEC Group is unable to provide or facilitate such payment arrangements or other forms of financing to its customers on terms acceptable to them or at all, due to financial difficulties or otherwise, the NEC Group's results of operations could be adversely affected. In addition, many of the NEC Group's customers purchase products and services from the NEC Group on payment terms that provide for deferred payment. If the NEC Group's customers for whom it has extended payment terms or provided other financing terms, or from whom it has substantial accounts receivable, encounter financial difficulties or inability to access credit from others, and are unable to make payments on time, the NEC Group's business, results of operations and financial condition could be adversely affected.

j. Retention of personnel

The NEC Group must compete for talented employees to develop its products, services and solutions that are acceptable to society, and its competition for these potential employees includes multinational technology companies with considerable resources. Accordingly, the NEC Group's human resources organization focuses significant efforts on attracting and retaining individuals needed in divisions that are driving the NEC Group's business, such as growth fields of the mid-term management plan. For this reason, recruitment and personnel costs may increase in the future. Changes in technology and industry trends may increase the need to recruit diverse human resources who are highly socially literate and have various values, abilities and backgrounds, as well as skills that differ from the conventional skillset. Specifically, recent trends in digitization and automation have resulted in increased demand for talent with skills in AI, machine learning, data science, and statistical analysis, and the NEC Group foresees fiercer competition from such talent. Furthermore, the recruitment of talent with these kinds of skills may require a different approach from the conventional recruitment method.

If the NEC Group experiences a substantial loss of, or an inability to attract and retain, talented personnel, or if it is unable to ensure the diversity of talent, it may experience difficulty in meeting its business objectives. This could leave the NEC Group unable to provide products, services, and solutions acceptable to society as a Social Value Innovator.

k. Financing

The NEC Group's primary sources of funds are cash flows from operations, borrowings from banks and other institutional lenders, and funding from the capital markets, such as offerings of commercial paper and other debt securities. A decline in the NEC Group's credit profile could result in a downgrade in its credit ratings and result in increases in its interest expenses, having an adverse impact on its ability to access the commercial paper market or other debt markets. This could have an adverse effect on the NEC Group's liquidity, business, and financial condition. Because the NEC Group maintains a relatively high level of leverage, its operations may be particularly affected in the event that it encounters difficulties in raising funds through debt.

A failure of one or more of the NEC Group's major lenders, a decision by one or more of them to stop lending to the NEC Group or instability in the capital markets could have an adverse impact on the NEC Group's access to funding. If the NEC Group fails to obtain external financing on terms acceptable to it, or at all, or to generate sufficient cash flows from its operations or sales of its assets, when necessary, the NEC Group will be unable to fulfill its obligations, and its business, results of operations, and financial condition will be materially adversely affected. In addition, to the extent the NEC Group finances its activities with additional debt, the NEC Group may become subject to financial and other covenants that may restrict its ability to pursue its growth strategy.

(4) Risks related to internal control, legal proceedings, laws and governmental policies

a. Internal control

The NEC Group is taking action to guarantee the accuracy of its financial reporting by strengthening its internal controls with expanding documentation of the business process and implementing stronger internal auditing. However, even effective internal control systems can provide only reasonable assurance with respect to the preparation and fair presentation of financial statements. For example, the inherent limitations of internal control systems include fraud, human error, or circumvention of controls, such as through collusion among multiple employees. In addition, the systems may not be able to effectively deal with changes in the business environment unforeseen at the time that the systems were implemented or with non-routine transactions. The NEC Group's established business processes may not function effectively, and fraudulent acts, such as false financial reporting or embezzlement, or inadvertent mistakes may occur. Such events may require restatement of financial information and could adversely affect the NEC Group's financial condition or results of operations. The NEC Group's reputation in the financial markets may also be damaged as a result of these events and occur much of additional costs in order to correct these events. In addition, if any administrative or judicial sanction is issued against the NEC Group as a result of these events, it may lose business opportunities.

If the NEC Group identifies a material weakness in its internal control systems, the NEC Group may incur significant additional costs for remedying such weakness. Despite the efforts by the NEC Group to continually improve and standardize its business processes from the perspective of ensuring effective operations and enhancing efficiency, it is difficult to design and establish common business processes since the NEC Group operates in a diverse range of countries and regions, using varying business processes, particularly when it acquires and integrates into the NEC Group a company that is engaged in an unfamiliar business or that operates in an unfamiliar market to the NEC Group. Consequently, the efforts by the NEC Group to further improve and standardize its business processes may continue to occupy significant management and human resources and the NEC Group may incur considerable financial costs.

b. Legal proceedings

From time to time, the NEC Group companies are involved in various lawsuits and legal proceedings, including intellectual property infringement claims. Due to the existence of a large number of intellectual property rights in the fields in which the NEC Group operates and the rapid rate of issuance of new intellectual property rights, it is difficult to completely judge in advance whether a product or any of its services may infringe upon the intellectual property rights of others. Whether or not intellectual property infringement claims against the NEC Group companies have merit, significant financial and management resources may be required to defend the NEC Group from such claims. If an intellectual property infringement claim by a third party is successful and the NEC Group could not obtain a license of technology which is subject of the infringement claim or any substitution thereof, it could have an adverse effect on the NEC Group's business, results of operations and financial condition.

The NEC Group may also from time to time be involved in various lawsuits and legal proceedings concerning such laws as business laws, antitrust laws, anticorruption laws, product liability laws, and environmental laws.

It is difficult to foresee the results of legal actions and proceedings currently involving the NEC Group or of those which may arise in the future, and an adverse result in these matters could have a significant negative effect on the NEC Group's business, results of operations and financial condition. In addition, any legal or administrative proceedings which the NEC Group is subject to could require management resources such as financial and human resources, including senior management, and the extend of such requirements is similarly difficult to predict. Such resources may be difficult for the NEC Group to acquire in a timely manner, and depending on the level of requirement, it could have a severe impact on the NEC Group's ability to conduct operations. Furthermore, if the NEC Group violates legal or regulatory requirements, it may be required to pay fines or penalties, and government agencies, local governments, and intergovernmental organizations could suspend or debar the NEC Group as a contractor or prevent it from participating in bidding or proposal processes, which could have a material adverse impact on the NEG Group's business, results of operation, financial condition, and reputation.

c. Laws and governmental policies

In many of the countries in which the NEC Group operates, its business is subject to various risks associated with unexpected regulatory changes, uncertainty in the application of laws and governmental policies and uncertainty relating to legal liabilities. Substantial changes in the regulatory or legal environments, including the economic, trade, tax, defense, labor, spending, privacy and other policies of the governments of Japan and other jurisdictions in which the NEC Group operates could oblige it to change its businesses or otherwise adversely affect its business, results of operations and financial condition.

For example, the regulatory authorities of each country may restrict or prohibit transactions with countries subject to economic sanctions, certain persons or entities, and such regulations may change dramatically within a short period. The NEC Group's existing compliance program may not be effective at preventing violations of such regulations, and the occurrence of such violations could have an adverse effect on the NEC Group's social credibility, business, results of operations and financial condition.

d. Environmental laws and regulations

The NEC Group's operations are subject to many environmental laws and regulations governing, among other things, air emissions, wastewater discharges, the use and handling of hazardous substances, waste disposal, chemical substances in products, product recycling, soil and ground water contamination and global warming. The NEC Group faces risks of environmental liability arising from its current, historical, and future manufacturing activities. The NEC Group's failure to comply with current and future environmental laws and regulations, or the identification of contamination for which it is liable, could subject the NEC Group to substantial costs, including fines, clean-up costs, third-party property damage or personal injury claims and require significant investments to upgrade its facilities and equipment. Moreover, the future occurrence of new environmental issues, enactment of more stringent regulatory requirements or other unanticipated events could give rise to adverse publicity, restrict the NEC Group's operations, affect the design or marketability of its products or otherwise cause it to incur material environmental costs, adversely affecting its results of operations and financial condition.

The NEC Group endeavors to comply with laws and government policies. It has established self-management norms, formulated guidelines on climate change mitigation measures from a long-term perspective up to 2050 and conducts daily inspections and environmental auditing in accordance with its internal environmental policies, but these measures may not be effective at avoiding potential liabilities arising from our current, historical and future business activities. Moreover, costs associated with future additional and stricter environmental compliance or remediation obligations could adversely affect the NEC Group's business, results of operations and financial condition. Details on the NEC Group's climate change response are provided in “6.Management Strategy and Policy (5) Response to Climate Change”.

e. Tax practice

The NEC Group's effective tax rate could be adversely affected by: earnings being lower than anticipated in countries that have lower tax rates and higher than anticipated in countries that have higher tax rates; changes in the valuation of the NEC Group's deferred tax assets and liabilities; transfer pricing adjustments; tax effects of nondeductible compensation; or changes in tax laws, regulations, accounting principles or interpretation thereof in the various jurisdictions in which the NEC Group operates. Any significant increase in the NEC Group's future effective tax rates could reduce net income for future periods.

The NEC Group currently carries deferred tax assets resulting from tax loss carry forwards and deductible temporary differences, both of which will reduce its taxable income in the future. However, the deferred tax assets may only be realized against taxable income. The amount of the NEC Group's deferred tax assets that is considered realizable could be reduced from time to time if estimates of future taxable income from its operations and tax planning strategies during the carry forward period are lower than forecasted, due to deterioration in market conditions or other circumstances. In addition, the amount of the NEC Group's deferred tax assets could be reduced due to changes in tax laws, regulations or accounting principles related to future deductions of income tax rates. Any such reduction will adversely affect the NEC Group's income for the period of the adjustment.

Furthermore, the NEC Group is subject to continuous audits and examination of its income tax returns by tax authorities of various jurisdictions. The NEC Group regularly assesses the likelihood of adverse outcomes resulting from these audits and examinations to determine the adequacy of its accrued income taxes. There can be no assurance that the outcomes of these audits and examinations will not have an adverse effect on the NEC Group's business, results of operations and financial condition.

f. Information management

The NEC Group collects, stores, uses, transfers, and performs other processes with a voluminous amount of personal information, including "My Number" social security and tax number information, as well as confidential information in the regular course of its business. There have been many cases where such information and records in the possession of corporations and institutions were leaked, improperly accessed or exposed by a cyberattack. If personal or confidential information in the NEC Group's possession about its customers or employees is leaked, improperly accessed or exposed by a cyberattack and subsequently misused, it may be subject to liability and regulatory action, and its reputation and brand value may be damaged. In particular, the increasingly sophisticated nature of cyberattacks, as well as the increasing scale and complexity of the business and infrastructure that can be targeted, make it possible that certain threats and vulnerabilities in systems related to information management will not be detected or mitigated in a timely manner. In addition, unauthorized access and cyberattack risk depends on the products, services and systems not only of the NEC Group, but also of its customers, contractors, suppliers, business partners and other third parties. These products, services and systems are also used by customers in highly regulated industries, such as financial and healthcare services, as well as government agencies. The NEC Group's products, services and systems may be used in customers' critical operations, and may involve the handling of sensitive data.

The NEC Group is required to handle personal information in compliance with Japan's Act on the Protection of Personal Information, the European Union's General Data Protection Regulation (GDPR) and other legal or regulatory requirements. The NEC Group may have to provide compensation for economic loss and emotional distress arising out of a failure to protect such information, or may be subject to large penalties imposed by regulatory authorities. The cost and operational consequences of implementing further data protection measures could be significant. In addition, if customers using the NEC Group's products, services and systems have been unable to protect their information, it could adversely affect the NEC Group's reputation and business. Furthermore, the NEC Group aims to grow by promoting NEC Safer Cities, using biometrics and AI technologies, among others. Given the increasing pace of development of these advanced technologies and the rising interest in related human rights issues, the scope of regulation around data projection and privacy protection is expanding and growing increasingly complex in individual countries and regions, which could lead to an increasing risk that the NEC Group will be subject to investigation and sanctions by regulatory authorities. Moreover, the NEC Group may lose business opportunities in certain countries and regions.

g. Human rights and work environment

In the countries and regions where the NEC Group operates, there is growing interest in how corporations respond to issues related to human rights and occupational safety and health, and the relevant laws and regulations are changing. In the event that the NEC Group's business offices and/or supply chain is unable to appropriately respond to these issues, the NEC Group may be faced with criticism from a range of stakeholders, including local residents, clients, consumers, shareholders, investors and human rights organizations, and it may cause the reputation and brand value of the NEC Group to be damaged. Moreover, in submitting to regulations, the NEC Group may bear a financial burden.

(5) Other Risks

a. Natural and fire disasters

Natural disasters such as earthquakes and typhoons, fires, abnormal weather (e.g. concentrated downpours, floods, water shortages) due to climate change, prevalence of highly virulent and fatal disease throughout the world (pandemic), armed hostilities, terrorism and other incidents, whether in Japan or any other country in which the NEC Group operates, could cause damage or disruption to the NEC Group, its suppliers or customers. These events could also create economic inactivity either in or outside Japan, fluctuation of foreign exchange or interest rates, political or economic instability, deterioration of public safety or public unrest, any of which could harm the NEC Group's business. In addition to various measures of disaster mitigation in place, the NEC Group has adopted a group-wide business continuity plan outlining countermeasures and recovery procedures to be taken in response to emergency, and has conducted training and learning programs. Despite the Company's efforts, natural disasters could disrupt social infrastructure such as electricity, gas and water supply, communication or transportation in affected areas, and could have a material adverse effect on NEC Group's business by causing human damages, disruptions of manufacturing, procurement and logistics, or occurrences of environmental and quality issues. Moreover, the spread of unknown infectious diseases to which human has no immunity, such as the further worsening of the outbreak of coronavirus described above in "(1) risks related to economic conditions and financial markets d. Impact of the outbreak of novel coronavirus (COVID-19)," could affect adversely the NEC Group's operations by increasing risks for inability to secure human resources and deterioration of working environment, as well as by reducing customer demand or disrupting its suppliers' operations in the infected areas.

b. Impairment of goodwill

The NEC Group has recorded significant goodwill as a result of its acquisitions of Northgate Public Services Limited in the United Kingdom in 2018 and KMD Holding ApS in Denmark in 2019, and it may also record additional goodwill as a result of further acquisitions in the future. The NEC Group's consolidated financial statements are prepared in accordance with IFRS, which requires testing cash generating units, or CGUs, to which goodwill has been allocated for impairment at least once annually, regardless of any indication of impairment. In addition, whenever it is recognized that there is a sign of impairment, it is necessary to perform an impairment test to determine whether the carrying amount of a CGU exceeds the recoverable amount. The recoverable amount of a CGU is the higher of its fair value less costs of disposal and its value in use. In determining the value in use, estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the carrying amount of a CGU with goodwill is found to exceed its recoverable amount as a result of testing, an impairment loss is recognized. Any impairment loss is processed by reducing the carrying amount of goodwill allocated to the CGU, which could adversely affect the NEC Group's results of operations and financial condition.

c. Defined benefit pension plan obligations

The NEC Group may face adverse effects on its financial condition and results of operations due to increases in defined benefit pension plan obligations arising from changes in the market value of equity securities and other pension assets and a decline in returns on pension assets. Changes in actuarial assumptions such as discount rates on which the calculation of projected defined benefit pension plan obligations are based may have an adverse effect on the NEC Group's financial condition and its results of operations. For example, there is a possibility of defined benefit pension plan obligations and/or defined benefit pension plan expenses increasing in the event of a future reduction in discount rates or prior service costs resulting from a change in the system.

d. Sale of NEC's common stock in the United States

As a result of the failure to file annual reports on Form 20-F with the Securities and Exchange Commission in the United States (hereinafter the "SEC") for the fiscal year ended March 31, 2006 and thereafter, American depositary shares of NEC were delisted from the NASDAQ Stock Market in October 2007. In addition, NEC was subject to an informal inquiry by the SEC concerning matters including its failure to file annual reports on Form 20-F for the fiscal year ended March 31, 2006 and thereafter. In June 2008, NEC entered into a settlement agreement with the SEC, and as part of the settlement, the SEC issued an order under Section 12(j) of the U.S. Securities Exchange Act of 1934 (hereinafter the "Exchange Act"). The SEC ordered that (a) NEC cease and desist from the violations of the Exchange Act because the SEC found that certain actions violated the Exchange Act, and (b) the registration under the Exchange Act of its common stock and American depositary shares be revoked (hereinafter the "SEC Order"). NEC did not admit or deny the findings by the SEC set forth in the SEC Order. No fine or other monetary payment was required under the order. As a result of the revocation, no broker or dealer worldwide and no member of a U.S. securities exchange may make use of the mails or any means or instrumentality of interstate commerce in the United States to effect any transaction in, or to induce the purchase or sale of, shares of common stock or American depositary shares of NEC. Accordingly, it may be difficult for shareholders of NEC to sell the shares of NEC's common stock in the United States, and this situation may continue in the future.

In response to this situation, NEC Corporation filed a registration statement on Form 20-F (the "Form 20-F") for its common stock with the SEC in order to resolve the restrictions of the SEC Order in the United States on March 17, 2020 (U.S. Eastern Standard Time). NEC has filed the Form 20-F in order to resolve the restrictions of the SEC Order. Once the Form 20-F becomes effective following review by the SEC, NEC Corporation expects that the restrictions of the SEC Order relating to making use of any means or instrumentality to effect or to induce any transaction of shares of common stock will be lifted, but the effect of the registration of Form 20-F has not been occurred as of June 24, 2020, the approval date of the consolidated financial statements.

6. Management Strategy and Policy

(1) Fundamental Management Policy

NEC Corporation revised the NEC Group's corporate philosophy, "the NEC Way," on April 1st, 2020, which summarizes the management practices and operations that the NEC Group adheres to, including its values and the driving principles behind its actions.

The NEC Way articulates NEC's "Purpose" and "Principles" as a company as well as the expected behaviors, "Code of Values" and "Code of Conduct", that all of the members comprising the NEC Group are expected to demonstrate.

Purpose

The "Purpose" is a declaration based on the statement of "Orchestrating a brighter world" to contribute to a prosperous society.

"NEC creates the social values of safety, security, fairness and efficiency to promote a more sustainable world where everyone has the chance to reach their full potential."

Principles

"Principles" are the basis for the NEC Group's actions and are comprised of three important positions.

The Founding Spirits of "Better Products, Better Services"
Uncompromising Integrity and Respect for Human Rights
Relentless Pursuit of Innovation

Code of Values

The "Code of Values" should be embodied by each and every one of the NEC Group, regardless of their position or level in the company.

"Look Outward. See the Future."
"Think Simply. Display Clear Strategy."
"Be Passionate. Follow through to the End."
"Move Fast. Never Miss an Opportunity."
"Encourage Openness. Stimulate the Growth of All."

Code of Conduct

To ensure NEC's ability to maintain society's trust and its commitment as a Social Value Innovator, the "Code of Conduct" details what is expected of each and every one of the NEC Group from today's society with respect to integrity and standards of conduct.

1. Basic Position
2. Respect for Human Rights
3. Environmental Preservation
4. Business Activities with Integrity
5. Management of the Company's Assets and Information

Consultation and Report on Doubts and Concerns about Compliance

To fulfill the Company's Purpose, the NEC Group aims to create social values continuously and to maximize its corporate values by implementing its middle and long term management strategy including its "Mid-term Management Plan" based on the Company's Principles.

Each and every one of the NEC Group, must compare our work style and organization structures to the Code of Values and identify where we need to strengthen and improve, and must conform to this Code of Conduct and conduct ourselves with high ethical standards and integrity.

The value that customers and society expect from us is constantly changing. To remain an essential company in the eyes of society in the years to come, we must create new value by constantly keeping our finger on the pulse of what it consists of. The NEC Group combines ICT technologies with diverse knowledge and ideas in collaboration with people around the world. We realize bright, hope-filled societies and ways of life, this is our aim.

(2) Management Indicator Goals

The NEC Group sets operating targets of revenue, operating profit margin, net profit, free cash flows and ROE (Return on Equity) as management indicators. NEC attaches paramount importance to operating profit margin among other indicators.

(3) Business environment

The worldwide economy during the fiscal year ended March 31, 2020 slowed down due to factors such as the US-China trade conflict and the effects of the novel coronavirus.

As for the Japanese economy, in addition to the slowdown of economies throughout the world and the increase in Japan's consumption tax rate, the impact of the novel coronavirus infectious disease resulted in sluggish performance.

(4) Middle and Long Term Management Strategy and Challenges to be Addressed by the NEC Group

Putting "the NEC Way" into practice, executives and employees at the NEC Group are striving as one to realize the "Mid-term Management Plan 2020" with the fiscal year ending March 31, 2021 as its final year, consisting of (i) Reform of profit structure, (ii) Achievement of growth, and (iii) Restructuring of execution capabilities.

(i) Reform of profit structure

In order to make the necessary investments to get back on a track to growth, the NEC Group aims to reduce the SGA ratio by enhancing employees' performance through business process reform and by efficiently managing expenditures. In addition, the NEC Group continues to work on reforming the business structure and implementing measures that lead to improved profits.

(ii) Achievement of growth

As the dissemination of digital technologies spurs a "Digital Transformation (DX)" that transforms the world around us, the NEC Group will, considering a society embedded with digital technologies a "digital inclusion society," aim to make all things in society become sophisticated in terms of total optimization, through visualizing, analyzing, and addressing the real world with the advantage of strength in its biometric authentication and AI technologies. By doing so, the NEC Group will create the social values of safety, security, fairness and efficiency to promote a more sustainable world where everyone has the chance to reach their full potential.

Specifically, the Company will focus on the two fields of "NEC Safer Cities" that realizes the establishment of safe, secure and convenient social infrastructure and abundant services, and "NEC Value Chain Innovation" that creates new value by connecting people, things and processes across the boundaries of industries. With Smart City, Mobility, Digital ID and Public Safety Networks etc. as its core, the NEC Group accelerates new business development through public-private sector partnership and cooperation among various industries.

(iii) Restructuring of execution capabilities

The NEC Group worked on challenging the creation of customer value leveraging advanced technology and reforms to maximize the abilities of employees in order to restructure execution capabilities.

Concerning challenging the creation of customer value leveraging advanced technology, in April 2020, a "Research and Development Unit" was newly established by integrating the central research labs and intellectual property/technology strategy division. The new unit will take the lead in maintaining and expanding the Company's core technologies, creating business models that maximize technological value through co-creation across the boundaries of industries, and promoting the sharing of infrastructure technology owned by each business unit, with an aim to accelerate the commercialization of technologies as an outcome of research and development.

Concerning reforms to maximize the abilities of employees, the NEC Group will continue activities under "Project RISE," a workstyle reform project launched in 2018. In order to allow each and every employee to flexibly select their working styles and fully perform their duties, the NEC Group takes steps for measures to accelerate shifts in working styles including smart work and office innovation.

Through these measures, the NEC Group aims to achieve the "Mid-term Management Plan 2020".

The NEC Group identified "materiality" comprising of the priority management themes from an

ESG (environment, society and governance) perspective in July 2018. More specifically, the five themes, including governance and compliance, environmental action with a particular focus on climate change, and privacy policies and measures aligned with societal expectations, are each positioned as a key to achieve a sustainable growth to minimize risks in the NEC Group and society and maximize social value created by the NEC Group, while other themes such as dialogue and co-creation with stakeholders and innovation management are positioned as an engine for growth innovation. To promote the sustainable growth of society and the Company, we engage in dialogue with diverse stakeholders, including customers, and promote initiatives together with them for resolving the priority management themes, with a view to contributing to the achievement of the Sustainable Development Goals (SDGs) set by the United Nations.

Moreover, the NEC Group recognizes that ensuring compliance in all of its operations is essential to continuing to exist as a good corporate citizen in society. The NEC Group will continue working to promote compliance.

(5) Response to Climate Change

Building a sustainable society requires initiatives on climate change caused by global warming, not only mitigation efforts to reduce greenhouse gas (GHG) emissions and prevent further warming, but also adaptation efforts to prepare for the risks of climate change and prevent or minimize the damage it causes. The NEC Group aims to minimize climate change risks and connect this with its own business growth by providing value to climate change countermeasures undertaken by its customers and society. To this end, the NEC Group have strategically evaluated the risks and opportunities that climate change presents to its businesses from both the mitigation and adaptation perspectives and set a direction and long-term targets for the Group. Specifically, in July 2017, the NEC Group formulated guidelines on climate change measures from a long-term perspective up to 2050, in which the NEC Group demonstrated how it collaborates with customers in co-creating a sustainable society, and the NEC Group is strengthening its climate change countermeasures. The guidelines comprise four components: 1) Reducing the supply chain CO2 emissions to zero, 2) Strict measures against climate change risks in supply chain, 3) Realizing the world-wide goal of a low carbon society, and 4) Achieving a safe and secure society that can withstand climate change risks. With a focus on component 1), the NEC Group has set a target of reducing CO2 emissions from its own business operations (Scope 1 and 2*) to zero by 2050.

As the main initiatives and accomplishments for the fiscal year ended March 31,2020, the NEC 's CO2 emission reduction targets were recognized by the international environmental organization "Science Based Targets (SBT) Initiative*" in October 2019 as the level of global warming to well-below 2°C above pre-industrial levels. Although NEC's targets were approved by the SBT Initiative as being a science-based for achieving the "2°C target" of the Paris Agreement in October 2018, it is also internationally recognized by this assessment to fully meet the level that the Paris Agreement requires.

Moreover, NEC participated in the CDP* Supply Chain Program run by the international NGO CDP.
NEC conducts a supplier survey through this program every year in addition to its own survey in order to recognize the progress on the countermeasures for climate change at suppliers to commend excellent suppliers which execute outstanding initiatives and promote to reduce emissions in the entire supply chain and enhance climate change countermeasures by working closely with its suppliers.
In January 2020, NEC has been named to the CDP "A List" for its initiatives of Climate Change and high evaluations to its information disclosures.

The NEC Group actively promotes provision of low-energy products and services using ICT and wider introduction of renewable energy among other measures, and promotes the development and provision of solutions to prepare against climate change risks such as flooding and landslide disasters. In this way, the Group will help its customers and society to counter climate change through both mitigation and adaptation.

* Scope 1: Direct GHG emissions from sources that are owned or controlled by the Company
Scope 2: Indirect GHG emissions from consumption of purchased electricity, heat or steam
SBT Initiative: A joint initiative of the CDP, UN Global Compact, World Resources Institute (WRI) and World Wide Fund for Nature (WWF).
CDP: An international non-profit organization in which investors, companies, cities, nations, and regions operate a global information disclosure system to manage environmental impacts. In fiscal 2019, more than 8,400 companies worldwide disclosed information through CDP.

(6) Policy on the Control over the Company

The Company believes that the ultimate decision as to the person who should control the financial and business policy of the Company shall be made by the shareholders of the Company. However, in the event that a person or entity (the "Proposer") proposes to purchase the substantial number of the shares of the Company with an intent to control the Company or proposes the takeover of the Company, the Company believes it is the responsibilities of the Board of Directors (i) to request the Proposer to provide appropriate information on the reasonableness of the consideration and other conditions of the proposal and the influence such action may have on the management policy and business plan of the Company, (ii) to evaluate the information provided and consider whether such proposal has merit in promoting the corporate value of the Company and the common interest of the shareholders, and (iii) to express the opinion of the Company for purposes of assisting the shareholders to make decisions whether or not to accept the proposal. In addition, the Company believes that, in the particular circumstances, it may be required to negotiate with the Proposer or to present alternative proposals to the shareholders.

Currently, the Company has not adopted a policy of defensive measures that will become effective when a proposal is made by a Proposer. It is the Company's intention, however, that if (i) the sufficient information is not provided by the Proposer, (ii) the shareholders are not afforded the time sufficient to consider the proposal or (iii) the Company decides that the proposal would have an adverse effect on the corporate value of the Company or the common interest of the shareholders, the Company will decide and implement reasonable countermeasures that are practicable at the time of the proposal and acceptable to the shareholders.

Consolidated Statements of Financial Position as of March 31, 2019 and 2020

JPY (millions)

	Notes	2019	2020
Assets			
Current assets			
Cash and cash equivalents	16	278,314	359,252
Trade and other receivables	15	734,431	737,484
Contract assets	26	265,725	247,625
Inventories	14	234,621	199,326
Other financial assets	31	5,875	5,584
Other current assets	17	110,199	108,436
Subtotal		1,629,165	1,657,707
Assets held for sale	18	9,071	41,210
Total current assets		1,638,236	1,698,917
Non-current assets			
Property, plant and equipment, net	8, 10	408,821	558,077
Goodwill	9, 10	188,183	182,334
Intangible assets, net	9, 10	218,581	199,093
Investments accounted for using the equity method	12	72,421	74,092
Other financial assets	31	250,409	219,326
Deferred tax assets	13	150,511	165,183
Other non-current assets	10, 17	36,060	26,232
Total non-current assets		1,324,986	1,424,337
Total assets		2,963,222	3,123,254

JPY (millions)

	Notes	2019	2020
Liabilities and equity			
Liabilities			
Current liabilities			
Trade and other payables	24	482,596	460,881
Contract liabilities	26	184,059	195,152
Bonds and borrowings	21	158,678	154,992
Accruals		178,911	191,440
Lease liabilities	31, 37	–	47,085
Other financial liabilities	31	16,169	14,995
Accrued income taxes		8,296	12,624
Provisions	23	58,448	59,412
Other current liabilities	25	61,985	55,153
Subtotal		1,149,142	1,191,734
Liabilities directly associated with assets held for sale	18	9,071	30,133
Total current liabilities		1,158,213	1,221,867
Non-current liabilities			
Bonds and borrowings	21	388,128	364,828
Lease liabilities	31, 37	–	108,514
Other financial liabilities	31	47,417	42,402
Net defined benefit liabilities	22	241,759	224,469
Provisions	23	24,803	12,369
Other non-current liabilities	25	43,221	34,282
Total non-current liabilities		745,328	786,864
Total liabilities		1,903,541	2,008,731
Equity			
Share capital	19	397,199	397,199
Share premium	19	138,824	139,735
Retained earnings	19	354,582	436,361
Treasury shares	19	(3,547)	(4,157)
Other components of equity	19	(28,119)	(58,464)
Total equity attributable to owners of the parent		858,939	910,674
Non-controlling interests	11	200,742	203,849
Total equity		1,059,681	1,114,523
Total liabilities and equity		2,963,222	3,123,254

See accompanying notes to consolidated financial statements.

Consolidated Statements of Profit or Loss for the Fiscal Years Ended March 31, 2019 and 2020

JPY (millions)

	Notes	2019	2020
Revenue	6, 26	2,913,446	3,095,234
Cost of sales	14, 28	2,083,517	2,207,675
Gross profit		829,929	887,559
Selling, general and administrative expenses	28	743,021	752,690
Other operating expenses	27	29,128	7,260
Operating profit	6	57,780	127,609
Finance income	6, 29	21,989	8,477
Finance costs	6, 29	8,377	15,464
Share of profit of entities accounted for using the equity method	6, 12	5,916	3,347
Profit before income taxes		77,308	123,969
Income taxes	13	25,378	11,250
Net profit		51,930	112,719
Net profit attributable to:			
Owners of the parent		39,675	99,967
Non-controlling interests		12,255	12,752
Total		51,930	112,719
Earnings per share attributable to owners of the parent:			
Basic earnings per share (JPY)	30	152.75	385.02
Diluted earnings per share (JPY)	30	152.75	385.01

See accompanying notes to consolidated financial statements.

Consolidated Statements of Comprehensive Income for the Fiscal Years Ended March 31, 2019 and 2020

JPY (millions)

	Notes	2019	2020
Net profit		51,930	112,719
Other comprehensive income, net of tax			
Items that will not be reclassified to profit or loss			
Equity instruments designated as measured at fair value through other comprehensive income	19	(3,035)	(20,297)
Remeasurements of defined benefit plans	19, 22	(40,348)	2,160
Share of other comprehensive income of entities accounted for using the equity method	19	(371)	(84)
Total items that will not be reclassified to profit or loss		(43,754)	(18,221)
Items that may be reclassified subsequently to profit or loss			
Exchange differences on translating foreign operations	19	(735)	(14,776)
Cash flow hedges	19	(61)	22
Share of other comprehensive income of entities accounted for using the equity method	19	26	(175)
Total items that may be reclassified subsequently to profit or loss		(770)	(14,929)
Total other comprehensive income, net of tax		(44,524)	(33,150)
Total comprehensive income		7,406	79,569
Total comprehensive income attributable to:			
Owners of the parent		(4,955)	69,622
Non-controlling interests		12,361	9,947
Total		7,406	79,569

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Equity for the Fiscal Years Ended March 31, 2019 and 2020

JPY (millions)

	Notes	Equity attributable to owners of the parent						Non-controlling interests	Total equity
		Share capital	Share premium	Retained earnings	Treasury shares	Other components of equity	Total		
As of April 1, 2018		397,199	138,704	265,879	(3,364)	82,415	880,833	173,452	1,054,285
Impact of changes in accounting policies		–	–	64,619	–	(65,904)	(1,285)	–	(1,285)
Recalculated beginning balance		397,199	138,704	330,498	(3,364)	16,511	879,548	173,452	1,053,000
Net profit		–	–	39,675	–	–	39,675	12,255	51,930
Other comprehensive income	19	–	–	–	–	(44,630)	(44,630)	106	(44,524)
Comprehensive income		–	–	39,675	–	(44,630)	(4,955)	12,361	7,406
Purchase of treasury shares	19	–	–	–	(215)	–	(215)	–	(215)
Disposal of treasury shares	19	–	2	–	32	–	34	–	34
Cash dividends	20	–	–	(15,591)	–	–	(15,591)	(4,302)	(19,893)
Put option, written over shares held by a non-controlling interest shareholder		–	836	–	–	–	836	–	836
Changes in interests in subsidiaries	11	–	(718)	–	–	–	(718)	19,231	18,513
Total transactions with owners		–	120	(15,591)	(183)	–	(15,654)	14,929	(725)
As of March 31, 2019		397,199	138,824	354,582	(3,547)	(28,119)	858,939	200,742	1,059,681

JPY (millions)

	Notes	Equity attributable to owners of the parent						Non-controlling interests	Total equity
		Share capital	Share premium	Retained earnings	Treasury shares	Other components of equity	Total		
As of April 1, 2019		397,199	138,824	354,582	(3,547)	(28,119)	858,939	200,742	1,059,681
Net profit		–	–	99,967	–	–	99,967	12,752	112,719
Other comprehensive income	19	–	–	–	–	(30,345)	(30,345)	(2,805)	(33,150)
Comprehensive income		–	–	99,967	–	(30,345)	69,622	9,947	79,569
Purchase of treasury shares	19	–	–	–	(674)	–	(674)	–	(674)
Disposal of treasury shares	19	–	(0)	–	63	–	63	–	63
Cash dividends	20	–	–	(18,188)	–	–	(18,188)	(4,941)	(23,129)
Put option, written over shares held by a non-controlling interest shareholder		–	912	–	–	–	912	–	912
Changes in interests in subsidiaries	11	–	0	–	–	–	0	(1,899)	(1,899)
Total transactions with owners		–	912	(18,188)	(611)	–	(17,887)	(6,840)	(24,727)
As of March 31, 2020		397,199	139,735	436,361	(4,157)	(58,464)	910,674	203,849	1,114,523

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows for the Fiscal Years Ended March 31, 2019 and 2020

JPY (millions)

	Notes	2019	2020
Cash flows from operating activities			
Profit before income taxes		77,308	123,969
Depreciation and amortization	6	99,745	166,360
Impairment loss	6,10	12,607	6,384
Increase (decrease) in provisions		15,101	(5,639)
Finance income	29	(21,989)	(8,477)
Finance costs	29	8,377	15,464
Share of profit of entities accounted for using the equity method		(5,916)	(3,347)
(Increase) in trade and other receivables		(41,470)	(26,263)
(Increase) decrease in contract assets		(16,951)	11,911
(Increase) decrease in inventories		(16,716)	11,430
Increase in trade and other payables		4,415	1,653
Increase in contract liabilities		21,500	11,536
Other, net		(48,544)	(20,517)
Subtotal		87,467	284,464
Interest and dividends received		7,580	6,947
Interest paid		(6,350)	(9,052)
Income taxes paid		(24,462)	(20,496)
Net cash provided by operating activities		64,235	261,863
Cash flows from investing activities			
Purchases of property, plant and equipment		(48,929)	(72,825)
Proceeds from sales of property, plant and equipment		4,283	6,903
Acquisitions of intangible assets		(11,764)	(16,372)
Purchase of equity instruments designated as measured at fair value through other comprehensive income		(7,375)	(1,820)
Proceeds from sales of equity instruments designated as measured at fair value through other comprehensive income		2,293	12,279
Purchase of shares of newly consolidated subsidiaries	7	(47,930)	(6,935)
Increase in cash flows resulting in change in scope of consolidation, net of consideration transferred	7	17	52
Proceeds from sales of shares of subsidiaries	18	20,230	–
Decrease in cash flows resulting in change in scope of consolidation, net of consideration transferred		–	(220)
Purchases of investments in associates or joint ventures		(1,148)	(376)
Proceeds from sales of investments in associates or joint ventures	18	13,816	2,098
Proceeds from collection of loans receivable		94	44
Other, net		(262)	(6,851)
Net cash used in investing activities		(76,675)	(84,023)

	Notes	2019	2020
			JPY (millions)
Cash flows from financing activities			
Increase (decrease) in short-term borrowings, net	21	48,234	(4,349)
Proceeds from long-term borrowings	21	9,681	37,879
Repayments of long-term borrowings	21	(157,778)	(48,723)
Proceeds from issuance of bonds	21	50,011	–
Repayments of lease liabilities	32	–	(53,620)
Proceeds from sales of interests in subsidiaries to non-controlling interests		18,810	–
Dividends paid	20	(15,586)	(18,177)
Dividends paid to non-controlling interests		(4,261)	(4,939)
Other, net		386	182
Net cash used in financing activities		(50,503)	(91,747)
Effect of exchange rate changes on cash and cash equivalents		(1,275)	(4,496)
Net (decrease) increase in cash and cash equivalents		(64,218)	81,597
Cash and cash equivalents, at beginning of the year		346,025	278,314
Decrease in cash and cash equivalents resulting from transfer to assets held for sale	18	(3,493)	(659)
Cash and cash equivalents, at end of the year	16	278,314	359,252

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

1. Reporting Entity

NEC Corporation (the "Company" or "NEC") is a public company incorporated in Japan. NEC and its subsidiaries (collectively, the "NEC Group") has six segments: Public Solutions business, Public Infrastructure business, Enterprise business, Network Services business, System Platform business and Global business, all of which are operating segments. For further information regarding these businesses, see Note 6. "Segment Information." The NEC Group's principal operating bases are located mainly in Japan and other countries as disclosed in Note 11. "Subsidiaries."

2. Basis of Preparation

Compliance with International Financial Reporting Standards

The Company fulfills the requirements of a "specified company of designated International Financial Reporting Standards" as provided in Article 1-2 of the "Ordinance on Terminology, Forms, and Preparation Methods of Consolidated Financial Statements" (Ordinance of the Ministry of Finance No. 28 of 1976, the "Ordinance on Consolidated Financial Statements"). Therefore, in accordance with the provisions of Article 93 of the Ordinance on Consolidated Financial Statements, the Company's consolidated financial statements are prepared in conformity with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). The term "IFRS" also includes International Accounting Standards ("IAS") and the related interpretations of the Standard Interpretations Committee ("SIC") and IFRS Interpretations Committee ("IFRIC").

Approval of Financial Statements

The consolidated financial statements were approved by Takashi Niino, President and CEO, and Takayuki Morita, Senior Executive Vice President, Member of the Board, and CFO, on June 24, 2020.

Changes in Presentation Method

The NEC Group has revised its presentation method for the purpose of providing more useful information regarding the notes to the consolidated financial statements for the fiscal year ended March 31, 2020. In addition, similar information has been added to the notes to the consolidated financial statements for the comparative year, which is comparative information, and disclosure of some insignificant information has been omitted. Also, regarding the disclosure of certain notes to the consolidated financial statements, the amounts for the comparative year have been restated.

Basis of Measurement

The consolidated financial statements have been prepared on historical cost, except for certain assets and liabilities separately stated in Note 3. "Significant Accounting Policies."

Functional and Presentation Currency

The consolidated financial statements are presented in Japanese yen ("JPY"), which is the functional currency of the Company. All financial information presented in JPY has been rounded to the nearest million JPY, except when otherwise indicated.

New Accounting Standards and Interpretations Adopted

During the fiscal year ended March 31, 2020, the NEC Group has adopted IFRS 16, "Leases" ("IFRS 16") with the method of recognizing the cumulative effect of the adoption of this new standard and the new accounting policy in equity as of the date of initial application on April 1, 2019. Accordingly, the comparative information as of March 31, 2019 and for the fiscal years ended March 31, 2019 has not been restated. For the details, please refer to Note 37. "Impact of Changes in Accounting Policies."

3. Significant Accounting Policies

Unless otherwise stated, accounting policies set out below have been applied consistently to all periods presented in the consolidated financial statements.

Basis of Consolidation

Subsidiaries

The consolidated financial statements include the accounts of the NEC Group and its subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Subsidiaries are entities that are directly or indirectly controlled by the Company. The NEC Group controls an entity when the NEC Group is exposed or has rights to variable returns from involvement with the entity and has the ability to affect those returns by using its power, which is the current ability to direct the relevant activities, over the entity. To determine whether or not the NEC Group controls an entity, status of voting rights or similar rights, contractual agreements, and other relevant factors are considered.

The financial statements of the subsidiaries are included in the consolidated financial statements from the date when the control is obtained until the date when the control is lost. The financial statements of subsidiaries have been adjusted in order to conform to the accounting policies adopted by the Company as necessary.

Changes in the Company's ownership interests in subsidiaries that do not result in a loss of control are accounted for as equity transactions. Any differences between the adjustment to non-controlling interest and fair value of consideration transferred or received are recognized directly in equity attributable to owners of the Company.

When control over a subsidiary is lost, the investment retained after the loss of control is re-measured at fair value as of the date when control is lost, and any gain or loss on such re-measurement and disposal of the interest sold is recognized in profit or loss.

Investments in Associates and Joint Arrangements

Associates are entities over which the NEC Group has significant influence over the decisions on financial and operating policies, but does not have control or joint control.

Joint arrangements are arrangements of which two or more parties have joint control. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. The NEC Group classifies joint arrangements into either joint ventures or joint operations. The classification of a joint arrangement as a joint venture or a joint operation depends upon the rights and obligations of the parties to the arrangement. Joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets and obligations for the liabilities, relating to the arrangement. There are no joint operations that are considered material to the NEC Group.

Investment in associates and joint ventures are accounted for using the equity method and recognized at cost on the acquisition date. The carrying amount is subsequently increased or decreased to recognize the NEC Group's share of profit or loss and other comprehensive income of the associates and joint ventures after the date of initial recognition.
The financial statements of associates and joint ventures have been adjusted in order to conform to the accounting policies adopted by the Company in applying the equity method, as necessary.

Impairment of an investment in associates and joint ventures is measured by comparing the recoverable amount and the carrying amount of the investment. The impairment loss is recognized in profit or loss. If there has been a change in the estimates used to determine the recoverable amount and the recoverable amount increases, the impairment loss is reversed.

Business Combinations

Business combinations are accounted for using the acquisition method.
The consideration transferred for the acquisition of a subsidiary is measured at fair value of the assets transferred, the liabilities incurred to former owners of the acquiree, and the equity interests issued by the NEC Group.
The consideration for certain acquisitions includes payments that are contingent upon future events, such as the achievement of milestones and sales targets.

Identifiable assets acquired and liabilities and certain contingent liabilities assumed are measured at the fair values at the acquisition date. Non-controlling interests are initially measured either at fair value or at the non-controlling interests' proportionate share of the recognized amount of the acquiree's identifiable net assets on a transaction-by-transaction basis.
Goodwill is measured as the excess of the sum of the fair value of consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest less the fair value of identifiable assets acquired, net of liabilities assumed at the acquisition date.

Acquisition related costs, such as agency, legal, and other professional, or consulting fees are recognized as expenses in the period they are incurred.

Foreign Currency Translation

Foreign Currency Transactions

Transactions in foreign currencies are translated into the respective functional currencies of the NEC Group companies using the exchange rate at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency using the exchange rate at the end of each reporting period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at historical cost are translated into the functional currency using the exchange rate at the transaction date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated into the functional currency using the historical exchange rates at the date when the fair value was determined. Exchange differences arising from the settlement or translation of monetary items are recognized in profit or loss except for exchange differences arising from financial assets measured at fair value through other comprehensive income and qualifying hedging instruments in cash flow hedges to the extent that the hedges are effective, which are recognized in other comprehensive income.

Foreign Operations

The assets and liabilities of foreign operations are translated into Japanese yen using the exchange rate prevailing at the reporting date and their income and expenses are translated into Japanese yen using the average exchange rate for the period, unless the exchange rate fluctuates significantly. The foreign exchange differences arising on translation are recognized in other comprehensive income. In cases foreign operations are disposed of, the cumulative amount of other comprehensive income relating to that particular foreign operation is reclassified to profit or loss as part of gains and losses on the disposal.

Financial Instruments

Non-derivative Financial Assets

The NEC Group classifies non-derivative financial assets into financial assets measured at amortized cost, financial assets measured at fair value through other comprehensive income, or financial assets measured at fair value through profit or loss. The NEC Group has irrevocably elected to designate all equity instruments, except for those in the form of venture capital investments, in principle as financial assets measured at fair value through other comprehensive income.
The NEC Group initially recognizes financial assets measured at amortized cost on the date they originated. All other financial assets are initially recognized in the consolidated statements of financial position when the NEC Group becomes a party to the contractual provisions of the financial instruments.
The NEC Group derecognizes financial assets when the contractual rights to the cash flows from the asset expire, or when the NEC Group transfers the contractual rights to the cash flows from the asset, as well as substantially all the risks and rewards of ownership of the financial asset. Separate assets or liabilities are recognized when the NEC Group derecognizes financial assets, but still retains an interest that does not result in the retention of control over the financial asset.

Financial assets held by the NEC Group are measured at amortized cost when both of the following conditions are met:

- The financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets measured at amortized cost are initially measured at fair value, plus any directly attributable transaction costs. Trade receivables that do not contain a significant financing component are measured at their transaction price. After initial recognition, the carrying amounts of financial assets measured at amortized cost are recognized using the effective interest method, less impairment loss. Amortization using the effective interest method and gains and losses on derecognition are recognized in profit or loss for the period.

The NEC Group has in principle elected to present subsequent changes in fair value of certain equity instruments in other comprehensive income except for those in the form of venture capital investments. These equity instruments are initially measured at fair value, plus any directly attributable transaction costs and measured at fair value in subsequent periods. Changes in fair value are included in other comprehensive income and never reclassified to profit or loss and the NEC Group never reclassifies accumulated other comprehensive income to retained earnings subsequently. Dividends from equity instruments designated as measured at fair value through other comprehensive income are recognized as finance income in profit or loss, unless the dividends clearly represent a recovery of part of the cost of the investment.

Financial assets other than financial assets measured at amortized cost or equity instruments designated as measured at fair value through other comprehensive income are classified as financial instruments measured at fair value through profit or loss. These financial assets are measured at fair value after initial recognition, and changes in their fair value are recognized in profit or loss. Gains and losses on financial instruments measured at fair value through profit or loss are recognized in profit or loss.

Impairment of Financial Assets

As for impairments on financial assets measured at amortized costs, the NEC Group recognizes allowances for expected credit losses by assessing whether the credit risk on the financial assets has increased significantly at each reporting date since initial recognition. Allowances are measured based on the estimated credit loss arising from the possible defaults during the 12 months after the reporting date (12-month expected credit loss) when the credit risk associated with the financial assets has not significantly increased since initial recognition. When the credit risk associated with the financial assets has significantly increased since initial recognition or the financial assets are credit-impaired, an allowance for expected credit loss is calculated based on the estimated credit loss arising from all possible defaults over the estimated remaining period of the financial instruments (life-time expected credit loss). Notwithstanding the above, an allowance for expected credit loss on trade receivables and contract assets is always calculated based on the estimated credit loss over the entire period. Significant increase in credit risk is determined based on changes in risks of a default occurring and the changes in such risks are determined considering significant financial difficulty, breach of contract, or increase in probability where the borrower will enter bankruptcy or other financial reorganization. Changes in allowances are recognized in profit and loss.

Non-derivative Financial Liabilities

The NEC Group classifies non-derivative financial liabilities into financial liabilities measured at amortized cost. The NEC Group recognizes debt securities on the date of issuance. All other financial liabilities are initially recognized on the date when the NEC Group becomes a party to contractual provisions. The NEC Group derecognizes a financial liability when its contractual obligations are discharged, canceled, or expired. These financial liabilities are measured initially at fair value less any directly attributable transaction costs and subsequently measured at amortized cost using the effective interest method. Amortization amounts are recognized as finance costs in profit or loss.

Derivative Financial Instruments

The NEC Group holds derivative financial instruments, such as forward exchange contracts, interest rate swaps, and currency options, to hedge foreign currency exposure and interest rate exposures. Derivatives are measured at fair value at the inception and subsequent periods. At the inception of a hedge relationship, derivatives designated as hedging instruments are classified as either cash flow hedge, fair value hedge, or hedge of a net investment. For derivatives that are not designated as hedging instruments, any changes in the fair value of the derivative are recognized in profit or loss. For derivatives that are designated as hedging instruments, the NEC Group documents the relationship between the hedging instrument and hedged item, risk management objectives and strategy in undertaking the hedge transaction and the hedged risk at the inception of the hedges. The NEC Group initially and continually assesses whether the hedging instruments are highly effective in offsetting changes in the fair value or the cash flows of the respective hedged items. The NEC Group does not currently have derivatives that are designated as hedging instruments in a fair value hedge nor net investment hedge relationship.

Cash Flow Hedges

The effective portion of changes in the fair value of derivatives is recognized in other comprehensive income and any ineffective portion of changes in the fair value is immediately recognized in profit or loss. The amount accumulated in other components of equity is reclassified to profit or loss in the same period during which the cash flows of the hedged item affect profit or loss. Hedge accounting is discontinued prospectively when the hedging instrument expires, is sold, terminated, exercised, when no longer meets the criteria for hedge accounting, a forecast transaction is no longer highly probable, or the designation is revoked.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, demand deposits, and short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of changes in value, and redeemable in three months or less from each acquisition date.

Property, Plant and Equipment

Property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenses directly attributable to acquisition of the asset, costs of dismantling and removing the assets, costs of restoring the site, and borrowing costs to be capitalized. When significant components of property, plant and equipment have different useful lives, they are accounted for as separate items (by major components) of property, plant and equipment. Gains or losses on disposals of property, plant and equipment are recognized in profit or loss.
Except for assets that are not subject to depreciation, such as land and construction in progress, assets are depreciated mainly using the straight-line method over the estimated useful lives of assets. The residual value is generally estimated at zero, except for the cases where the selling price, after deducting the costs of disposal, at the end of the useful lives is estimable.

The estimated useful lives of major property, plant and equipment are as follows:

Buildings and structures	7–60 years
Machinery and equipment	2–22 years
Tools, furniture and fixtures	2–20 years

Depreciation methods, useful lives, and residual values of assets are reviewed at the end of each reporting period and revised, as necessary.

Goodwill

An asset representing the future economic benefits arising together with other assets through the acquisition of a subsidiary that are not individually identifiable is recognized as Goodwill. Goodwill is not amortized, but is tested for impairment at least annually or more frequently whenever there is any indication of impairment for a cash-generating unit ("CGU") to which goodwill is allocated. The NEC Group initially measures goodwill at the acquisition date as the excess of the aggregate of consideration transferred, amount of any non-controlling interest in the acquired entity, and acquisition-date fair value of any previous equity interest in the acquired entity, less the net recognized amount of the identifiable assets acquired and liabilities assumed. If those amounts are less than the fair value of the net identifiable assets of the business acquired, the difference is recognized directly in profit or loss as a bargain purchase gain.

Intangible Assets

Development expenditures on software for sale and software for internal use are recognized as intangible assets, if all of the following criteria of capitalization are met:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- its intention to complete the intangible asset and use or sell it;
- its ability to use or sell the intangible asset;
- how the intangible asset will generate probable future economic benefits;
- the availability of adequate technical, financial, and other resources to complete the development and to use or sell the intangible asset; and
- its ability to measure reliably the expenditure attributable to the intangible asset during its development.

Other intangible assets, such as patents and licenses, are recognized at cost when acquired. Intangible assets acquired in business combinations and recognized separately from goodwill, including acquired capitalized development costs, are recognized at fair value at the acquisition date.

Intangible assets with definite useful lives are amortized mainly on a straight-line basis over their estimated useful lives from the date when the assets are available for use. Amortization of intangible assets is included in cost of sales and selling, general and administrative expenses. Customer relationship is amortized on a straight-line basis over the estimated useful lives. Software for sale is amortized based on the expected sales volume over the expected effective period unless such amortization method does not reflect the pattern of consumption of the expected future benefits from the asset. In such cases, software for sale is amortized on a straight-line basis over the remaining useful life. Software for internal use is amortized on a straight-line basis over the estimated useful lives. Other intangible assets, such as patents and licenses, are amortized from the date when the asset is available for use over the estimated useful lives, such as a contract period, using the method that reflects the pattern of consumption of the future economic benefits by the NEC Group.

The estimated useful lives of major intangible assets are as follows:

Software for sale	1–8 years
Software for internal use	3–5 years
Customer relationship	3–19 years
Acquired capitalized development costs	7–17 years
Others	2–10 years

Amortization methods, useful lives, and residual values of intangible assets with definite useful lives are reviewed at the end of each reporting period and revised as necessary.

Leases

During the fiscal year ended March 31, 2020, the NEC Group has adopted IFRS 16 . Please also refer to Note 37. "Impact of Changes in Accounting Policies" for the details of change in accounting policies regarding IFRS 16.

The accounting policies applicable before April 1, 2019, for the fiscal years ended March 31, 2019

The NEC Group classifies a lease as a finance lease if it transfers substantially all the risks and rewards incidental to ownership to the NEC Group. Leases other than finance leases are classified as operating leases.

A leased asset or liability under a finance lease is measured at the lower of fair value of the leased asset or the present value of the minimum lease payments. Subsequently, the leased asset is depreciated over the shorter of the lease term or the economic useful life of the leased asset.

Minimum lease payments made under finance leases are allocated between finance costs and reduction of the remaining balance of the lease liability. The finance cost on the lease liability in each accounting period during the lease term are the amount that produces a constant periodic rate of interest on the remaining balance of the liability.
Lease payments made under an operating lease are recognized as an expense on a straight-line basis over the lease term.

The accounting policies applicable after April 1, 2019, for the fiscal year ended March 31, 2020

At inception of a contract, the NEC Group assesses whether the contract is, or contains, a lease. The NEC Group determines a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. In addition, the NEC Group elected not to recognize right-of-use assets and lease liabilities for either short-term leases with a lease term of 12 months or less or leases for which the underlying assets are of low value. The NEC Group recognizes the lease payments associated with those leases as an expense on a straight-line basis over their lease term.

As a lessee

At the commencement date of a lease, the NEC Group recognizes right-of-use assets that represent the right to use an underlying asset and a lease liability that represents its obligation to make lease payments. The lease liabilities are measured at the present value of the lease payments that are not paid at the commencement date. The lease payments are discounted using the interest rate implicit in the lease, if it is readily determinable, or otherwise, the lessee's incremental borrowing rate.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index or a rate, initially measured using the index or rate at the commencement date;
- amounts expected to be payable under a residual value guarantee;
- the exercise price under a purchase option that the NEC Group is reasonably certain to exercise; and
- penalties for early termination of a lease unless the NEC Group is reasonably certain not to terminate the lease early.

The lease liability is subsequently measured at amortized cost using the effective interest method, and is remeasured under certain circumstances, such as when there is a change in future lease payments arising from a change in an index or a rate, if there is a change in the NEC Group's estimate of the amount expected to be payable under a residual value guarantee, or if the NEC Group changes its assessment of whether it will exercise a purchase, extension or termination option.

The right-of-use assets are initially measured at the initial measurement amount of the lease liabilities adjusted for any prepaid lease payments before the commencement date and certain other items and are subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the underlying asset or the end of the lease term. The estimated useful lives of the underlying assets are determined on the same basis as those of property, plant and equipment. In addition, after the commencement date, the right-of-use asset is measured at cost less accumulated depreciation and accumulated impairment losses, and is adjusted for remeasurements of the lease liability. The right-of-use assets are presented as part of property, plant, and equipment, net.

Inventories

Inventories are measured at the lower of cost and net realizable value. The cost of inventories is determined principally by using the first-in first-out method or the periodic average method, whereas the cost of inventories of items that are not interchangeable is determined by using the specific identification of their individual cost. Cost of inventories comprises all costs of purchase, costs of production, costs of conversion, and other costs incurred in bringing the inventories to their present location and condition. Costs of finished goods and work in process include an allocation of production overheads that are based on the normal capacity of the production facilities. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

Impairment of Non-Financial Assets

Non-financial assets other than inventories, deferred tax assets, assets held for sale, assets arising from employee benefits and contract assets and assets recognized from costs to obtain a contract with a customer are assessed for indications of impairment at the end of each reporting period. This assessment is performed for an asset or a CGU, which is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. An impairment loss is recognized in profit or loss and the carrying amount is reduced to the recoverable amount. The recoverable amount is determined for an individual asset, or a CGU when the individual asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. The NEC Group's corporate assets do not generate independent cash inflows. If there is any indication that corporate assets may be impaired, the recoverable amount is estimated for the CGU to which the corporate assets belong. Corporate assets are assets other than goodwill that contribute to the future cash flows of both the CGU to which the corporate assets belong and other CGUs, and include land or buildings held by administrative departments.

The recoverable amount is the higher of the fair value of an asset or a CGU, less costs of disposal and its value in use. Value in use is calculated as the present value of the estimated future cash flows associated with the asset or CGU. In assessing value in use, the estimated future cash flows are discounted to the present value using a pre-tax discount rate, which reflects current market assessments of the time value of money and any risks specific to the asset or the CGU.

For goodwill and intangible assets with indefinite useful lives, the recoverable amount is estimated at the same time each year for the level of a CGU to which goodwill and intangible assets with indefinite lives have been allocated, and they are also tested for impairment whenever there is any indication of impairment.

An impairment loss recognized in prior periods for an asset other than goodwill is reversed if there is any indications that the loss recognized for the asset may no longer exist or may have decreased, and if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. Impairment losses are reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, had no impairment loss been recognized. Impairment losses on goodwill are not reversed.

Assets Held for Sale

A non-current asset or disposal group is classified as held for sale if its carrying amount will be recovered through a sale transaction rather than through its continuing use. The condition above is met only when the asset is available for immediate sale in its present condition and its sale is highly probable. If the NEC Group commits to a sale plan involving loss of control of a subsidiary, it classifies all the assets and liabilities of the subsidiary as held for sale when the criteria set out above are met, regardless of whether it will retain a non-controlling interest in its former subsidiary after the sale. Non-current assets or disposal groups classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell. Property, plant and equipment and intangible assets classified as held for sale are not depreciated or amortized.

Employee Benefits

Defined Benefit Plans

The NEC Group's defined benefit plans consist of defined benefit pension plans and lump-sum severance payment plans. For defined benefit plans, the present value of defined benefit obligations, less the fair value of plan assets is recognized as either liability or asset. Defined benefit obligations are measured separately for each plan by discounting estimated amount of future benefits employees have earned in return for their services in the current and prior periods to its present value. The discount rate is the yield at the reporting date on high-quality corporate bonds that is consistent with the currency and estimated terms of the NEC Group's post-employment benefit obligations. The NEC Group uses the projected unit credit method to determine the present value of defined benefit obligations, service cost, and the past service cost for each defined benefit obligation. Past service costs arising from a plan amendment or curtailment are recognized in profit or loss upon occurrence of the plan amendment or curtailment. Remeasurement of net defined benefit plans is recognized in full as other comprehensive income and not reclassified to retained earnings in subsequent periods.

Defined Contribution Pension Plans

Defined contribution pension plans are post-employment benefit plans under which the NEC Group pays fixed contributions to a separate entity (fund) and has no legal or constructive obligations to pay further amounts. Contributions to defined contribution pension plans are recognized as expense in profit or loss when the employees render related services.

Provisions

Provisions are recognized when the NEC Group has present legal or constructive obligations as a result of past events, it is probable that outflows of resources embodying economic benefits will be required to settle the obligations and reliable estimates can be made of the amount of the obligations.

Revenue

In accordance with IFRS 15, the following five-step approach is applied to recognize revenue, except for interest and dividend income within the scope of IFRS 9 and lease payments within the scope of IAS 17 or IFRS 16.

Step 1: Identify the contract with a customer
Step 2: Identify performance obligations in the contract
Step 3: Determine the transaction price
Step 4: Allocate the transaction price to each performance obligation in the contract
Step 5: Recognize revenue when (or as) each performance obligation is satisfied

Identifying Distinct Performance Obligations in Contracts with Customers

The NEC Group recognizes revenue from contracts with customers for contracts for hardware and packaged software deployments, for services to customers and for system integrations and equipment constructions. The NEC Group identifies distinct promised goods or services (i.e., performance obligations) within these contracts and accounts for revenue in accordance with their performance obligations. The NEC Group separately accounts for the good or service, if a promised good or service is distinct where the NEC Group's promise to transfer the good or service to the customer is separately identifiable from other promises in the contracts, and a customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer.

Determining the Transaction Price

The NEC Group considers the effects of variable consideration, constraining estimates of variable consideration, the existence of a significant financing component in the contract, non-cash consideration, and consideration payable to a customer when determining the transaction price. The NEC Group recognizes a variable consideration, which consists primarily of sales incentives that are offered to wholesalers and retailers as part of the NEC Group's sales promotion activities. When there is a possibility of subsequent variability in the consideration receivable from these customers, the variable consideration is estimated and included in revenue to the extent that it is highly probable that its inclusion will not result in a significant reversal in the amount of cumulative revenue recognized when the uncertainty has been subsequently resolved. When estimating the sales incentives, NEC Group uses the expected value method considering the historical experience of sales by customers and products. In assessing whether a contract contains a financing component and whether that financing component is significant to the contract, the NEC Group considers the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services. The NEC Group also considers the combined effect of the expected length of time between when it transfers the promised goods or services to the customer and when the customer pays for those goods or services and the prevailing interest rates in the relevant market.

Allocating the Transaction Price to Performance Obligation

The NEC Group allocates the transaction price to each performance obligation (or distinct good or service) in an amount that depicts the amount of consideration to which it expects to be entitled in exchange for transferring the promised goods or services to the customer. To allocate the transaction price to each performance obligation on a relative stand-alone selling price basis, the stand-alone selling price at contract inception of the distinct good or service underlying each performance obligation in the contract is determined and the transaction price is allocated in proportion to those stand-alone selling prices. A stand-alone selling price is estimated if it is not directly observable. For contracts for hardware and packaged software deployments, the NEC Group estimates stand-alone selling prices mainly based on adjusted market assessment approach. For contracts for services to customers and for system integrations and equipment constructions, the NEC Group estimates stand-alone selling price mainly based on expected cost plus a margin approach.

Satisfaction of Performance Obligation

The NEC Group recognizes revenue when or as the NEC Group satisfies a performance obligation at a point in time or over time by transferring a promised good or service to a customer.

The NEC Group recognizes revenue over time if one of the following criteria is met; i) the customer simultaneously receives and consumes the benefits provided by the NEC Group's performance as the NEC Group performs, ii) the NEC Group's performance creates or enhances an asset that the customer controls as the asset is created or enhanced, or iii) the NEC Group's performance does not create an asset with an alternative use to the NEC Group and it has an enforceable right to payment for performance completed to date. If none of the above is met, the NEC Group recognizes revenue at a point in time when it is determined that control of an asset is transferred to a customer.

Performance Obligations and Revenue Measurement Methods by Type of Goods or Services

Contracts for Hardware and Packaged Software Deployments

The major transactions regarding revenue from contracts for hardware and packaged software deployments are hardware (servers, mainframes, supercomputers, storage, business PCs, POS, ATMs, control equipment, wireless LAN routers), software (integrated operation management, application servers, security, database software), enterprise network solutions (IP telephony systems, WAN/wireless access equipment, LAN products), network infrastructure (core network, mobile phone base stations, optical transmission systems, routers / switches, mobile backhaul), system devices (displays, projectors) and lighting equipment.

The NEC Group recognizes revenue when control over goods is transferred to customers. To determine the point in time at which the control is transferred to the customer, the NEC Group considers whether or not a) the NEC Group has a present right to payment for the asset; b) the customer has legal title to the asset; c) the NEC Group has transferred physical possession of the asset; d) the customer has the significant risks and rewards related to the ownership of the asset; and e) the customer has accepted the asset. This transfer generally corresponds to the date of the inspection by the customer.

Revenue on Hardware requiring significant services, including installation, such as servers and network products, is in principle recognized upon the customer's acceptance. Revenue on standard Hardware, such as personal computers and electronic devices, is recognized in principle upon delivery, where the control of the Hardware is transferred to the customer.

Contracts for Services to Customers (Including Maintenance and Outsourcing)/Contracts for System Integrations and Equipment Constructions

The major transactions regarding revenue from contracts for services to customers/system integrations and equipment constructions are systems integration (systems implementation, consulting), safety (biometric solutions, surveillance and others), software & services for service providers (Operation Support System (OSS)/ Business Support System (BSS), Software-Defined Networking (SDN), Network Functions Virtualization (NFV)), services & management (OSS/BSS, and service solutions), network infrastructure (submarine systems), energy storage system, outsourcing/cloud services, data center infrastructure services and maintenance and support.

Supply of the above services usually corresponds to any of the following criteria: a) the customer simultaneously receives and consumes all of the benefits provided by the NEC Group as the NEC Group performs; b) the NEC Group's performance creates or enhances an asset that the customer controls as the asset is created; or c) the NEC Group's performance does not create an asset with an alternative use to the NEC Group and the NEC Group has an enforceable right to payment for performance completed to date and, therefore, is a performance obligation that is satisfied over time. If the progress toward complete satisfaction of the performance obligation can be reasonably measured, revenue from a service is recognized by measuring the progress. If the progress cannot be reasonably measured, revenue from a service is recognized only to the extent of the costs incurred if the NEC Group expects to recover the costs until such time that the outcome of the performance obligation can be reasonably measured.

Revenue for fixed price service contracts, including construction contracts is in principle recognized by the method of measuring the progress based on the costs incurred to date as a percentage of the total estimated project costs. When milestones for the obligations to be performed by the NEC Group are defined at contract inception, revenue is recognized based on completion of the contractual milestones.

Revenue on ongoing service contracts is recognized by measuring the progress based on the period of services already provided over the entire service period. Where outsourcing services are charged on a per unit basis, such as data usage, revenue is recognized when the service is provided. Where services are charged on a time period basis, revenue is recognized evenly over the period of the service contract. For maintenance, in principle revenue is recognized over the period in which the services are provided; however, where the contracts are charged on a time basis, revenue is recognized on a time and materials basis.

Where changes occur in the initial estimates of revenues, measure of progress, and costs incurred for a contract, the cumulative impact arising from a change of estimates is recognized in profit or loss in the period in which the changes become certain and possible to be estimated.

Contracts with Multiple Performance Obligations

Contracts with multiple performance obligations represent one contract that consists of several types of goods or services, such as supply of Hardware and related services or supply of software sales and support services. Goods or services promised to a customer are identified as a distinct performance obligation if the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e., the good or service is capable of being distinct); and the NEC Group's promise to transfer the goods or service to the customer is separately identifiable from other promises in the contract (i.e., the promise to transfer the good or service is distinct within the context of the contract).

The transaction price is allocated to each performance obligation on a relative stand-alone selling price basis, as mentioned above.

Methods for Measuring Progress

When revenue is recognized over time, the NEC Group measures the progress to depict the performance in transferring control of goods or services promised to a customer. Revenue is recognized for a performance obligation satisfied over time only if the progress can be reasonably measured as mentioned above. When the progress cannot be measured reasonably, revenue is recognized only to the extent of the costs incurred also as mentioned above.

Product Warranty

The NEC Group repairs or exchanges products for free of charge to honor warranty within the warranty period after the sale of products or delivery of developed software based on contracts. Product warranty liabilities are recognized for individually estimated future warranty costs using the historical ratio of warranty costs to net sales or other relevant factors, considering the additional incremental costs that are expected to be incurred. If a product warranty is purchased separately or purchased in addition to the standard warranty by a customer, the product warranty is identified as a separate performance obligation. The transaction price is allocated to the performance obligation and revenue is recognized for the allocated amount over a warranty period.

Contract Asset and Contract Liability

Contract asset is an entity's right to consideration in exchange for goods or services that the entity has transferred to a customer when that right is conditioned on something other than the passage of time (i.e., the entity's future performance) and contract liability is an entity's obligation to transfer goods or services to a customer for which the entity has received consideration or the amount is due from the customer. Advances received from construction contracts are recorded as "contract liabilities" in the consolidated statements of financial position.

Incremental Costs of Obtaining a Contract

An asset is recognized for the incremental costs of obtaining a contract with a customer if those costs are expected to be recovered. The incremental costs of obtaining a contract are those costs that the NEC Group incurs to obtain a contract with a customer that it would not have incurred if the contract had not been obtained. The costs are amortized on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the asset relates.

Income Taxes

Income tax expenses comprise current and deferred taxes, both of which are recognized in profit or loss, except for the tax arising from transactions which are recognized either directly in equity or other comprehensive income.

Current tax is the expected tax payable or receivable on taxable profit or tax losses for the reporting period, using tax rates and tax laws enacted or substantively enacted at the end of the reporting period.

Deferred taxes are calculated based on the temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, and unused tax losses carryforward at the end of the reporting period.

Deferred tax assets and liabilities are not recognized for the following temporary differences:

- Temporary differences on the initial recognition of an asset or liability in a transaction which is not a business combination and that affects neither accounting nor taxable profit nor loss;
- Temporary differences arising from investments in subsidiaries, associates, and joint arrangements to the extent that it is probable that the temporary difference will not reverse in the foreseeable future; and
- Taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax assets and liabilities are measured using the tax rates that are expected to apply to the period in which the temporary differences are expected to reverse based on the tax rates and tax laws that have been enacted or substantively enacted at the end of the reporting period.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and the deferred tax assets and liabilities are for those related to income taxes levied by the same taxation authority on the same taxable entity.

A deferred tax asset is recognized for the carryforward of unused tax losses, and deductible temporary differences to the extent that it is probable that future taxable profit will be available against which they can be utilized.
The amount of deferred tax assets is reduced to the extent that it is no longer probable that future taxable income would be sufficient to allow the benefit of part or all of the deferred tax asset to be utilized.

Share Capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of ordinary shares are recognized as a deduction from equity.

Treasury shares are measured at cost and deducted from equity. When NEC Group sells the treasury shares subsequently, the difference between the carrying amount and the consideration received is recognized in share premium. Additional costs directly related to repurchase or sale of treasury shares are deducted from equity.

4. Use of Accounting Estimates and Judgments

The preparation of consolidated financial statements in accordance with IFRS requires management to make certain judgments, estimates, and assumptions that affect the application of policies and reported amounts of assets, liabilities, revenues, and expenses. These estimates and assumptions may differ from the actual results.

These estimates and underlying assumptions are reviewed by management on a continuous basis. Changes in these accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

The NEC Group has assessed the impact of significant uncertainty introduced by the COVID-19 pandemic on its accounting estimates and judgments based upon the information currently available. The areas for which the estimate of potential effects of the COVID-19 and various governments' counter-measures on future macroeconomic conditions was of particular importance as of March 31, 2020, are the recoverable amount in the impairment testing of non-financial assets, and the recoverability of deferred tax assets. Given the uncertainties associated with the nature of the COVID-19 pandemic, it is extremely difficult to estimate the ultimate impact of the outbreak. While the NEC Group's operating results may be temporarily adversely impacted, management has determined that the impact of the COVID-19 pandemic on the NEC Group's long-term operating results would not be significant, considering the business environment in the ICT industry in which the NEC Group operates, where the management of the NEC Group expects a strong demand for investments in IT infrastructures, such as DX (Digital Transformation) in response to coming changes in society after the COVID-19 crisis. While there was not a material impact to the consolidated financial statements as of and for the fiscal year ended March 31, 2020, as events continue to evolve and additional information becomes available, actual results and outcomes in future reporting periods may differ materially from the managements of the NEC Group's estimates.

Information about judgments and estimates that have been made in the process of applying accounting policies and that have significant effects on the amounts reported in the consolidated financial statements, and information about accounting estimates and assumptions that have significant effects on the amounts reported in the consolidated financial statements, are as follows:

- Fair Value of Financial Instruments (Note 31)
- Recoverable Amount in Impairment Test of Non-financial Assets (Note 10)
- Actuarial Assumptions of Post-retirement Benefits (Note 22)
- Recognition and Measurement of Provisions (Note 23)
- Revenue Recognition (Note 26)
- Recoverability of Deferred Tax Assets (Note 13)
- Identification of Lease and Determination of Lease Term (Note 32)
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5. New Accounting Standards and Interpretations Issued and Not Yet Adopted

Of the new or amendments to IFRS standards that have been issued but are not effective as of the date of the approval of the consolidated financial statements of the NEC Group, none is expected to have material effects on the NEC Group's financial position or results of operations.

6. Segment Information

The NEC Group has six reportable segments: Public Solutions business, Public Infrastructure business, Enterprise business, Network Services business, System Platform business and Global business, all of which are operating segments. Operating segments are defined as the components of the NEC Group for which separate financial information is available that is evaluated regularly by the board of directors of NEC, which is the NEC Group's chief operating decision maker in deciding how to allocate resource and in assessing performance. The NEC Group's various operations are organized into the following six operating segments based primarily on the characteristics of the customers served, and into other business activities that provide products and services such as data center solutions and security solutions to customers:

Public Solutions business provides system integration and development services mainly to local and regional government entities, medical institutions and medium-sized enterprises in Japan.

Public Infrastructure business provides primarily system integration and development services, satellites and satellite management services, sensors and air traffic management systems and broadcasting systems to Japanese national-level government organizations and enterprises in the aerospace, defense and media industries that support national and social infrastructures primarily in Japan.

Enterprise business mainly provides system integration and development services, including consulting, design and implementation, system maintenance and support services, and system outsourcing and cloud services, as well as related equipment, to business enterprises especially in the manufacturing, retail and services, and financial sectors primarily in Japan.

Network Services business mainly provides mobile phone network base stations, fixed and mobile phone networks and other ICT solutions to customers in the telecommunications market primarily in Japan.

System Platform business mainly provides both non-customized and customized hardware, such as servers, mainframes, storage devices, wireless LAN routers and personal computers, and software products as well as maintenance services to government agencies and business enterprises primarily in Japan.

Global business mainly provides *"Safer Cities"*—public safety solutions, software services for service providers, network infrastructure, system devices and energy storage solutions in overseas markets outside of Japan.

Changes to reportable segments and matters related to measurement for segment profit or loss

Effective April 1, 2019, the NEC Group has changed its internal organization and the composition of its current operating segments, which resulted in a change in reporting segments. Major changes to the reportable segments include a transfer of Enterprise Network Solutions from "System Platform" segment to "Network Services" segment. Also, NEC's "Public Solutions Business" which is responsible for business involving regional sales functions and regional government entities in Japan, and its "Public Infrastructure Business" which is in charge of business involving government organizations and enterprises supporting national and social infrastructure, were consolidated into the "Public Business" segment because their economic characteristics, products and services were generally similar. NEC has split each business unit into separate reportable segments, the "Public Solutions Business" segment and the "Public Infrastructure Business" segment. In addition, from the fiscal year ended March 31, 2020, segment profit (loss) is measured by deducting amortization expenses on intangible assets recognized as a result of mergers and acquisitions ("M&A") and M&A-related expenses (financial advisory fee and other fees.) from selling, general and administrative expenses and other operating expenses for the respective segments. The new "segment profit (loss)" is an indicator for measuring underlying profitability in order to clarify the contribution of acquired companies to NEC's overall earnings. Intersegment sales revenues are made at amount that approximates arm's-length prices.

Segment information on revenue, profit or loss and other metrics by reportable segment reflecting above changes retrospectively for the fiscal year ended March 31, 2019, and segment information on revenue, profit or loss and other metrics by reportable segment for the fiscal year ended March 31, 2020, are as follows:

Fiscal year ended March 31, 2019

JPY (millions)

	Reportable segments									
	Public Solutions	Public Infrastructure	Enterprise	Network Services	System Platform	Global	Total	Others	Reconciling items	Consolidated total
Revenue:										
External customers	286,151	621,879	431,801	460,307	500,213	409,369	2,709,720	203,726	–	2,913,446
Intersegment	7,739	7,772	10,634	11,475	49,207	2,488	89,315	95,393	(184,708)	–
Total	293,890	629,651	442,435	471,782	549,420	411,857	2,799,035	299,119	(184,708)	2,913,446
Segment profit (loss)	7,239	45,358	35,807	20,677	20,078	(22,517)	106,642	18,955	(55,670)	69,927
Amortization of acquisition-related intangible assets										(10,384)
M&A related expenses										(1,763)
Operating profit										57,780
Finance income										21,989
Finance costs										(8,377)
Share of profit of entities accounted for using the equity method										5,916
Profit before income taxes										77,308
Other items:										
Depreciation and amortization	3,863	33,226	4,558	7,597	14,260	14,248	77,752	16,063	5,930	99,745
Impairment loss	164	136	34	–	1,465	4,900	6,699	463	5,445	12,607
Capital expenditures	3,979	40,302	10,066	10,754	18,964	26,844	110,909	17,710	21,749	150,368

Fiscal year ended March 31, 2020

JPY (millions)

	Reportable segments									
	Public Solutions	Public Infrastructure	Enterprise	Network Services	System Platform	Global	Total	Others	Reconciling items	Consolidated total
Revenue:										
External customers	324,608	631,140	455,508	509,832	548,692	493,761	2,963,541	131,693	–	3,095,234
Intersegment	7,443	6,095	8,976	16,897	52,353	732	92,496	89,656	(182,152)	–
Total	332,051	637,235	464,484	526,729	601,045	494,493	3,056,037	221,349	(182,152)	3,095,234
Segment profit (loss)	18,602	53,857	37,154	38,207	48,859	(3,752)	192,927	9,374	(56,503)	145,798
Amortization of acquisition-related intangible assets										(16,968)
M&A related expenses										(1,221)
Operating profit										127,609
Finance income										8,477
Finance costs										(15,464)
Share of profit of entities accounted for using the equity method										3,347
Profit before income taxes										123,969
Other items:										
Depreciation and amortization	3,850	40,443	6,743	9,516	16,922	27,876	105,350	42,882	18,128	166,360
Impairment loss	679	83	23	1,789	382	2,841	5,797	586	1	6,384
Reversal of impairment loss	–	–	–	–	–	–	–	(150)	–	(150)
Capital expenditures	6,228	46,187	10,754	17,156	18,949	57,703	156,977	33,214	19,248	209,439

"Others" mainly includes businesses such as data center service and lighting equipment for the fiscal year ended March 31, 2019, and data center service and security for the fiscal year ended March 31, 2020. "Reconciling items" in segment profit (loss) includes amounts not allocated to each reportable segment that consist principally of corporate expenses of 55,105 million JPY and 60,769 million JPY for the fiscal years ended March 31, 2019, and 2020, respectively. Corporate expenses mainly include general and administrative expenses and research and development expenses incurred at the headquarters of NEC.

Geographical information

Revenues from contract with customers by country or region for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Japan	2,224,345	2,343,260
North America and Latin America	174,385	164,075
Europe, Middle East, and Africa	161,094	234,097
China, East Asia, and Asia Pacific	353,622	353,802
Total	2,913,446	3,095,234

Non-current assets other than financial instruments, deferred tax assets, and net defined benefit assets by country/region as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Japan	544,289	670,192
North America and Latin America	39,836	43,141
Europe, Middle East, and Africa	232,517	228,515
China, East Asia, and Asia Pacific	15,110	15,131
Total	831,752	956,979

Goodwill of 86,940 million JPY and 82,387 million JPY as of March 31, 2019 and 2020, respectively recognized as a result of the acquisition of KMD Holding ApS ("KMD") during the fiscal year ended March 31, 2019, was included in Denmark, which is part of, Europe, Middle East, and Africa.

Major customers

The NEC Group does not have any external customers that comprise more than 10% of revenue in the consolidated statements of profit or loss.

7. Business Combinations

Acquisitions during the fiscal year ended March 31, 2019

On February 21, 2019, NEC completed an acquisition of 100% of the outstanding shares of KMD in cash of 48,377 million JPY. KMD is a Danish IT company, which provides software solution and maintenance services mainly to government offices. The acquisition enables the NEC Group to accelerate the expansion of safety business in Europe and globally. The Company incurred acquisition-related costs of 1,128 million JPY related to the share acquisition. These costs were included in selling, general and administrative expenses in the consolidated statement of profit or loss.

The fair value of assets acquired and liabilities assumed at the acquisition date is as follows:

JPY (millions)

	Amount
Cash and cash equivalents	3,104
Trade and other receivables	9,604
Other current assets	6,933
Property, plant and equipment	2,181
Intangible assets	73,769
Other non-current assets	911
Trade and other payables	(9,396)
Other current liabilities	(22,535)
Other financial liabilities-non-current	(79,365)
Other non-current liabilities	(24,655)
Total identifiable net liabilities assumed	(39,449)

Trade and other receivables comprise gross contractual amounts due of 9,655 million JPY, of which 51 million JPY was expected to be uncollectable at the date of acquisition.

Goodwill arising from the acquisition is as follows:

JPY (millions)

	Amount
Consideration for the acquisition	48,377
Fair value of identifiable net liabilities assumed by the NEC Group	39,449
Goodwill arising from acquisition	87,826

The goodwill is attributable mainly to the synergies expected to be achieved from integrating the acquiree into the NEC Group's existing "Safer Cities" business. There is no goodwill recognized that is expected to be deductible for tax purposes.

Since the acquisition date, KMD contributed revenue of 6,617 million JPY and net profit of 120 million JPY to the NEC Group's results for the year ended March 31, 2019. Had the acquisition occurred on April 1, 2018, consolidated revenue would have been 2,995,268 million JPY, and consolidated net profit for the year would have been 39,909 million JPY.

Acquisitions during the fiscal year ended March 31, 2020

There are no business combinations that are considered material to the NEC Group.

8. Property, Plant and Equipment

Reconciliation of the carrying amounts, cost, accumulated depreciation and accumulated impairment losses of property, plant and equipment for the fiscal years ended March 31, 2019 and 2020, is as follows:

JPY (millions)

Carrying amounts	Buildings and structures	Machinery and equipment	Tools, furniture and fixtures	Land	Construction in progress	Right-of-use assets	Total
As of April 1, 2018	181,508	46,319	83,038	68,794	19,931	–	399,590
Acquisitions	6,148	2,625	6,475	392	47,048	–	62,688
Acquisitions through business combinations	846	123	1,174	38	–	–	2,181
Reclassifications	8,646	10,438	38,618	(32)	(34,834)	–	22,836
Depreciation	(14,445)	(12,592)	(37,368)	–	–	–	(64,405)
Impairment losses	(3,953)	(256)	(1,856)	(1,509)	(128)	–	(7,702)
Disposals	(1,205)	(862)	(763)	(764)	(2,917)	–	(6,511)
Foreign currency translation adjustments	65	(31)	26	51	33	–	144
As of March 31, 2019	177,610	45,764	89,344	66,970	29,133	–	408,821
Impact of changes in accounting policies	(772)	(126)	(3,221)	–	–	179,818	175,699
Beginning balance as adjusted	176,838	45,638	86,123	66,970	29,133	179,818	584,520
Acquisitions	3,338	3,239	8,145	175	52,528	31,000	98,425
Reclassifications	25,191	10,058	38,642	(923)	(54,084)	–	18,884
Depreciation	(15,439)	(12,228)	(41,766)	–	–	(53,917)	(123,350)
Impairment losses	(918)	(23)	(687)	(982)	(132)	(559)	(3,301)
Reversal of impairment loss	–	–	–	150	–	–	150
Disposals	(629)	(553)	(1,301)	(273)	(4,738)	(3,410)	(10,904)
Transfer to assets held for sale	(425)	(1,072)	(513)	(725)	(111)	(1,089)	(3,935)
Foreign currency translation adjustments	(270)	(342)	(516)	(28)	(95)	(1,161)	(2,412)
As of March 31, 2020	187,686	44,717	88,127	64,364	22,501	150,682	558,077

JPY (millions)

Cost	Buildings and structures	Machinery and equipment	Tools, furniture and fixtures	Land	Construction in progress	Right-of-use assets	Total
As of April 1, 2018	545,067	258,411	419,497	75,255	19,943	–	1,318,173
As of March 31, 2019	550,115	249,618	427,384	75,373	29,133	–	1,331,623
As of March 31, 2020	558,814	241,499	420,597	72,768	22,608	206,338	1,522,624

JPY (millions)

Accumulated Depreciation and Accumulated impairment losses	Buildings and structures	Machinery and equipment	Tools, furniture and fixtures	Land	Construction in progress	Right-of-use assets	Total
As of April 1, 2018	363,559	212,092	336,459	6,461	12	–	918,583
As of March 31, 2019	372,505	203,854	338,040	8,403	–	–	922,802
As of March 31, 2020	371,128	196,782	332,470	8,404	107	55,656	964,547

The "Reclassifications" in the table above for the fiscal years ended March 31, 2019 and 2020, includes the transfer from inventories under current assets.

Carrying amounts of leased assets under finance leases included within property, plant and equipment as of March 31, 2019, were as follows:

	JPY (millions)
	2019
Buildings and structures	772
Machinery and equipment	126
Tools, furniture and fixtures	3,221
Total	4,119

Pledged assets as of March 31, 2019 and 2020, were as follows:

	JPY (millions)	
	2019	2020
Land	3,417	128
Others	828	666
Total	4,245	794

Impairment losses

Impairment losses are included in other operating expenses in the consolidated statements of profit or loss. The aggregate amount of impairment losses is disclosed in Note 10 "Impairment Losses of Non-Financial Assets."

During the fiscal year ended March 31, 2019, the NEC Group recorded impairment losses of 3,584 million JPY mainly over buildings and structures, machinery and equipment, tools, furniture and fixtures, and land in the corporate research facilities. The losses are included in corporate expenses, and are not allocated to any reportable segment. The recoverable amount was measured based on the fair value less costs of disposal. As the assets were measured using the significant unobservable inputs such as discount rate, terminal capitalization rate, and average rent growth rate, their fair value measurements are classified as Level 3 in the fair value hierarchy.

During the fiscal year ended March 31, 2020, the NEC Group recorded impairment losses of 1,788 million JPY mainly over buildings and structures, tools, furniture and fixtures, and land in training facilities. The losses are allocated to Network Services segment. The recoverable amount was measured based on the fair value less costs of disposal. As the assets were measured using the significant unobservable inputs such as discount rate, terminal capitalization rate, and average rent growth rate, their fair value measurements are classified as Level 3 in the fair value hierarchy.

As a result of the assessment of the impact of uncertainties introduced by the COVID-19 pandemic, the management of the NEC Group has determined that the impact of the COVID-19 pandemic on the NEC Group's long-term financial results would not be significant, given the business environment of the ICT industry in which the NEC Group operates, and accordingly there was not a material impact on the determination of the recoverable amounts at March 31, 2020.

9. Intangible Assets including Goodwill

Reconciliation of the carrying amounts, cost, accumulated amortization and accumulated impairment losses of intangible assets including goodwill for the fiscal years ended March 31, 2019 and 2020, is as follows:

JPY (millions)

Carrying amount	Goodwill	Software for sale	Software for internal use	Customer relationship	Acquired capitalized development costs	Other	Total
As of April 1, 2018	103,967	24,176	57,613	24,557	29,806	20,096	260,215
Acquisitions	–	7,252	8,293	–	–	2,564	18,109
Acquisitions through business combinations	89,267	24,154	1,121	48,424	–	71	163,037
Reclassifications	–	15,948	9,352	–	–	3,552	28,852
Amortization	–	(20,787)	(22,211)	(3,841)	(4,078)	(3,342)	(54,259)
Impairment losses	(2,941)	–	(709)	–	–	(971)	(4,621)
Disposals	–	(886)	(1,053)	–	–	(731)	(2,670)
Foreign currency translation adjustments	(2,110)	(299)	(12)	(357)	(337)	(429)	(3,544)
Other	–	722	963	–	–	(40)	1,645
As of March 31, 2019	188,183	50,280	53,357	68,783	25,391	20,770	406,764
Acquisitions	–	9,244	13,057	–	–	1,010	23,311
Acquisitions through business combinations	5,788	–	–	–	881	–	6,669
Reclassifications	–	13,670	12,931	–	–	1,608	28,209
Amortization	–	(24,250)	(23,198)	(11,899)	(4,116)	(2,171)	(65,634)
Impairment losses	(611)	(87)	(1,773)	–	–	(94)	(2,565)
Disposals	–	(264)	(542)	–	–	(109)	(915)
Foreign currency translation adjustments	(10,340)	(775)	(165)	(2,447)	(1,047)	(466)	(15,240)
Other	(686)	358	1,308	–	–	(152)	828
As of March 31, 2020	182,334	48,176	54,975	54,437	21,109	20,396	381,427

JPY (millions)

Cost	Goodwill	Software for sale	Software for internal use	Customer relationship	Acquired capitalized development costs	Other	Total
As of April 1, 2018	112,287	106,862	141,193	36,089	34,957	35,252	466,640
As of March 31, 2019	199,444	132,119	133,575	84,648	34,788	37,202	621,776
As of March 31, 2020	194,206	136,813	134,887	81,701	34,205	35,792	617,604

JPY (millions)

Accumulated amortization and accumulated impairment losses	Goodwill	Software for sale	Software for internal use	Customer relationship	Acquired capitalized development costs	Other	Total
As of April 1, 2018	8,320	82,686	83,580	11,532	5,151	15,156	206,425
As of March 31, 2019	11,261	81,839	80,218	15,865	9,397	16,432	215,012
As of March 31, 2020	11,872	88,637	79,912	27,264	13,096	15,396	236,177

The "Reclassifications" in the table above for the fiscal years ended March 31, 2019 and 2020, includes the transfer from inventories under current assets.

Internally generated intangible assets mainly consist of software for sale and software for internal use. Amortization is recognized either as selling, general and administrative expenses or as cost of sales when the amortization expenses have been allocated to the cost of inventories and those inventories are sold. The NEC Group does not have capitalized research and development costs. Research and development costs recognized as expenses during the fiscal years ended March 31, 2019, and 2020, are 108,141 million JPY and 109,787 million JPY, respectively.

The Company acquired KMD on February 21, 2019, and recognized goodwill and intangible assets in the total amount of 161,595 million JPY. This amount is mainly included in "Goodwill," "Software for sale," and "Customer relationship" presented above as acquisitions through business combinations.

The carrying amounts of goodwill allocated to each operating segment as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Public Infrastructure	6,171	6,150
Enterprise	3,516	3,493
Network Services	551	551
System Platform	2,720	2,720
Global	147,426	137,921
Others	27,799	31,499
Total	188,183	182,334

The CGUs to which significant amounts of goodwill are allocated as of March 31, 2019 and 2020, are as follows:

JPY (millions)

CGUs	2019	2020
KMD	86,940	82,387
NPS	41,475	39,051
Others	59,768	60,896
Total	188,183	182,334

The NEC Group recognized impairment losses due to the lower profitability than initially expected for certain of its goodwill and intangible assets. Impairment losses are included in other operating expenses in the consolidated statements of profit or loss. The aggregate amount of impairment losses is disclosed in Note 10. "Impairment Losses of Non-Financial Assets." NPS and KMD were both newly acquired in recent years, and based on its assessment of their profitability compared with the initially developed business plans, management considers there is no significant impairment risk associated with goodwill allocated to NPS and KMD.

During the fiscal years ended March 31, 2019, the NEC Group recorded impairment losses of 2,941 million JPY due to the impairment of goodwill in the IT services business subsidiaries. The losses are allocated to the "Global" segment. The recoverable amount of the assets was calculated based on the value in use. Value in use is calculated by discounting the estimated future cash flows based on a five-year business plan and the terminal value to the present value. The growth rate used for estimating the terminal value of each CGU is determined by considering the status of the respective country and industry that the CGU belongs to, and it does not exceed the long-term average growth rate of the industry of the CGU. The growth rate used to calculate the recoverable amount was 2.0% and the discount rate used to calculate the recoverable amount was 16.0% for the years ended March 31, 2019.

The significant assumptions used to calculate the recoverable amount (value in use) for the fiscal years ended March 31, 2019, and 2020, are as follows:

	2019	2020
Growth Rate	0.0 to 2.0 %	0.0 to 2.0 %
Discount Rate (Pre-tax)	5.3 to 16.0 %	5.2 to 15.3 %

The NEC Group considers, except for CGUs of which impairment losses are recognized for the fiscal years ended March 31, 2019 and 2020, that it is less likely that a significant impairment occurs even when the discount rate and growth rate, which are significant assumptions used for impairment testing of goodwill, have changed to a reasonable extent.

As a result of the assessment of the impact of uncertainties introduced by the COVID-19 pandemic, the management of the NEC Group has determined that the impact of the COVID-19 pandemic on the NEC Group's long-term financial results would not be significant, given the business environment of the ICT industry in which the NEC Group operates, and accordingly there was not a material impact on the determination of the recoverable amounts at March 31, 2020.

10. Impairment Losses of Non-Financial Assets

A breakdown of impairment losses and subsequent reversals by asset class for the fiscal years ended March 31, 2019, and 2020, is as follows:

JPY (millions)

	2019		2020	
	Impairment loss	Reversal	Impairment loss	Reversal
Property, plant and equipment				
Buildings and structures	3,953	–	918	–
Machinery and equipment	256	–	23	–
Tools, furniture and fixtures	1,856	–	687	–
Land	1,509	–	982	(150)
Construction in progress	128	–	132	–
Right-of-use assets	–	–	559	–
Goodwill	2,941	–	611	–
Intangible asset				
Software for internal use	709	–	1,773	–
Others	1,255	–	699	–
Total	12,607	–	6,384	(150)

Impairment losses and reversal of impairment loss are included in other operating expenses in the consolidated statements of profit or loss. Details of impairment losses are described in Note 8. "Property, Plant and Equipment" for property, plant and equipment, and Note 9. "Intangible Assets including Goodwill" for goodwill and intangible assets.

11. Subsidiaries

Material subsidiaries

The number of consolidated subsidiaries increased by 12 in the fiscal year ended March 31, 2020, primary due to establishments and acquisitions and decreased by 39 primarily due to divestitures.

Major consolidated subsidiaries as of March 31, 2020, are as follows:

Name of entity	Country of incorporation	Ownership of voting rights (%)	Principal activities
Japan Aviation Electronics Industry, Limited	Japan	50.9	Manufacturing and sale of connectors and electronic devices for aircraft, satellites and spacecraft
ABeam Consulting Ltd.	Japan	100.0	Management consulting, business process consulting, and IT consulting and outsourcing
NEC Networks & System Integration Corporation	Japan	51.5	Design, construction and maintenance of information and communications systems, installation of telecommunications systems, and sale of information and communications equipment
NEC Platforms, Ltd.	Japan	100.0	Development, manufacturing, sale and maintenance of information and communications systems, equipment, and provision of system integration services
NEC Corporation of America	U.S.A.	100.0	Regional representative and supervising operations in North America, sale of computer-related equipment and communications equipment, and provision of system integration services
NEC Europe Ltd.	U.K.	100.0	Regional representative and supervising operations in Europe
NEC Asia Pacific Pte. Ltd.	Singapore	100.0	Regional representative and supervising operations in Asia, sale of computer-related equipment and communications equipment, and provision of system integration services
NEC (China) Co., Ltd.	China	100.0	Regional representative and supervising operations in Greater China
NEC Latin America S.A.	Brazil	100.0	Regional representative and supervising operations in Latin America, sale of communications equipment, and provision of system integration services
KMD A/S	Denmark	100.0	Software development and IT services
Northgate Public Services (UK) Limited.	U.K.	100.0	IT services

Subsidiaries that have non-controlling interests material to NEC

NEC Networks & System Integration Corporation

NEC Networks & System Integration Corporation is a subsidiary that has non-controlling interest material to NEC. Proportion of ownership interests held by non-controlling interests as of March 31, 2019 and 2020 were 61.4%, which is inclusive of the interest in the subsidiary held in the retirement benefit trust acting as an agent of NEC. Proportion of voting rights held by non-controlling interests as of March 31, 2019 and 2020 were 48.5%.

Summarized financial information before eliminating inter-company transactions as of March 31, 2019, and 2020, is as follows:

	JPY (millions)	
	2019	2020
Current assets	181,377	192,501
Non-current assets	36,150	46,735
Current liabilities	72,723	82,325
Non-current liabilities	42,005	47,308
Net assets	102,799	109,603
Carrying amount of non-controlling interests	62,303	67,024

Summarized financial information before eliminating inter-company transactions for the fiscal years ended March 31, 2019, and 2020, is as follows:

	JPY (millions)	
	2019	2020
Revenue	278,102	302,253
Net profit	9,458	11,805
Other comprehensive income	(366)	339
Comprehensive income	9,092	12,144
Net profit allocated to non-controlling interests	4,513	6,898
Dividends paid to non-controlling interests	2,287	2,460
Cash flows from operating activities	8,396	14,939
Cash flows from investing activities	(5,604)	(6,726)
Cash flows from financing activities	(5,615)	(4,304)
Effect of exchange rate changes on cash and cash equivalents	(104)	58
Net (decrease) increase in cash and cash equivalents	(2,927)	3,967
Cash and cash equivalents, at end of reporting period	54,354	58,321

Japan Aviation Electronics Industry, Limited

Japan Aviation Electronics Industry, Limited ("JAE") is a subsidiary that has non-controlling interest material to NEC. The figures below reflect changes that occurred after the acquisition date. Proportion of ownership interests held by non-controlling interests as of March 31, 2019 and 2020 were 64.3%, which is inclusive of the interest in the subsidiary held in the retirement benefit trust acting as an agent of NEC. Proportion of voting rights held by non-controlling interests as of March 31, 2019 and 2020 were 49.1%.

Summarized financial information before eliminating inter-company transactions as of March 31, 2019 and 2020, is as follows:

	JPY (millions)	
	2019	2020
Current assets	108,657	113,559
Non-current assets	120,491	123,374
Current liabilities	48,483	52,647
Non-current liabilities	18,800	18,206
Net assets	161,865	166,080
Carrying amount of non-controlling interests	104,368	107,030

Summarized financial information before eliminating inter-company transactions for the fiscal years ended March 31, 2019, and 2020, is as follows:

	JPY (millions)	
	2019	2020
Revenue	222,358	208,237
Net profit	12,824	11,255
Other comprehensive income	41	(3,314)
Comprehensive income	12,865	7,941
Net profit allocated to non-controlling interests	7,396	6,290
Dividends paid to non-controlling interests	1,752	2,337
Cash flows from operating activities	37,627	29,685
Cash flows from investing activities	(23,042)	(24,536)
Cash flows from financing activities	(6,891)	(7,565)
Effect of exchange rate changes on cash and cash equivalents	134	(389)
Net increase (decrease) in cash and cash equivalents	7,828	(2,805)
Cash and cash equivalents, at end of reporting period	47,608	44,802

12. Investments Accounted for Using the Equity Method

Investments in associates and joint ventures are accounted for using the equity method. The number of associates accounted for using the equity method increased by six in the fiscal year ended March 31, 2020, due to new investments and decreased by four due to divestiture. There is no change in the number of joint ventures accounted for using the equity methods for the fiscal year ended March 31, 2020.

Associates

Material associates

NEC Capital Solutions Limited is the only associate, which is material to the NEC Group as of March 31, 2020. NEC Capital Solutions Limited engages in leasing various types of equipment, facilities, and products in Japan. The Company owns 37.7% of the voting rights as of March 31, 2019 and 2020.

Summarized financial information as of March 31, 2019 and 2020, is as follows:

JPY (millions)

	2019	2020
Current assets	768,549	870,638
Non-current assets	121,777	152,196
Current liabilities	414,038	444,073
Non-current liabilities	365,715	468,188
Total equity	110,573	110,573

Summarized financial information for the fiscal years ended March 31, 2019, and 2020, is as follows:

JPY (millions)

	2019	2020
Revenue	517,983	64,531
Net profit	10,852	5,449
Other comprehensive income	(409)	(28)
Comprehensive income	10,443	5,421
Dividends received from the associate	430	486

Reconciliation between the summarized financial information and the carrying amount of interests in associates as of March 31, 2019 and 2020, is as follows:

JPY (millions)

	2019	2020
Equity attributable to owners of the investee	93,523	97,280
Proportion of ownership interest	37.7%	37.7%
Equity attributable to the NEC Group	35,230	36,645
Elimination of unrealized profit on inter-company transactions	(21)	(25)
Carrying amount of the associate in the consolidated financial statements	35,209	36,620
Fair value of the associate	13,803	14,922

Aggregate information of associates that are not individually material for the fiscal years ended March 31, 2019, and 2020, is as follows:

JPY (millions)

	2019	2020
Aggregate carrying amount of individually immaterial associates in the consolidated financial statements	36,838	36,085
Aggregate amounts of the NEC Group's share of those associates:		
Net profit	3,178	1,553
Other comprehensive income	19	(254)
Comprehensive income	3,197	1,299

Unrecognized share of losses of associates accounted for using the equity method which the Company has stopped recognizing its share of losses for the fiscal years ended March 31, 2019, and 2020, was as follows:

JPY (millions)

	2019	2020
Unrecognized share of losses of associates for the period	–	–
Accumulated unrecognized share of losses of associates	638	538

Joint ventures

None of joint ventures are material to the NEC Group.

Aggregate information of joint ventures that are not individually material for the fiscal years ended March 31, 2019, and 2020, is as follows:

JPY (millions)

	2019	2020
Aggregate carrying amount of individually immaterial joint ventures in the consolidated financial statements	374	1,387
Aggregate amounts of the NEC Group's share of those joint ventures:		
Net profit (loss)	(251)	(75)
Other comprehensive income	–	–
Comprehensive income	(251)	(75)

Unrecognized share of losses of joint ventures that the Company has stopped recognizing its share of losses in applying the equity method for the fiscal years ended March 31, 2019, and 2020, was as follows:

JPY (millions)

	2019	2020
Unrecognized share of losses of joint ventures for the period	199	–
Accumulated unrecognized share of losses of joint ventures	199	–

13. Income Taxes

Current and deferred tax expenses

The components of income tax expenses for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Current tax expense		
Current year	18,145	25,839
Adjustments for current tax of prior periods	605	(420)
Subtotal	18,750	25,419
Deferred tax expense		
Origination and reversal of temporary differences	9,094	10,286
(Recognition of previously unrecognized) / derecognition of previously recognized tax losses	(1,131)	9,825
(Recognition of previously unrecognized) / derecognition of previously recognized deductible temporary differences	(1,335)	(34,280)
Subtotal	6,628	(14,169)
Income taxes	25,378	11,250

The Company and its subsidiaries in Japan are mainly subject to Japanese national and local income taxes, inhabitant tax, and enterprise tax. The statutory tax rates in Japan for the fiscal years ended March 31, 2019, and 2020, are 30.5%, and 30.5%, respectively. The foreign subsidiaries are subject to taxes based on income at rates ranging from 0.0% to 34.9%.

Reconciliation between the Japanese statutory income tax rate and the effective tax rate of the Company for the fiscal years ended March 31, 2019, and 2020, is as follows:

(%)

	2019	2020
Statutory tax rate	30.5	30.5
Movement in tax rate		
Effects of undistributed earnings	7.1	0.3
Effects of investments accounted for using the equity method	(1.9)	(0.9)
Non-deductible expenses	1.1	1.3
Differences in tax rates applied to foreign subsidiaries	0.3	1.3
(Recognition or use of previously unrecognized) / Derecognition of previously recognized tax losses	(1.5)	4.0
(Recognition of previously unrecognized) / derecognition of previously recognized deductible temporary differences	(1.7)	(30.0)
Others	(1.1)	2.6
Effective tax rate	32.8	9.1

As a result of the assessment of the recoverability of deferred tax assets, due to an improved long-term prospect of its ability to generate future taxable profit which is reflected in the improvement in the NEC Group's operating results for the fiscal year ended March 31, 2020, despite the adverse impact of significant uncertainty caused by the COVID-19 pandemic, the effective tax rate for the fiscal year ended March 31, 2020 became lower than the statutory tax rate. The decrease in the effective tax rate was mainly due to the recognition of deferred tax assets for previously unrecognized deductible temporary differences.

Deferred taxes

Major components of deferred tax assets and liabilities as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	As of April 1, 2018	Changes in accounting policies	Recognized through profit or loss	Recognized in other comprehensive income	Acquisitions by business combinations	As of March 31, 2019
Deferred tax assets:						
Accrued expenses and product warranty liabilities	31,455	–	2,329	–	–	33,784
Write-off of inventories	24,626	–	(2,068)	–	–	22,558
Depreciation	16,688	–	(3,006)	–	–	13,682
Elimination of unrealized profit from intercompany transactions among consolidated companies	7,077	–	(298)	–	–	6,779
Investments in associates	3,826	–	(1,987)	85	–	1,924
Provision for retirement benefits	74,057	–	(12,315)	12,302	–	74,044
Tax losses carried forward	31,846	–	3,140	–	–	34,986
Others	16,718	205	8,118	(45)	110	25,106
Total deferred tax assets	206,293	205	(6,087)	12,342	110	212,863
Offset with deferred tax liabilities	(63,891)					(62,352)
Total deferred tax assets, net	142,402					150,511
Deferred tax liabilities:						
Valuation differences due to equity instruments measured at fair value through other comprehensive income	(33,428)	–	–	1,410	–	(32,018)
Undistributed earnings	(14,790)	–	(2,095)	228	–	(16,657)
Gain on contribution of securities to the retirement benefit trust	(12,072)	–	127	–	–	(11,945)
Valuation differences due to business combination	(17,040)	–	2,302	–	(9,841)	(24,579)
Others	(1,480)	–	782	–	(2,467)	(3,165)
Total deferred tax liabilities	(78,810)	–	1,116	1,638	(12,308)	(88,364)
Offset with deferred tax asset	63,891					62,352
Total deferred tax liabilities, net	(14,919)					(26,012)
Net deferred tax asset	127,483					124,499

JPY (millions)

	As of April 1, 2019	Recognized through profit or loss	Recognized in other comprehensive income	Acquisitions by business combinations	Transfer to assets held for sale	As of March 31, 2020
Deferred tax assets:						
Accrued expenses and product warranty liabilities	33,784	550	–	–	(722)	33,612
Write-off of inventories	22,558	(764)	–	–	(721)	21,073
Depreciation	13,682	(1,170)	–	–	(6)	12,506
Elimination of unrealized profit from intercompany transactions among consolidated companies	6,779	1,259	–	–	(344)	7,694
Investments in associates	1,924	(453)	16	–	(21)	1,466
Provision for retirement benefits	74,044	16,216	(679)	–	(174)	89,407
Tax losses carried forward	34,986	(12,263)	–	–	–	22,723
Others	25,106	4,218	–	–	(347)	28,977
Total deferred tax assets	212,863	7,593	(663)	–	(2,335)	217,458
Offset with deferred tax liabilities	(62,352)					(52,275)
Total deferred tax assets, net	150,511					165,183
Deferred tax liabilities:						
Valuation differences due to equity instruments measured at fair value through other comprehensive income	(32,018)	515	7,358	–	–	(24,145)
Undistributed earnings	(16,657)	(553)	172	–	–	(17,038)
Gain on contribution of securities to the retirement benefit trust	(11,945)	724	–	–	–	(11,221)
Valuation differences due to business combination	(24,579)	4,005	–	(430)	–	(21,004)
Others	(3,165)	594	–	–	171	(2,400)
Total deferred tax liabilities	(88,364)	5,285	7,530	(430)	171	(75,808)
Offset with deferred tax asset	62,352					52,275
Total deferred tax liabilities, net	(26,012)					(23,533)
Net deferred tax asset	124,499					141,650

The NEC Group considers the probability that a portion, or all of future deductible temporary differences or unused tax losses can be utilized against future taxable profits in the recognition of deferred tax assets. In assessing recoverability of deferred tax assets, the NEC Group considers the scheduled reversal of taxable temporary differences, projected future taxable profits and tax planning strategies. Based on the level of historical taxable profits and projected future taxable profits, reversal of taxable temporary differences and tax planning during the periods in which the temporary differences become deductible, the NEC Group believes that it is probable that tax benefits of recognized deferred tax assets as of March 31, 2020, can be utilized.

The tax effect by applicable tax rates of deductible temporary differences and tax losses carried forward for which deferred tax assets were not recognized as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Deductible temporary differences	225,759	134,788
Unused tax losses carried forward	85,946	75,761
Total	311,705	210,549

The tax effect by applicable tax rates of unused tax losses as of March 31, 2019 and 2020, for which deferred tax assets were not recognized will expire as follows:

JPY (millions)

	2019	2020
The 1st year	3,553	1,501
The 2nd year	1,548	1,099
The 3rd year	1,420	394
The 4th year	578	519
The 5th year and thereafter	78,847	72,248
Total	85,946	75,761

The aggregate amounts of temporary differences relating to investments in subsidiaries for which no deferred tax liabilities were recognized were 143,969 million JPY and 145,707 million JPY as of March 31, 2019 and 2020, respectively.

14. Inventories

Components of inventories as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Merchandise and finished goods	79,209	53,682
Work in process	98,373	92,020
Raw materials and supplies	57,039	53,624
Total	234,621	199,326

The amount of inventories recognized as an expense during the period was included within cost of sales. Inventory write-down to net realizable value recognized as cost of sales for the fiscal years ended March 31, 2019, and 2020, was 15,723 million JPY, and 7,693 million JPY, respectively. There was no material reversal of write-downs during the fiscal years presented.

15. Trade and Other Receivables

Components of trade and other receivables as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Notes receivable	21,237	16,937
Accounts receivable	665,556	679,496
Other receivables	47,638	41,051
Total	734,431	737,484

The amounts of trade and other receivables to be collected after 12 months as of March 31, 2019, and 2020, are 1,978 million JPY and 806 million JPY, respectively.

16. Cash and Cash Equivalents

Components of cash and cash equivalents as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Cash and deposits	216,962	217,049
Certificates of deposits	61,352	142,203
Total	278,314	359,252

17. Other Assets

Components of other current assets and other non-current assets as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Advance payments	40,254	44,558
Income taxes receivable	10,609	1,775
Prepaid expenses	43,747	44,665
Others	15,589	17,438
Other current assets	110,199	108,436
Net defined benefit assets	19,893	8,757
Long-term prepaid expenses	16,167	17,471
Others	–	4
Other non-current assets	36,060	26,232

18. Assets Held for Sale

Major components of assets held for sale and liabilities directly associated with assets held for sale as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Cash and cash equivalents	3,502	4,161
Trade and other receivables	2,686	12,349
Inventories	2,568	16,496
Other assets	315	8,204
Assets held for sale	9,071	41,210

JPY (millions)

	2019	2020
Trade and other payables	3,637	11,786
Other liabilities	5,434	18,347
Liabilities directly associated with assets held for sale	9,071	30,133

The assets held for sale as of March 31, 2019, consisted of a group of assets and liabilities relating to a subsidiary, NEC Lighting, Ltd. The business of the subsidiary were transferred on April 1, 2019.

The assets held for sale as of March 31, 2020, consisted of groups of assets and liabilities relating to two subsidiaries, NEC Display Solutions, Ltd. and Showa Optronics Co., Ltd. NEC Display Solutions, Ltd. belongs to the "Global" segment, and the sale of its 66% share is scheduled to close by the end of 2020.
In addition, the assets and liabilities of Nippon Avionics Co., Ltd, ("Nippon Avionics") were classified as a disposal group held for sale during the fiscal year ended March 31, 2020. NEC sold all of common shares of Nippon Avionics through a cash tender offer. As a result, these assets and liabilities were excluded from the scope of consolidation on January 31, 2020.

19. Equity

Changes in ordinary shares for the fiscal years ended March 31, 2019, and 2020, are as follows:

(Thousands of shares)

	2019	2020
Total number of authorized shares:		
End of the year	750,000	750,000
Total number of issued shares:		
Beginning of the year	260,473	260,473
Changes during the year	–	–
End of the year	260,473	260,473

Note: The number of shares is rounded to the nearest thousand.

The shares issued by the Company are ordinary shares with no par value that have no restrictions on any rights.

Changes in treasury shares as of March 31, 2019, and 2020, are as follows:

(Thousands of shares)

	2019	2020
Ordinary shares		
Beginning of the year	702	763
Changes during the year	61	123
End of the year	763	886

Surplus

The Companies Act of Japan (the "Companies Act") provides that an amount of 50% or more of contribution at the share issuance may be incorporated into share capital and the remaining into capital reserve. The capital reserve may be incorporated into share capital upon the resolution at the shareholders' meeting.

The Companies Act requires that an amount equivalent to 10% of dividends of surplus must be appropriated as capital reserve or retained earnings reserve. No further appropriations are required when the total amount of capital reserve and retained earnings reserve equals 25% of share capital. The appropriated retained earnings reserve may be used to offset losses carried forward. The Companies Act also provides that retained earnings reserve may be reduced upon the resolution at the shareholders' meeting.

Share premium in the consolidated financial statements includes capital reserve and other capital surplus in the non-consolidated financial statements of the Company. In addition, retained earnings include retained earnings reserve and other retained earnings. The amount that may be distributed is calculated based on the Company's non-consolidated financial statements prepared in accordance with the Companies Act and Japanese accounting standards.

A breakdown of other components of equity as of March 31, 2019, and 2020, is as follows:

JPY (millions)

	2019	2020
Remeasurements of defined benefit plans	(37,575)	(35,326)
Exchange differences on translating foreign operations	(19,801)	(32,415)
Cash flow hedges	(650)	(609)
Equity instruments designated as measured at fair value through other comprehensive income	29,907	9,886
Total	(28,119)	(58,464)

Components of other comprehensive income included in non-controlling interests for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Remeasurements of defined benefit plans	(286)	(77)
Exchange differences on translating foreign operations	452	(2,371)
Cash flow hedges	–	15
Equity instruments designated as measured at fair value through other comprehensive income	(60)	(372)
Total	106	(2,805)

Other comprehensive income

The components of other comprehensive income and related tax expense and tax benefit for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Items that will not be reclassified to profit or loss		
Equity instruments designated as measured at fair value through other comprehensive income		
Decrease during the year	(4,021)	(25,696)
Tax benefit	986	5,399
Subtotal, net of tax	(3,035)	(20,297)
Remeasurements of defined benefit plans		
(Decrease) increase during the year	(52,650)	2,839
Tax benefit (expense)	12,302	(679)
Subtotal, net of tax	(40,348)	2,160
Share of other comprehensive income of entities accounted for using the equity method		
Decrease during the year	(371)	(84)
Subtotal	(371)	(84)
Items that may be reclassified subsequently to profit or loss		
Exchange differences on translating foreign operations		
Decrease during the year	(846)	(17,014)
Reclassification adjustments	(28)	2,001
Subtotal, before tax	(874)	(15,013)
Tax benefit	139	237
Sub-total, net of tax	(735)	(14,776)
Cash flow hedges		
(Decrease) increase during the year	(125)	87
Reclassification adjustments	(1)	(29)
Subtotal, before tax	(126)	58
Tax (expense) benefit	65	(36)
Sub-total, net of tax	(61)	22
Share of other comprehensive income of entities accounted for using the equity method		
Decrease during the year	(2)	(175)
Reclassification adjustments	28	-
Subtotal, net of tax	26	(175)
Total other comprehensive income, net of tax	(44,524)	(33,150)

20. Dividends

Dividends declared for which the effective date falls in the fiscal years ended March 31, 2019, and 2020, are as follows:

Fiscal year ended March 31, 2019

Resolution	Board of directors on April 27, 2018
Type of shares	Ordinary shares
Total dividends JPY (millions)	15,591
Source of dividends	Retained earnings
Dividends per share (JPY)	60
Record date	March 31, 2018
Effective date	June 1, 2018

Fiscal year ended March 31, 2020

Resolution	Board of directors on April 26, 2019
Type of shares	Ordinary shares
Total dividends JPY (millions)	10,393
Source of dividends	Retained earnings
Dividends per share (JPY)	40
Record date	March 31, 2019
Effective date	June 3, 2019

Resolution	Board of directors on October 29, 2019
Type of shares	Ordinary shares
Total dividends JPY (millions)	7,795
Source of dividends	Retained earnings
Dividends per share (JPY)	30
Record date	September 30, 2019
Effective date	December 2, 2019

Dividends declared for which the record date is in the fiscal year ended March 31, 2020, but the effective date falls in the following fiscal year are as follows:

Resolution	Board of directors on May 12, 2020
Type of shares	Ordinary shares
Total dividends JPY (millions)	10,393
Source of dividends	Retained earnings
Dividends per share (JPY)	40
Record date	March 31, 2020
Effective date	June 1, 2020

21. Bonds and Borrowings

A breakdown of bonds and borrowings and interest rates as of March 31, 2019 and 2020, is as follows:

	JPY (millions)		Average interest rate (%)	Maturity
	2019	2020		
Short-term borrowings	80,634	96,976	2.66	–
Current portion of long-term borrowings	48,044	3,029	0.36	–
Current portion of bonds	–	54,987	–	–
Commercial papers (short-term)	30,000	–	–	–
Long-term borrowings (excluding the current portion)	188,687	220,219	0.96	September 30, 2021 to October 5, 2076
Bonds (excluding the current portion)	199,441	144,609	–	–
Total	546,806	519,820		
Current	158,678	154,992		
Non-current	388,128	364,828		
Total	546,806	519,820		

A detail by issue of bonds, excluding the current portion, as of March 31, 2019 and 2020, are as follows:

Company name	Series	Issued date	JPY (millions)		Interest rate (%)	Maturity
			2019	2020		
NEC	The 47th	July 17, 2015	29,965	–	0.412	July 17, 2020
NEC	The 48th	July 17, 2015	19,957	19,971	0.658	July 15, 2022
NEC	The 49th	June 15, 2017	24,962	–	0.110	June 15, 2020
NEC	The 50th	June 15, 2017	34,903	34,933	0.290	June 15, 2022
NEC	The 51st	June 15, 2017	24,918	24,934	0.360	June 14, 2024
NEC	The 52nd	June 15, 2017	14,937	14,944	0.455	June 15, 2027
NEC	The 53rd	September 21, 2018	29,883	29,909	0.260	September 21, 2023
NEC	The 54th	September 21, 2018	9,956	9,963	0.360	September 19, 2025
NEC	The 55th	September 21, 2018	9,949	9,955	0.500	September 21, 2028
dot Data, Inc.	Convertible bond-type bonds with subscription rights to shares	May 21, 2018	11	–	1.750	May 24, 2022
	Total		199,441	144,609		

A breakdown of lease liabilities for finance leases included in long-term borrowings and interest rates as of March 31, 2019, is as follows:

	JPY (millions) 2019	Average interest rate (%)	Maturity
Current portion of lease liabilities	1,662	1.53	April 20, 2019 to March 24, 2020
Lease liabilities (excluding the current portion)	4,051	1.15	April 13, 2020 to March 31, 2029
Total	5,713		

Commitment line agreements

The NEC Group has entered into commitment line agreements for short-term borrowings with 19 financial institutions for the purpose of securing stable and flexible short-term funding. The unused commitment line of credit based on such agreements for short-term borrowings as of March 31, 2019 and 2020, is as follows:

JPY (millions)

	2019	2020
Aggregate amount of commitment line contracts	331,000	328,000
Amount used	2,000	2,000
Unused balance	329,000	326,000

Total future minimum lease payments under finance leases as of March 31, 2019 are as follows:

JPY (millions)

	2019	
	Minimum Lease Payment	Present value of Minimum Lease Payment
Within one year	1,715	1,662
Between one year and five years	4,028	3,967
More than five years	84	84
Total	5,827	5,713
Less – future finance charges	(114)	
Present value of minimum lease payments	5,713	

Reconciliation of liabilities arising from financing activities for the fiscal years ended March 31, 2019 and 2020, is as follows:

JPY (millions)

	As of April 1, 2018	Changes arising from cash flows	Changes not arising from cash flows: Business combinations	Foreign currency translation differences	Others	As of March 31, 2019
Short-term borrowings	62,293	48,234	–	107	–	110,634
Long-term borrowings	308,850	(148,097)	79,368	362	1,961	242,444
Bonds	149,600	50,011	–	0	(170)	199,441
Total	520,743	(49,852)	79,368	469	1,791	552,519

JPY (millions)

	As of April 1, 2019	Adjusted by changes in accounting policies	Changes arising from cash flows	Changes not arising from cash flows: Business combinations /disposals	Foreign currency translation differences	Lease liabilities resulting from new lease	Others	As of March 31, 2020
Short-term borrowings	110,634	–	(4,349)	(2,270)	(7,039)	–	–	96,976
Long-term borrowings	242,444	(5,713)	(10,844)	(3,030)	(17)	–	408	223,248
Lease liabilities	–	180,831	(53,620)	(1,154)	(1,202)	31,000	(256)	155,599
Bonds	199,441	–	–	–	–	–	155	199,596
Total	552,519	175,118	(68,813)	(6,454)	(8,258)	31,000	307	675,419

Short-term borrowings comprise primarily of bank borrowings and commercial papers. Long-term borrowings include lease liabilities for the year ended March 31, 2019. As a result of adoption of IFRS 16 on April 1, 2019, lease liabilities are disclosed separately for the year ended March 31, 2020.

22. Employee Benefits

Employee benefit plans

The Company and its domestic subsidiaries provide cash balance pension plans, other defined benefit pension plans, lump-sum severance payment plans, and the defined contribution pension plans in accordance with the Defined-Benefit Corporate Pension Act and the Defined Contribution Pension Act of Japan. The Company's defined benefit pension plans are administered by the Pension fund of NEC Corporation (the "Fund") which is legally independent of the Company. The Director of the Fund has the fiduciary duty to comply with laws, the directives by the Minister of Health, Labour and Welfare and the Director-Generals of Regional Bureaus of Health and Welfare made pursuant to those laws, and the by-laws of the Fund and the decisions made by the Board of Representatives of the Fund. The Company is required to make contributions to the Fund and obligated to make contributions in the amount stipulated by the Fund. Contributions are also regularly reviewed and adjusted as necessary to the extent permitted by laws and regulations.

Certain of its foreign subsidiaries have various types of defined benefit plans and defined contribution plans, covering substantially all of their employees. However, these plans are not considered material in aggregate to the NEC Group's employee benefit arrangements.

The Company and certain of its subsidiaries transferred a portion of their unfunded lump-sum defined benefit retirement plans to defined contribution pension plans on April 1, 2018. In this connection, the NEC Group transferred 52,529 million JPY of defined benefit obligations to other financial liabilities for its funding obligations to the defined contribution pension plans.

The defined benefit plans of the NEC Group are exposed to the following risks:

Investment risks

The present value of defined benefit obligations is calculated using a discount rate by reference to market yields at the end of the reporting period on high quality corporate bonds. When the yield on plan assets falls below the discount rate, there is a risk of reduction in equity due to deterioration of the funding status. In short-term, plan assets may be exposed to fluctuations in the investment performance. The portfolio of plan assets is reviewed on a regular basis in order to secure sufficient income streams over the long term for pension and severance payments in the future to meet the investment objective.

Interest rate risks

When a discount rate is adjusted downwards in line with the fallen market yields on high quality corporate bonds, the present value of defined benefit obligations may increase and cause deterioration of the funding status, exposing the NEC Group to a risk of reduction in equity.

Defined benefit obligations and plan assets

The changes in present value of defined benefit obligations and fair value of plan assets of the NEC Group for the fiscal years ended March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Present value of defined benefit obligations		
Balance at beginning of the year	1,113,774	1,036,768
Current service cost	33,513	32,140
Interest cost	6,868	5,604
Remeasurements:		
Actuarial (gains) losses arising from changes in demographic assumptions	11,348	(6,939)
Actuarial gains arising from changes in financial assumptions	(623)	(8,996)
Past service cost and gains on settlements	(1,476)	(449)
Benefits paid	(68,275)	(63,512)
Effects of business combinations and disposals	(2,525)	(13,094)
Settlements of defined benefit pension plans	(54,070)	(8,303)
Foreign currency translation differences	(1,049)	(3,221)
Transfer to liabilities directly associated with assets held for sale	(1,090)	(4,197)
Others	373	762
Balance at the end of the year	1,036,768	966,563
Fair value of plan assets		
Balance at beginning of the year	890,360	814,902
Interest income	6,162	4,823
Remeasurement: Actual loss on plan assets	(41,925)	(13,096)
Employer contributions	13,252	10,583
Benefits paid	(50,903)	(53,282)
Effects of business combinations and disposals	(920)	(8,377)
Settlements of defined benefit pension plans	(538)	–
Foreign currency translation differences	(1,616)	(3,435)
Transfer to liabilities directly associated with assets held for sale	458	(1,983)
Others	572	716
Balance at end of the year	814,902	750,851
Defined benefit liabilities	241,759	224,469
Defined benefit assets	(19,893)	(8,757)
Net defined benefit liabilities recognized in the consolidated statements of financial position	221,866	215,712

Components of defined benefit cost for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Current service cost	33,513	32,140
Net interest	706	781
Past service cost and gains on settlements	(1,476)	(449)
Total	32,743	32,472

Fair value of plan assets

The fair value of the plan assets by asset category as of March 31, 2019 and 2020, is as follows:

JPY (millions)

	2019		2020	
	With quoted market price in an active market	No quoted market price in an active market	With quoted market price in an active market	No quoted market price in an active market
Cash and cash equivalents	30,818	–	21,235	–
Equity securities	145,054	–	128,334	–
Mutual funds	–	627,645	–	590,972
Others	–	11,385	–	10,310
Total	175,872	639,030	149,569	601,282

Consolidated subsidiaries' shares that are contributed to retirement benefit trust included in Equity securities are 38,386 million JPY and 46,114 million JPY, as of March 31, 2019 and 2020, respectively. Equity securities consist of only Japanese securities.

Mutual funds are investment vehicles such as commingled funds and primarily invested in the marketable instruments such as listed stocks and government and municipal bonds in both Japanese and global markets.

In addition, the above table has been changed to show the nature of the Company's direct investments from the fiscal year ended March 31, 2020. The amounts for the fiscal year ended March 31, 2019 have been restated.

Significant actuarial assumptions used to determine the present value of the defined benefit obligations as of March 31, 2019 and 2020, are as follows:

	2019	2020
Discount rate	0.5%	0.6%

The assumptions for future mortality are based on the official mortality table generally used for actuarial assumptions in Japan. Under the mortality table used at March 31, 2019 and 2020, the current average remaining life expectancy of an individual retiring at age 60 was 23 years for males and 28 years for females.

The effects on defined obligations of a 0.1% change in the discount rate as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Discount rate		
Increased by 0.1%	(11,994)	(10,610)
Decreased by 0.1%	12,240	10,822

The NEC Group makes contributions to its defined benefit plans considering various factors, including the financial condition of the Company and its subsidiaries, funding status of the plans, and actuarial assumptions. Regarding the NEC corporate pension fund, the contribution amount is reviewed on a regular basis, and financial recalculations are conducted every five years in accordance with the Defined-Benefit Corporation Pension Act. The Fund determines investment strategies for each pension asset categories by considering expected returns and risks. Plan assets are managed within those set parameters to minimize risk, and the Company and certain of its consolidated subsidiaries may make contributions of a necessary amount if the amount of reserve falls below the minimum base amount.

The NEC Group plans to contribute 18,128 million JPY to its defined benefit pension plans during the fiscal year ending March 31, 2021.

The remaining weighted-average duration of the defined benefit obligation was 11.5 years and 11.0 years as of March 31, 2019 and 2020, respectively.

Contribution to the defined contribution plans

The Company and certain of its subsidiaries provide defined contribution benefit plans. The contributions made by the NEC Group recorded as retirement benefit expenses were 57,950 million JPY, and 57,542 million JPY for the years ended March 31, 2019, and 2020, respectively. The amount includes the payment of premiums by employer in welfare pension insurance premiums.

23. Provisions

A rollforward of provisions by major component for the fiscal year ended March 31, 2020, is as follows:

JPY (million

	Product warranty liabilities	Provision for business structure improvement	Asset retirement obligations	Provision for loss on construction contracts and others	Provision for Commercial Disputes and Litigation	Other	Total
Balance as of April 1, 2019	22,349	5,326	3,974	20,665	23,454	7,483	83,251
Increase	15,237	1,521	545	12,313	5,109	4,768	39,493
Decrease (used during the year)	(15,853)	(2,106)	(170)	(11,661)	(9,132)	(1,335)	(40,257)
Decrease (reversed during the year)	(1,734)	–	–	(936)	(410)	(269)	(3,349)
Other	(4,344)	(746)	(7)	(66)	(159)	(2,035)	(7,357)
Balance as of March 31, 2020	15,655	3,995	4,342	20,315	18,862	8,612	71,781
Balance as of April 1, 2019	22,349	5,326	3,974	20,665	23,454	7,483	83,251
Balance as of April 1, 2019 – Current	15,501	3,388	209	20,665	15,617	3,068	58,448
Balance as of April 1, 2019 – Non-current	6,848	1,938	3,765	–	7,837	4,415	24,803
Balance as of March 31, 2020	15,655	3,995	4,342	20,315	18,862	8,612	71,781
Balance as of March 31, 2020 – Current	11,362	2,531	701	20,315	17,616	6,887	59,412
Balance as of March 31, 2020 – Non-current	4,293	1,464	3,641	–	1,246	1,725	12,369

Product Warranty Liabilities

The NEC Group sells products that are repaired or exchanged for free of charge within the warranty period after the sale of products or delivery of developed software, based on contracts.

Product warranty liabilities are recognized for individually estimated future warranty costs using the historical ratio of warranty costs to net sales or other relevant factors, considering the additional incremental costs that are expected to be incurred. Most of these costs are expected to be incurred in the following fiscal year and the rest to be incurred within approximately two years after the end of the reporting period.

Provision for Business Structure Improvement

The provision is recognized for the estimated expenses and losses in connection with restructuring activities. Most of this provision is expected to be utilized in the next year and the rest to be utilized within approximately two years from the end of the reporting period.

Asset Retirement Obligations

The provision is made mainly for the expenses in association with scrap, removal and retirement of long-lived assets, and restoring the site based on past experience. These expenses are added to the carrying amount of the related assets. The expenses and discount rate are reviewed every year. Most of these costs are expected to be incurred by 2030.

Provision for Loss on Construction Contracts and Others

A provision is recognized for customized software or construction contracts for which the NEC Group is fulfilling its contract obligations, when it identifies construction contracts for which it is probable, at the end of the reporting period, that it will incur a loss, and the amount of the loss after the reporting period is reasonably estimable. The timing of cash outflows depends on the progress of the project in the future.

Provision for Commercial Disputes and Litigation

A provision is recognized for certain potential commercial claims and disputes as well as pending, threatened or possible legal proceedings and litigation. The timing of cash outflows depends on the progress of cases in the future. The Company's management has conducted an assessment of the probable outcome of each commercial claim and dispute. Regarding the most significant matter in terms of provision amount, management has decided not to disclose further details of the matter as such disclosure could seriously prejudice the position of the Company with respect thereto. The remaining matters are significantly smaller, a substantial majority of them being disputes in the ordinary course of business regarding alleged breach of contract claims related to product delivery.

Other

A provision is recognized for present obligations other than those included in the above categories.

24. Trade and Other Payables

Components of trade and other payables as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Notes payable	6,001	4,932
Accounts payable-trade	405,798	398,741
Accounts payable-other	70,797	57,208
Total	482,596	460,881

25. Other Liabilities

Components of other current and non-current liabilities as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Consumption tax withheld	29,853	39,368
Deposits from employees	5,757	3,811
Others	26,375	11,974
Other current liabilities	61,985	55,153
Deferred tax liabilities	26,012	23,533
Others	17,209	10,749
Other non-current liabilities	43,221	34,282

26. Revenue

Fiscal years ended March 31, 2019 and 2020

Disaggregation of revenue

The NEC Group has six reportable segments: Public Solutions, Public Infrastructure, Enterprise, Network Services, System Platform and Global.

The NEC Group recognizes sales revenue by disaggregating revenue into the following three types: “Contracts for hardware and packaged software deployments”, “Contracts for services to customers (including maintenance and outsourcing)”, and “Contracts for system integrations and equipment constructions”.

The revenue disaggregated by type of good or service and the reconciliation of the disaggregated revenue with the six reportable segments for the fiscal years ended March 31, 2019 and 2020, are as follows:

Fiscal year ended March 31, 2019

JPY(millions)

	Reportable segments							Others	Consolidated Total
	Public Solutions	Public Infrastructure	Enterprise	Network Services	System Platform	Global	Total		
Contracts for hardware and packaged software deployments	55,986	254,064	40,224	119,678	343,751	184,413	998,116	118,771	1,116,887
Contracts for services to customers (including maintenance and outsourcing)	113,955	109,309	196,344	200,526	134,929	120,811	875,874	76,957	952,831
Contracts for system integrations and equipment constructions	116,210	258,506	195,233	140,103	21,533	104,145	835,730	7,998	843,728
Total	286,151	621,879	431,801	460,307	500,213	409,369	2,709,720	203,726	2,913,446

Fiscal year ended March 31, 2020

JPY(millions)

	Reportable segments							Others	Consolidated Total
	Public Solutions	Public Infrastructure	Enterprise	Network Services	System Platform	Global	Total		
Contracts for hardware and packaged software deployments	59,251	248,268	58,173	150,678	391,456	161,286	1,069,112	28,946	1,098,058
Contracts for services to customers (including maintenance and outsourcing)	121,486	101,488	176,003	219,776	133,711	195,645	948,109	76,888	1,024,997
Contracts for system integrations and equipment constructions	143,871	281,384	221,332	139,378	23,525	136,830	946,320	25,859	972,179
Total	324,608	631,140	455,508	509,832	548,692	493,761	2,963,541	131,693	3,095,234

The NEC Group has changed the method of disaggregated sales revenue into three types: “Contracts for hardware and packaged software deployments”, “Contracts for services to customers (including maintenance and outsourcing)”, and “Contracts for system integrations and equipment constructions”. In addition, the above disaggregated revenue information for the fiscal year ended March 31, 2019 has been restated to conform to the current segment composition reflecting the organizational changes effective April 1, 2019.

Contract balances

There are no significant changes to contract assets during the fiscal year ended March 31, 2019 and 2020. The amount of revenue recognized for the fiscal years ended March 31, 2019 and 2020, that was included in the contract liability balances at the beginning of the years is 98,509 million JPY and 124,758 million JPY, respectively.

Remaining performance obligations

The revenue expected to be recognized in the future related to performance obligations that are unsatisfied (or partially unsatisfied) as of March 31, 2019 and 2020, is as follows:

	JPY (millions)	
	2019	2020
Timing of recognition in revenue		
One year or less	580,129	527,020
More than one year	705,047	785,843
Remaining performance obligations	1,285,176	1,312,863

The table above does not include the remaining performance obligations that have original expected durations of one year or less.

27. Other Operating Income (Expenses)

Components of other operating income (expenses) for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Other operating income		
Insurance recovery	1,219	2,735
Gain on loss of control of subsidiaries	–	1,684
Gain on sale of land	633	1,656
Indemnification received	2,712	1,514
Gain on reversal of contingent loss	286	679
Gain on sales of subsidiaries' stocks	9,148	245
Other	7,717	4,797
Subtotal	21,715	13,310
Other operating expenses		
Impairment loss	(12,607)	(6,384)
Loss on disposal of property, plant and equipment	(3,819)	(3,280)
Provision for contingent loss	(1,306)	(2,242)
Business structure improvement cost	(26,921)	(1,089)
Settlement payment and indemnification for damages	(408)	(667)
Other	(5,782)	(6,908)
Subtotal	(50,843)	(20,570)
Other operating expenses, net	(29,128)	(7,260)

"Gain on sales of subsidiaries' stocks" for the fiscal year ended March 31, 2019, mainly represents a gain on sale of shares of NEC Energy Devices.

For "Impairment loss," please refer to Note 10. "Impairment Losses of Non-Financial Assets."

28. Expenses by Nature

Major components of expenses by nature included in "Cost of sales" and "Selling, general and administrative expenses" for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Material costs	995,947	998,644
Personnel expenses	890,715	891,123
Outsourcing and subcontracting fees	544,142	588,727
Depreciation and amortization	118,664	188,984

Components of personnel expenses for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Salaries and bonuses	709,987	709,281
Retirement benefit expenses	96,248	94,665
Social security expense	58,987	60,957
Other	25,493	26,220
Total	890,715	891,123

29. Finance Income and Finance Costs

Components of finance income and finance costs for the fiscal years ended March 31, 2019, and 2020, are as follows:

JPY (millions)

	2019	2020
Finance income		
Interest income	1,995	1,994
Dividend income	5,444	5,148
Gain on sales of associates	12,603	135
Foreign exchange gains, net	265	–
Other	1,682	1,200
Total	21,989	8,477

JPY (millions)

	2019	2020
Finance costs		
Interest expenses	6,870	9,844
Foreign exchange losses, net	–	3,560
Other	1,507	2,060
Total	8,377	15,464

Interest income arises from financial assets measured at amortized cost. Dividend income arises from equity instruments designated as measured at fair value through other comprehensive income. In addition, interest expenses arise from financial liabilities measured at amortized cost and lease liabilities. "Gain on sales of associates" in the fiscal year ended March 31, 2019, is mainly from the sale of shares of Automotive Energy Supply Corporation.

30. Earnings Per Share

The calculation of basic earnings per share ("EPS") and diluted EPS has been based on the following profit attributable to ordinary shareholders of the parent company for the fiscal years ended March 31, 2019, and 2020:

JPY (millions)

	2019	2020
Net profit attributable to owners of the Parent	39,675	99,967
Net profit attributable to ordinary shareholders of the parent to calculate basic EPS	39,675	99,967
Net profit attributable to ordinary shareholders of the Parent after adjustment for the effects of dilutive potential ordinary shares	39,674	99,967
Weighted-average number of ordinary shares to calculate basic EPS (in thousands of shares)	259,738	259,644
Weighted-average number of ordinary shares (diluted) (in thousands of shares)	259,738	259,644
Basic EPS (JPY)	152.75	385.02
Diluted EPS (JPY)	152.75	385.01

Net Profit attributable to ordinary shareholders of the Parent after adjustment for the effects of dilutive potential ordinary shares includes the effect of share options issued by JAE, a subsidiary of the Company.

31. Financial Instruments

Capital management

The NEC Group focuses on the business operation for emphasizing capital efficiency, invests to growth sectors, and enhances capital base to create long-term corporate value of the NEC Group. The NEC Group manages net debt-equity ratio for enhancing capital base.

Total assets, total liabilities, and total equity are as follows:

Condensed Consolidated Statement of Financial Position as of March 31, 2019 and 2020

	JPY (billions)		YoY Change
	2019	2020	2020/2019
Total Assets	2,963.2	3,123.3	160.0
Total liabilities	1,903.5	2,008.7	105.2
Total equity	1,059.7	1,114.5	54.8
Interest-bearing debt	552.5	675.4	122.9
Net interest-bearing debt	274.2	316.2	42.0
Equity attributable to owners of the parent	858.9	910.7	51.7
Ratio of equity attributable to owners of the parent	29.0%	29.2%	0.2
Debt equity ratio	0.64 times	0.74 times	0.10
Net debt-equity ratio	0.32 times	0.35 times	0.03

** Net debt-equity ratio = (Interest-bearing debt – Cash and cash equivalents) / Equity attributable to owners of the parent*

Financial risk management

The NEC Group operates its business in various countries and jurisdictions, and as such, it has exposure to credit risk, liquidity risk, and market risk (mainly represented by interest rate risk and currency risk). The NEC Group conducts appropriate risk management activities to minimize the effect of these financial risks on its financial position and performance.

Credit risk

Credit risk is a risk of financial loss to the NEC Group if a customer or a counterparty to a financial instrument fails to meet its obligations and arises principally from the NEC Group's receivables from customers and investments in debt securities. The NEC Group is monitoring the financial position and past due balances of customers in order to minimize the risk of default resulting from deterioration of customers' financial position. Further, if necessary, preventative measures are taken by holding collateral or through other means. Financial institutions with high credit capabilities are selected as counterparties while dealing in derivative transactions, deposit transactions, and the purchase of financial assets for short-term investments in order to reduce the counterparty risk.

The NEC Group guarantees its employees and its subcontractors' borrowings from financial institutions. The total amounts of financial guarantee were 645 million JPY and 574 million JPY as of March 31, 2019 and 2020, respectively. The maximum exposure to credit risk, without taking into account of any collateral held at the end of the reporting period, is represented by the total amount of financial guarantee and carrying amount of the financial instruments which is exposed to credit risk in the consolidated statement of financial position.

Credit risk exposure relating to trade and other receivables and contract assets

The trade and other receivables are mainly from Japanese customers. An allowance for expected credit losses for trade and other receivables and contract assets is measured at an amount equal to the lifetime expected credit losses. The assets are grouped by each asset with similar characteristics of credit risks and expected credit losses are calculated based on historical default rates, concerning the current conditions and future economic environment. Expected credit losses for credit-impaired financial assets are calculated by each asset.

The NEC Group determines whether credit risk of financial assets has increased significantly since initial recognition by considering reasonable and supportable information. This information includes past information, external ratings, past due information, as well as forward-looking information.

The NEC Group determines that credit risk has increased significantly since initial recognition when, for example, a borrower falls under any of the following conditions:

- The external rating of the borrower is deemed ineligible for investment.
- The delinquency period exceeds 30 days.

The NEC Group defines that a default has occurred when a borrower falls under any of the following conditions:

- It is judged that there is almost no possibility that the borrower pays obligations to the NEC Group without executing the security interest.
- The delinquency period exceeds 90 days.

The NEC Group determines that a financial asset has been credit impaired when any of the following situations is confirmed:

- Significant financial difficulty of the issuer or borrower.
- A breach of contract, such as a default or past due event.
- The lender(s) of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession(s) that the lender(s) would not otherwise consider.
- It is becoming probable that the borrower will enter bankruptcy or other financial reorganization.
- The disappearance of an active market for that financial asset because of financial difficulties.

Credit risk exposure relating to trade receivables

The NEC Group's credit risk exposure relating to trade receivables as of March 31, 2019 and 2020, is as follows:

			JPY (millions)
	Gross carrying amount of a financial asset	Allowance for expected credit losses	Carrying amount, net of allowance for expected credit losses
March 31, 2019	673,922	(8,366)	665,556
March 31, 2020	686,839	(7,343)	679,496

In determining whether the financial assets are credit-impaired, the NEC Group uses reasonable and substantiated information which is available without undue cost or effort. The NEC Group considers that the financial assets are not credit-impaired if the information provides counterevidence. Expected credit losses from other receivables, contract assets, other financial assets, and financial guarantee contracts are not significant and the table above does not include them.

The changes in allowance for expected credit losses on trade receivables for the fiscal years ended March 31, 2019 and 2020, are as follows:

		JPY (millions)
	2019	2020
Beginning balance	7,771	8,366
Increase	2,495	1,144
Decrease (written off)	(1,438)	(978)
Decrease (reversal)	(568)	(660)
Others	106	(529)
Ending balance	8,366	7,343

Liquidity risk

Liquidity risk is the risk that the NEC Group encounters difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The NEC Group's approach of managing liquidity is to ensure that it has sufficient liquidity to meet its liabilities when they are due. The NEC Group periodically updates forecasts of its future cash flows aiming to maintain the level of its cash and cash equivalents and the unused balance of commitment line of credit at an amount in excess of expected cash outflows on financial liabilities required for conducting its business.

The following are the remaining contractual maturities of financial liabilities as of March 31, 2019 and 2020. The amounts below include contractual interest payments and exclude the impact of netting agreements.

As of March 31, 2019

JPY (millions)

	Carrying amount	Contractual cash flows	Within one year	Between one and two years	Between two and three years	Between three and four years	Between four and five years	More than five years
Non-derivative financial liabilities:								
Trade and other payables	482,596	482,596	482,596	–	–	–	–	–
Accruals	52,775	52,775	52,775	–	–	–	–	–
Short-term borrowings	80,634	82,602	82,602	–	–	–	–	–
Commercial papers	30,000	30,000	30,000	–	–	–	–	–
Long-term borrowings	236,731	347,092	50,206	6,234	7,539	10,306	43,618	229,189
Bonds	199,441	203,186	706	55,631	555	55,449	30,283	60,562
Finance lease obligations	5,713	5,827	1,715	1,839	1,038	781	370	84
Derivative financial liabilities:								
Forward exchange contracts	1,064	1,064	511	445	60	18	20	10
Total	1,088,954	1,205,142	701,111	64,149	9,192	66,554	74,291	289,845

As of March 31, 2020

JPY (millions)

	Carrying amount	Contractual cash flows	Within one year	Between one and two years	Between two and three years	Between three and four years	Between four and five years	More than five years
Non-derivative financial liabilities:								
Trade and other payables	460,881	460,881	460,881	–	–	–	–	–
Accruals	56,795	56,795	56,795	–	–	–	–	–
Short-term borrowings	96,976	99,474	99,474	–	–	–	–	–
Long-term borrowings	223,248	332,170	6,051	6,741	44,501	43,678	3,864	227,335
Bonds	199,596	202,242	55,631	555	55,438	30,283	25,199	35,136
Lease liabilities	155,599	162,261	49,777	38,093	29,729	17,464	12,348	14,850
Derivative financial liabilities:								
Forward exchange contracts	1,058	1,058	828	210	5	9	6	–
Total	1,194,153	1,314,881	729,437	45,599	129,673	91,434	41,417	277,321

It is not expected that the contractual cash flows included in the maturity analysis disclosed above could occur significantly earlier or at significantly different amounts.
However, certain long-term borrowings with an aggregate principal amount of 130,000 million JPY contain a covenant for early repayment, under which the NEC Group is able to make an early repayment of all (or part) of the principal during or after 2021, provided that certain conditions are met.

Market risk

Interest rate risk

Interest-bearing debts with floating interest rates, including long-term borrowings, are exposed to interest rate risk. The NEC Group may use interest rate swaps as hedges of the variability in cash flows attributable to interest rate risk.

The following table shows the floating-rate financial liabilities of the NEC Group as of March 31, 2019 and 2020. Interest-bearing debts with floating rates that are fixed rates in substance under interest rate swap contracts are excluded from the amounts.

JPY (millions)

	2019	2020
	Carrying amount	Carrying amount
Long-term borrowings (floating rates)	67,407	65,671

Sensitivity analysis for financial instruments with floating rates

An increase of 1% in interest rates on the financial instruments with floating rates at the end of the reporting period would have decreased profit before income taxes by the amounts shown below. The amounts are calculated by multiplying the balance of financial liabilities with the floating rate held by the NEC Group at the end of the reporting period (except for those with floating rates that are fixed rates in substance under interest rate swap contracts) by 1% and assuming that all other variables, in particular foreign current exchange rates, remain constant. The analysis applies the same assumptions in each fiscal year.

JPY (millions)

	2019	2020
Profit before income taxes	(674)	(657)

Foreign currency risk

The NEC Group operates its business globally and is exposed to the risk of fluctuation in foreign exchange rates. The NEC Group mitigates foreign currency risk exposures to an extent possible by offsetting trade receivables and payables denominated in the same foreign currencies and conducting hedge transactions mainly on the remaining net exposures and net forecast transaction exposures using forward exchange contracts.

The NEC Group's exposure to foreign currency risk as of March 31, 2019 and 2020, is as follows:

(Thousands of U.S. dollars and euros)

	2019		2020	
	U.S. dollars	Euros	U.S. dollars	Euros
Trade receivables	389,194	38,970	310,704	5,883
Trade payables	(333,677)	(34,602)	(290,909)	(9,025)
Forward exchange contracts	37,768	(72,337)	(337,754)	(22,349)
Net exposure	93,285	(67,969)	(317,959)	(25,491)

Sensitivity analysis for foreign exchange rates

Strengthening of the JPY by 1% against the U.S. dollar and euro at the end of the reporting period would have increased or decreased profit before income taxes by the amounts shown below.

This analysis assumes that all other variables, such as interest rates, remain constant.

JPY (millions)

	2019	2020
	Profit before income taxes	Profit before income taxes
U.S. dollars (1% strengthening of the JPY)	(104)	346
Euros (1% strengthening of the JPY)	85	30

Equity price risk

The NEC Group holds listed equity instruments of parties with which the NEC Group has a business relationship, and, therefore, is exposed to the risk of fluctuation in prices of equity instruments. The equity instruments are held for if the NEC Group determines that it will contribute to the increase of the mid- to long-term corporate value of the NEC Group after comprehensive consideration of its management strategy, the relationships with business partners and other circumstances.

Sensitivity analysis for fluctuation in equity prices

An increase or decrease of 1% in equity prices based on the price risk of equity instruments at the end of the reporting period would have increased or decreased other components of equity (before tax) by the amounts shown below.

JPY (millions)

	2019	2020
Increase or decrease of 1% in equity prices	1,290	943

Fair value measurement

Fair value hierarchy

Hierarchy and classification used for the fair value measurement for financial assets and liabilities measured at fair value are as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities

Level 2: Inputs other than quoted prices classified into Level 1 that are observable for the financial asset or liability, either directly or indirectly

Level 3: Unobservable inputs that are not based on observable market data

The NEC Group recognizes transfers between levels of the fair value hierarchy when a triggering event of the change has occurred.

Basis of the fair value measurement for financial instruments

Cash and cash equivalents, trade and other receivables, trade and other payables, and accruals: The fair value is determined as equal or close to the carrying amount since they are to be settled in a short term.

The fair value of loans is measured by discounting estimated future cash flows to the present value based on an interest rate that takes into account the remaining period to the maturity date and credit risk.

Of equity instruments designated as measured at fair value through other comprehensive income, and financial assets measured at fair value through profit or loss, the fair value of listed equity instruments is determined using a quoted market price at an exchange. The fair value of equity securities with no active market is measured mainly by using the comparable company valuation method or other appropriate valuation methods. Price book-value ratio (PBR) of a comparable company is used as a significant unobservable input in the fair value measurement of the equity securities with no active market. The fair value increases (decreases) as the PBR of a comparable company rises (declines).

Among the fair values of derivative assets and liabilities, forward exchange contracts are determined using quoted forward exchange rates at the end of the fiscal year, while interest rate swaps are calculated as the present value of the estimated future cash flows based on the interest rate at the end of the reporting period.

The fair values of short-term borrowings and long-term borrowings (current portion) are determined as the carrying amount, as the carrying amount is a reasonable estimate of fair value due to the relatively short period of maturity of these instruments. The fair value of long-term borrowings (excluding the current portion) is calculated as the present value of the estimated future cash flows, based on the expected interest rate at which a similar new borrowing was made.

The fair value of bonds is determined based on the quoted market price in a non-active market.

The carrying amounts and fair values of financial assets and liabilities as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019		2020	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets measured at amortized cost:				
Cash and cash equivalents	278,314	278,314	359,252	359,252
Trade and other receivables	734,431	734,431	737,484	737,484
Others	46,907	46,907	45,576	45,576
Financial liabilities measured at amortized cost:				
Trade and other payables	482,596	482,596	460,881	460,881
Short-term borrowings	80,634	80,634	96,976	96,976
Commercial papers	30,000	30,000	–	–
Current portion of long-term borrowings	48,044	48,044	3,029	3,029
Bonds	199,441	201,107	199,596	200,425
Long-term borrowings	188,687	189,637	220,219	220,879
Accruals	52,775	52,775	56,795	56,795
Others	17,987	17,987	12,412	12,412

Regarding the fair value hierarchy of assets and liabilities (except for those whose fair value is determined as equal or close to the carrying amount) presented in the table above, bonds are categorized as Level 2 and long-term borrowings are categorized as Level 3.

Additionally, accruals that are categorized as financial instruments do not include accruals for employee benefit and accruals by statutory requirements.

Financial assets and liabilities measured at fair value on a recurring basis by fair value category as of March 31, 2019 and 2020, are as follows:

As of March 31, 2019 — JPY (millions)

	Level 1	Level 2	Level 3	Total
Financial assets measured at fair value through profit or loss	–	344	4,257	4,601
Equity instruments designated as measured at fair value through other comprehensive income	129,024	–	75,752	204,776
Financial liabilities measured at fair value through profit or loss	–	1,064	–	1,064

As of March 31, 2020 — JPY (millions)

	Level 1	Level 2	Level 3	Total
Financial assets measured at fair value through profit or loss	–	1,578	10,531	12,109
Equity instruments designated as measured at fair value through other comprehensive income	94,273	–	72,952	167,225
Financial liabilities measured at fair value through profit or loss	–	1,058	–	1,058

There were no significant financial assets or liabilities that were transferred between levels during the fiscal years ended March 31, 2019 and 2020.

Level 3 fair value

Financial assets classified into Level 3 mainly consist of unquoted equity instruments. The fair value of significant unquoted equity instruments is measured by using comparable company valuation multiples and other appropriate valuation techniques. For the financial assets classified into Level 3, changes of unobservable inputs to reasonably possible alternative assumptions are not expected to cause significant changes in the fair value of those financial assets. Further, fair value measurements of financial assets and liabilities classified into Level 3 are reviewed and approved by the personnel responsible in the accounting department based on relating internal regulations. The significant changes in Level 3 assets measured at fair value on a recurring basis for the fiscal year ended March 31, 2019 and 2020, are mainly due to purchase of equity instruments designated as measured at fair value through other comprehensive income, and purchase of equity instruments measured at fair value through profit or loss, respectively.

Equity instruments designated as financial assets measured at fair value through other comprehensive income

The NEC Group designates long-term stock holdings for the purpose of maintaining and strengthening relationship with its business partners and expanding its revenue base as equity instruments measured at fair value through other comprehensive income. The NEC Group, in principle, makes an irrevocable election to present in other comprehensive income subsequent changes in the fair value of an investment in equity instruments, except those in the form of venture capital investment. The fair value and dividend income of equity instruments designated as measured at fair value through other comprehensive income and recognized in other financial assets are 204,776 million JPY and 4,732 million JPY, respectively, for the fiscal year ended March 31, 2019, and 167,225 million JPY and 4,426 million JPY, respectively, for the fiscal year ended March 31, 2020. Of equity instruments designated as measured at fair value through other comprehensive income, derecognized amount of the fair value is not significant for the fiscal years ended March 31, 2019 and 2020. Also, of equity instruments designated as measured at fair value through other comprehensive income, derecognized amount of accumulated gains and losses is not significant for the fiscal years ended March 31, 2019 and 2020.

Equity instruments designated as measured at fair value through other comprehensive income classified as Level 1 in the fair value hierarchy as of March 31, 2019 and 2020, include the following:

JPY (millions)

	2019	2020
Hua Hong Semiconductor Ltd.	25,768	19,745
Sumitomo Electric Industries, Ltd.	10,154	7,869
Sumitomo Mitsui Trust Holdings, Inc.	5,203	4,088
Tokyo Broadcasting System Holdings, Inc.	4,881	3,623
COMSYS Holdings Corporation	4,253	3,919
MS&AD Insurance Group Holdings, Inc.	4,211	3,325
DAIKIN INDUSTRIES, LTD	2,961	3,007
MEIDENSHA CORPORATION	2,649	2,832
Seven Bank, Ltd.	3,270	2,790

Equity instruments designated as measured at fair value through other comprehensive income classified as Level 3 in the fair value hierarchy as of March 31, 2019 and 2020, include the following:

JPY (millions)

	2019	2020
JECC Corporation	35,680	36,788
Dalian Hi-Think Computer Technology Corp.	15,391	11,211
BostonGene Corporation	5,550	5,986

Hedge accounting

There were no significant transactions to which hedge accounting was applied.

Other financial assets and other financial liabilities

A breakdown of other financial assets and other financial liabilities as of March 31, 2019 and 2020, is as follows:

	JPY (millions)	
	2019	2020
Financial assets measured at amortized cost:		
Deposits	1,897	496
Others	45,010	45,080
Financial assets measured at fair value through other comprehensive income:		
Equity instruments	204,776	167,225
Financial assets measured at fair value through profit or loss:		
Equity instruments	4,257	10,531
Others	344	1,578
Total	256,284	224,910
Other financial assets-current	5,875	5,584
Other financial assets-non-current	250,409	219,326
Total	256,284	224,910
Financial liabilities measured at amortized cost:		
Deposits received	5,984	5,636
Long-term accounts payable	39,713	39,793
Others	16,825	10,910
Financial liabilities measured at fair value through profit or loss:		
Others	1,064	1,058
Total	63,586	57,397
Other financial liabilities-current	16,169	14,995
Other financial liabilities-non-current	47,417	42,402
Total	63,586	57,397

32. Leases

Fiscal year ended March 31, 2019

The NEC Group is a lessee under several operating leases, primarily for buildings and vehicles. Future minimum lease payments under non-cancelable operating leases that have initial or remaining lease terms in excess of one year as of March 31, 2019 were as follows:

	JPY (millions)
	2019
Within one year	17,139
Between one year and five years	35,464
After five years	10,892
Total	63,495

Minimum lease payments under operating leases recognized as expenses for the fiscal years ended March 31, 2019 were 36,933 million JPY.

Fiscal year ended March 31, 2020

The nature of the leasing activities

The NEC Group, as a lessee, leases mainly buildings and land ("property") for its office space and vehicles for its administrative and sales functions. Certain of these property leases include options to extend the lease term after the end of the lease period exercisable by the NEC Group to obtain operational flexibility. There are no significant restrictions or covenants, such as those restricting additional debts and further leasing, imposed by leases. The vast majority of the building lease contracts, especially for those entered into for the use in the domestic businesses, contain extension options exercisable at the discretion of the NEC Group, and only lease payments for the duration of the lease term that is a period covered by the options which the NEC Group is reasonably certain to exercise are included in measuring the lease liability.

Expenses, and cash outflows related to lease arrangements for the fiscal year ended March 31, 2020, are as follows:

	JPY (millions)
	2020
Depreciation expense for right-of-use assets by the class of underlying asset	
Property	50,366
Machinery and equipment	1,076
Tools, furniture and fixtures	2,475
Total	53,917
Interest expense on lease liabilities	2,375
Expense relating to short-term leases	4,578
Expense relating to leases of low-value assets	4,934
Total cash outflow for leases	65,339

The carrying amount of right-of-use assets by class of underlying asset as of March 31, 2020 are as follows:

	JPY (millions)
	2020
Property	141,092
Machinery and equipment	1,950
Tools, furniture and fixtures	7,640
Total	150,682

Additions to right-of-use assets amounted to 31,000 million JPY for the fiscal year ended March 31, 2020.

The future cash outflows to which the NEC Group is potentially exposed that are not reflected in the measurement of lease liabilities, arising from leases not yet commenced to which the NEC Group is committed, as of March 31, 2020, are 7,712 million JPY.

Maturity analysis of lease liabilities is disclosed in Note 31, "Financial Instruments".

33. Related Parties

In the ordinary course of business, the NEC Group purchases from and sells to its related parties materials, supplies, and services. Such related parties include associates and joint ventures accounted for using the equity method.

Transactions with related parties

Other than those purchase and sales transaction entered into in the ordinary course of business that are summarized in the table below, there were no significant transactions between the NEC Group and its related parties for the fiscal years ended March 31, 2019 and 2020.

Purchases from and sales to related parties for the fiscal years ended March 31, 2019 and 2020 are as follows:

JPY (millions)

	2019	2020
Purchases	163,514	147,255
Sales	182,986	150,591

Balances of trade and other receivables due from related parties and trade and other payables due to related parties as of March 31, 2019 and 2020, are as follows:

JPY (millions)

	2019	2020
Trade and other receivables	14,331	25,270
Trade and other payables	42,442	39,545

Key management personnel compensation

Key management personnel are defined as the NEC's board of directors and members of the audit and supervisory board. The compensation for the key management personnel for the fiscal years ended March 31, 2019 and 2020, is as follows:

JPY (millions)

	2019	2020
Basic compensation	345	402
Bonuses	168	217
Stock compensation	44	375
Total	557	994

34. Commitments

The amounts of contractual commitments for the purchases of property, plant and equipment as of March 31, 2019 and 2020, are 2,006 million JPY and 1,856 million JPY, respectively.

The amounts of contractual commitments for the purchases of intangible assets as of March 31, 2019 and 2020, are 636 million JPY and 552 million JPY, respectively.

35. Contingencies

The Company and certain of its subsidiaries are subject to legal proceedings, including civil litigations related to trade, tax, products, or intellectual properties, and governmental investigations. The Company has been dealing with the various litigations and investigations. Depending upon the outcome of these proceedings, the Company and certain of its subsidiaries may be subject to fines, and accordingly, the Company has accrued for certain probable and reasonable estimated amounts for the fines as it has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

There are a number of legal actions against the Company and certain subsidiaries. Management is of the opinion that damages, if any, resulting from these actions will not have a material effect on the Company's consolidated financial statements.

It is difficult to predict the outcome of these actions and proceedings, given that certain of the investigations and legal proceedings are still at an early stage and present novel legal theories, involving a large number of parties or taking place in jurisdictions outside of Japan where the laws are complex or unclear. Accordingly, the Company is unable to estimate the losses or range of losses for the actions and proceedings where there is only a reasonable possibility that a loss exceeding the amounts already recognized may have been incurred.

36. Subsequent Events

Issuance of Unsecured Straight Bonds

The Company announced the terms for the issuance of its 56th, 57th and 58th series of Unsecured Straight Bonds on April 17, 2020 for the purpose of funding the scheduled redemption of the outstanding straight bonds. All series were issued at par on April 23, 2020, and have, as a financial covenant, a negative pledge clause (with an inter-bond pari passu clause). The information about the aggregate notional amount, coupon rate and maturity date is as follows:

Series	Aggregate notional amount (million JPY)	Coupon rate (per annum)	Maturity date
56th	10,000	0.280%	April 21, 2023
57th	15,000	0.400%	April 23, 2025
58th	10,000	0.540%	April 23, 2030

37. Impact of Changes in Accounting Policies

Application of IFRS 16, "Leases"

During the fiscal year ended March 31, 2020, the NEC Group has adopted IFRS 16. The comparative information has not been restated using the transition method under IFRS 16 and the cumulative effect of the adoption of IFRS 16 is recognized as of the date of initial application on April 1, 2019.

The NEC Group elected to not to reassess whether a contract is, or contains, a lease at the date of initial application using a practical expedient of IFRS 16. Accordingly, the NEC Group grandfathers its previous assessment of whether a contract is, or contains, a lease based on IAS 17 and IFRIC 4, "Determining whether an Arrangement Contains a Lease." In addition, the adoption of IFRS 16 did not have a significant effect on the retained earnings at the beginning of fiscal year ended March 31, 2020.

Leases previously classified as operating leases applying IAS 17

In transitioning to IFRS 16, the NEC Group has elected to apply the following practical expedients for leases previously classified as operating leases applying IAS 17:

- As an alternative to performing an impairment review, the NEC Group relied on its assessment of whether leases were onerous by applying IAS 37, "Provisions, Contingent Liabilities and Contingent Assets," immediately before the date of initial application.
- The NEC Group elected not to recognize right-of-use assets and lease liabilities for leases for which the lease term ends within 12 months of the date of initial application.
- The NEC Group excluded initial direct costs from the measurement of the right-of-use asset at the date of initial application.

In addition, at the date of initial application, the lease liabilities were measured at the present value of the remaining lease payments discounted using the NEC Group's incremental borrowing rate. The weighted average of the lessee's incremental borrowing rates was 1.3%.

Leases previously classified as finance leases applying IAS 17

For leases that the NEC Group as a lessee previously classified as finance leases applying IAS 17, the carrying amounts of the right-of-use assets and the lease liabilities at the date of initial application were the carrying amounts of the leased assets and the lease liabilities immediately before that date measured applying IAS 17.

The following is a reconciliation of non-cancellable operating lease commitments applying IAS 17 as of March 31, 2019, and the lease liabilities recognized at the date of initial application:

	JPY (millions)
Non-cancellable operating lease commitments discounted using the incremental borrowing rate as of April 1, 2019	59,469
Finance lease obligations as of March 31, 2019	5,713
Cancellable operating lease contracts	81,800
Extension options reasonably certain to be exercised	33,849
Lease liabilities as of April 1, 2019	180,831

The right-of-use assets recognized for leases previously classified as operating leases applying IAS 17 at the date of initial application were 175,716 million JPY.

KPMG

Independent Auditor's Report

To the Board of Directors of NEC Corporation (Nippon Denki Kabushiki Kaisha):

Opinion

We have audited the accompanying consolidated financial statements of NEC Corporation ("the Company") and its consolidated subsidiaries (collectively referred to as "the Group") which comprise the consolidated statements of financial position as of March 31, 2020, and the consolidated statements of profit or loss, consolidated statements of comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as of March 31, 2020, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards prescribed in Article 93 of "the Regulation on Terminology, Forms, and Preparation Methods of Consolidated Financial Statements" (hereinafter referred to as "IFRS").

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in Japan. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Japan, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Corporate auditors and the Audit and Supervisory board for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern in accordance with IFRS and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Corporate auditors and the Audit and Supervisory board are responsible for overseeing the directors' performance of their duties including the design, implementation and maintenance of the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with auditing standards generally accepted in Japan will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

KPMG

As part of our audit in accordance with auditing standards generally accepted in Japan, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, while the objective of the audit is not to express an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate whether the presentation and disclosures in the consolidated financial statements are in accordance with IFRS, the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with corporate auditors and the Audit and Supervisory board regarding, among other matters, the planned scope and timing of the audit, significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide corporate auditors and the Audit and Supervisory board with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Interest required to be disclosed by the Certified Public Accountants Act of Japan

Our firm and its designated engagement partners do not have any interest in the Company and its subsidiaries which are required to be disclosed pursuant to the provisions of the Certified Public Accountants Act of Japan.

KPMG

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