# Quarterly Financial Statements for the Nine Months Ended December 31, 2008

January 30, 2009

Listed company's name: **Kawasaki Heavy Industries, Ltd.**
Listed on: 1st sections of TSE, OSE, NSE
Stock code: 7012
URL: http://www.khi.co.jp/
Representative: Tadaharu Ohashi, President
Contact: Mitsutoshi Takao, Senior Vice President and Senior Manager of Finance and Accounting Department
Tel: +81 3-3435-2130
Submission of quarterly financial statements: February 13, 2009

## 1. Consolidated Financial Results for the Nine Months Ended December 31, 2008
## (April 1, 2008 to December 31, 2008)

(Amounts rounded down to the nearest million yen)

(1) Operating Results

(Percentage figures represent changes versus the year-ago period)

| | Net sales | | Operating income | | Recurring profit | | Net income | |
|---|---|---|---|---|---|---|---|---|
| | million yen | % | million yen | % | million yen | % | million yen | % |
| Nine months ended December 31, 2008 | 954,962 | - | 14,706 | - | 21,578 | - | 7,460 | - |
| Nine months ended December 31, 2007 | 1,051,155 | 4.9 | 53,771 | 20.4 | 48,008 | 32.9 | 28,962 | 25.5 |

| | Earnings per share | Earnings per share – diluted |
|---|---|---|
| | yen | yen |
| Nine months ended December 31, 2008 | 4.47 | 4.41 |
| Nine months ended December 31, 2007 | 17.38 | 16.95 |

(2) Financial Condition

| | Total assets | Net assets | Ratio of net assets to total assets | Net assets per share |
|---|---|---|---|---|
| | million yen | million yen | % | yen |
| December 31, 2008 | 1,425,028 | 303,362 | 20.8 | 178.24 |
| March 31, 2008 | 1,378,769 | 319,037 | 22.7 | 187.73 |

Note: Shareholders' equity: December 31, 2008: 297,351 million yen
March 31, 2008: 313,192 million yen

## 2. Dividends

| Record date | Dividend per share | | | | |
|---|---|---|---|---|---|
| | End of first quarter | End of second quarter | End of third quarter | End of financial year | Full year |
| | yen | yen | yen | yen | yen |
| Year ended March 31, 2008 | — | 0.00 | — | 5.00 | 5.00 |
| Year ending March 31, 2009 | — | 0.00 | — | | — |
| Year ending March 31, 2009 (forecast) | | | | — | |

Note: 1. Revision of dividend forecast during the nine months ended December 31, 2008: Yes
2. Dividends for the year ending March 31, 2009, are yet to be determined.

## 3. Forecast of Consolidated Earnings for the Year Ending March 31, 2009 (April 1, 2008 to March 31, 2009)

(Percentage figures represent changes versus the year-ago period)

| | Net sales | | Operating income | | Recurring profit | | Net income | | Earnings per share |
|---|---|---|---|---|---|---|---|---|---|
| | million yen | % | million yen | % | million yen | % | million yen | % | yen |
| Full year | 1,330,000 | (11.3) | 18,000 | (76.5) | 28,000 | (56.2) | 11,000 | (68.6) | 6.59 |

Note: Revision of earnings forecast during the nine months ended December 31, 2008: Yes

## 4. Other Information

1) Changes affecting the status of material subsidiaries (scope of consolidation): None

2) Use of simplified accounting methods and/or accounting methods specific to the preparation of quarterly consolidated financial statements: Yes
Note: For details, see “4. Other information” on page 6 in the “Qualitative Information and Financial Statements” section.

3) Changes in accounting principles, procedures, and methods of presentation applicable to the preparation of quarterly consolidated financial statements:
(1) Changes in accordance with revisions to accounting standards: Yes
(2) Changes other than (1) above: Yes
Note: For details, see “4. Other information” on page 6 in the “Qualitative Information and Financial Statements” section.

4) Number of shares issued (common stock)
(1) Number of shares issued at end of period (treasury stock included):
December 31, 2008: 1,669,629,122 shares
March 31, 2008: 1,669,629,122 shares
(2) Number of shares held in treasury at end of period:
December 31, 2008: 1,373,842 shares
March 31, 2008: 1,324,199 shares
3) Average number of shares (for the nine months):
Nine months ended December 31, 2008: 1,668,279,917 shares
Nine months ended December 31, 2007: 1,666,323,762 shares

*** Appropriate Use of Financial Forecasts and Other Important Matters**

*Forward-Looking Statements*

1. The Company has revised its consolidated full-year earnings forecasts for the fiscal year ending March 31, 2009, which were released on October 31, 2008. This document reflects the revised forecasts.
2. The year-end dividend for the fiscal year ending March 31, 2009, has not yet been determined because the Company downwardly revised its earnings outlook and the operating environment remains uncertain. Kawasaki Heavy Industries, Ltd., will issue further information on dividends after evaluating results of operations for the full fiscal year ending March 31, 2009, and the Company's earnings outlook for the fiscal year ending March 31, 2010.
3. These materials contain various forward-looking statements and other forecasts regarding performance and other matters. Such statements are based on information available at the time of preparation. Actual results may differ from those expressed or implied by forward-looking statements due to a range of factors. For the assumptions underlying the earnings forecasts presented and other information regarding the use of such forecasts, refer to "3. Consolidated Earnings Outlook" on page 6 in the "Qualitative Information and Financial Statements" section.

*Other Important Matters*

Effective this consolidated fiscal year, the Company has adopted the Accounting Standard for Quarterly Financial Reporting (Accounting Standards Board of Japan (ASBJ) Statement No. 12) and its accompanying Guidance on Accounting Standard for Quarterly Financial Reporting (ASBJ Guidance No. 14). The consolidated financial statements for nine months ended December 31, 2008, were prepared in accord with the Regulations on Terminology, Format, and Preparation of Quarterly Financial Statements.

## Qualitative Information and Financial Statements

### 1. Consolidated operating results

In the nine months to December 31, 2008 (first three quarters of the fiscal year ending March 31, 2009), the Japanese economy entered a steep downturn marked by a consumer spending slump, retrenchment in capital spending, deterioration in employment conditions, and an export slowdown amid precipitous yen appreciation, most notably against the euro and US dollar.

Much of the global economy, including hitherto buoyant emerging economies, likewise slowed markedly or sank into recession under the weight of the financial crisis that originated in the US.

Amid such an operating environment, certain KHI Group businesses (e.g., Rolling Stock & Construction Machinery, Gas Turbines & Machinery) continued to perform solidly in the three quarters to December 31, but the Aerospace, Shipbuilding, and Consumer Products & Machinery segments all saw their earnings decline in the wake of yen appreciation and a falloff in American and European demand.

Relative to the corresponding year-earlier period, the Group's consolidated order bookings in the nine months to December 31 decreased ¥56.3 billion to ¥1,087.2 billion, net sales fell ¥96.1 billion to ¥954.9 billion, operating income declined ¥39.0 billion to ¥14.7 billion, recurring profit fell ¥26.4 billion to ¥21.5 billion, and net income decreased ¥21.5 billion to ¥7.4 billion.

Consolidated operating performance in the nine months to December 31, 2008, is summarized by segment below.

**Shipbuilding**

The Shipbuilding segment booked new orders for one LPG tanker and five bulk carriers, but its consolidated order bookings nonetheless shrank to ¥64.1 billion, a ¥119.3 billion decrease from the year-earlier period, when it benefited from a heavy influx orders for bulk carriers.

Consolidated net sales fell ¥16.5 billion year-on-year to ¥95.8 billion, largely reflecting a decline in sales of large vessels.

The decline in sales weighed on profitability, as did the yen's appreciation against the dollar and sharp increases in material costs. The segment incurred an operating loss of ¥2.5 billion, ¥5.5 billion below its operating income in the year-earlier period.

**Rolling Stock & Construction Machinery**

Consolidated order bookings increased ¥28.1 billion year-on-year to ¥186.4 billion by virtue of orders for *shinkansen* (bullet trains), electric commuter trains, and locomotives from JR Group and other railway companies, and, overseas, orders for subway cars for the New York City subway system.

Consolidated net sales grew ¥14.5 billion year-on-year to ¥131.8 billion as growth in overseas sales of rolling stock offset a decline in North American sales of construction machinery.

Sales growth boosted operating income to ¥7.7 billion, a ¥3.6 billion year-on-year increase.

**Aerospace**

Although the Aerospace segment won new orders for parts for the Boeing 767 and 777 jetliners, its consolidated order bookings fell ¥37.8 billion year-on-year to ¥87.7 billion.

Consolidated net sales were down ¥45.0 billion year-on-year to ¥126.4 billion as a result of declines in sales to Japan's Ministry of Defense and sales of Boeing 767 and 777 parts, coupled with the yen's appreciation against the dollar.

Profitability-wise, the decrease in sales was compounded by cost increases, including inventory valuation losses. The segment incurred an operating loss of ¥4.3 billion, ¥16.7 billion below its operating income in the year-earlier period.

**Gas Turbines & Machinery**

Consolidated order bookings rose ¥120.5 billion year-on-year to ¥279.3 billion, lifted by growth in orders for ship propulsion systems, diesel generator systems, and marine diesel engines. New orders for aircraft engine parts for Trent XWB aircraft engines also contributed to order growth.

Consolidated net sales grew ¥8.4 billion year-on-year to ¥138.8 billion, driven largely by growth in sales of marine diesel engines and gas turbine generator systems.

Despite this sales growth, operating income declined ¥600 million year-on-year to ¥6.7 billion, largely as a result of material price inflation and inventory valuation losses.

**Plant & Infrastructure Engineering**

Despite an influx of orders for LNG storage tanks and various plant facilities, consolidated order bookings decreased ¥4.4 billion year-on-year to ¥61.6 billion.

Consolidated net sales fell ¥16.0 billion year-on-year to ¥66.1 billion as growth in overseas cement plant sales was outweighed by declines in revenues from trash incineration plant and bridge projects.

Operating income grew ¥1.4 billion to ¥5.3 billion, largely by virtue of an increase in high-margin contracts, reflecting greater selectivity in screening incoming orders.

**Consumer Products & Machinery**

Consolidated net sales fell ¥57.7 billion year-on-year to ¥247.8 billion in the wake of the yen's progressive appreciation against the dollar and euro, a decline in industrial robot sales to the semiconductor industry, and a drop in North American and European motorcycle sales.

The segment incurred a ¥7.7 billion operating loss, ¥22.4 billion below its operating income in the year-earlier period.

**Hydraulic Machinery**

Consolidated order bookings grew ¥3.8 billion year-on-year to ¥71.5 billion, driven chiefly by demand from construction machinery manufacturers.

Consolidated net sales were up ¥7.1 billion year-on-year to ¥68.2 billion by virtue of strong sales to the construction machinery industry through mid-year.

Operating income grew in tandem with sales, up ¥500 million year-on-year to ¥7.0 billion.

**Other Operations**

Consolidated net sales rose ¥9.0 billion year-on-year to ¥79.8 billion. Operating profit grew ¥800 million year-on-year to ¥2.6 billion.

## 2. Consolidated Financial Condition

At December 31, 2008, the Company had total consolidated assets of ¥1,425 billion, an increase of ¥46.2 billion from March 31, 2008. The increase was largely attributable to fixed-asset growth stemming from capital investment, and accretion of work-in-process through progress made toward completion of existing contracts. Such growth was partially offset by a decrease in trade receivables resulting from reduction in sales and collection of receivables. Consolidated liabilities totaled ¥1,121.6 billion at December 31, up ¥61.9 billion from March 31, largely due to increased borrowings and customer advances, which were partially offset by the decrease in trade payables. Consolidated net assets decreased ¥15.6 billion from March 31, 2008, to ¥303.3 billion at December 31, 2008, largely because of reduction in net unrealized gains on available-for-sale securities due to fallen equity prices, and a decrease in foreign currency translation adjustments due to the yen's appreciation.

## 3. Consolidated Earnings Outlook

The Company now expects that its consolidated results for the fiscal year ending March 31, 2009, will fall short of its previously announced forecast as a result of revision of the forecast's underlying exchange rate assumptions to reflect the yen's recent appreciation and revision of sales and profit budgets in response to deeper than anticipated demand retrenchment in mass-production businesses' markets, most notably consumer products.

The revised exchange rate assumptions are ¥90 to the US dollar and ¥120 to the euro, revised from ¥100 and ¥130, respectively.

## 4. Other Information

1) Changes affecting the status of material subsidiaries (scope of consolidation) during the period

Not applicable

2) Use of simplified accounting and/or accounting procedures specific to preparation of quarterly consolidated financial statements

*Simplified accounting*

(1) Bad debt estimation method for general claims

The Company estimates the value of uncollectible general claims based on the preceding fiscal year's actual credit loss rate, unless the credit loss rate is deemed to have substantially changed relative to the historical rate calculated at the end of the preceding fiscal year.

(2) Inventory valuation method

The Company estimates quarter-end inventories by a rational method based on the preceding fiscal year's physical inventory count, without conducting a physical inventory count.

The Company writes down inventory from book value to estimated net realizable value only when its utility has clearly diminished. In the case of inventory expected to be disposed of and slow-moving inventory with a turnover period that extends beyond the Company’s operating cycle, the Company writes the inventory down to its estimated liquidation value. Such inventories are carried at their written-down book value, unless their value was deemed to have substantially changed during the first three quarters of the fiscal year.

(3) Fixed-asset depreciation method

For fixed asset depreciated by the declining-balance method, the Company calculates quarterly depreciation expense by prorating annual depreciation expense. For certain consolidated subsidiaries, quarterly depreciation expense is calculated by prorating annual depreciation expense based on a budget that factors in expected acquisitions, sales, and disposals of fixed assets during the fiscal year.

(4) Deferred-tax asset and liability calculation method

To assess deferred assets' collectability, the Company uses tax planning and earnings forecasts used in the preceding fiscal year if it deems that the operating environment and status of temporary differences have not changed substantially since the preceding fiscal year-end.

If the operating environment or status of temporary differences is deemed to have changed substantially since the preceding fiscal year-end, the Company uses said tax planning and earnings forecasts adjusted to reflect the changes' impact.

(5) Elimination of unrealized gains/losses on inventories

For some products, the Company calculates unrealized gains/losses on inventories using the gain/loss rate used in the preceding fiscal year or quarter or a gain/loss rate based on rational budgeting, unless business conditions are deemed to have changed substantially from the preceding fiscal year or quarter.

*Accounting procedures specific to preparation of quarterly consolidated financial statements*

The Company calculates tax expense by rationally estimating its effective tax rate after application of deferred-tax accounting to pretax net income for the fiscal year that includes the third quarter under review and multiplying quarterly pretax net income by said estimated effective tax rate. If unable to use the estimated effective tax rate, the Company calculates tax expense by multiplying the statutory effective tax rate by quarterly pretax net income adjusted to reflect material differences other than temporary differences.

Income taxes are reported inclusive of income tax adjustments.

3) Changes in accounting principles, procedures, or presentation methods applicable to preparation of quarterly consolidated financial statements

*Changes related to accounting standards*

(1) Change related to quarterly financial reporting

Effective from the current fiscal year, the Company has adopted the Accounting Standard for Quarterly Financial Reporting (ASBJ Statement No. 12) and its accompanying Guidance on Accounting Standard for Quarterly Financial Reporting (ASBJ Guidance No. 14). Additionally, the company prepares quarterly consolidated financial statements in accord with the Regulations for Quarterly Consolidated Financial Statements.

(2) Change in inventory valuation standard and method

The Company has previously valued ordinary held-for-sale inventories mainly at cost by the specific identification, moving average, and FIFO methods. Effective from the first quarter of the current fiscal year, the Company has switched to valuing inventories mainly at the lower of cost or market (i.e., writing down inventories' carrying value to reflect impairment of the goods' utility) by the specific identification, moving average, and FIFO methods in conjunction with adoption of Accounting Standard for Measurement of Inventories (ASBJ Statement No. 9, as revised July 5, 2006). In the first three quarters of the current fiscal year, this change resulted in a ¥4,577 million reduction in gross profit, operating income, recurring profit, and pretax net income.

The change's impact by segment is detailed below in the relevant note to the financial statements.

(3) Adoption of Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements

Effective from the first quarter of the current fiscal year, the Company has adopted the Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements (ASBJ Practical Issues Task Force Report No. 18, May 17, 2006).

This change had no impact on earnings in the first three quarters of the current fiscal year.

(4) Adoption of accounting standard for lease transactions (lessee transactions)

Effective from the first quarter of the current fiscal year, the Company has adopted the Accounting Standard for Lease Transactions (ASBJ Statement No. 13, issued June 17, 1993; last revised March 30, 2007) and accompanying Guidance on Accounting Standard for Lease Transactions (ASBJ Guidance No. 16, issued January 18, 1994; last revised March 30, 2007) in conjunction with their applicability to quarterly financial statements from the first fiscal year beginning on or after April 1, 2008. As a result of their adoption, the Company has changed its accounting treatment of finance leases that do not transfer ownership. When it is the lessee in such lease transactions, the Company now treats the leases as ordinary sales transactions, whereas it previously treated them as operating leases. To depreciate assets leased in finance lease transactions that do not transfer ownership, the Company uses the straight-line method with a useful life equivalent to the lease term and a salvage value of zero.

For transactions with a lease inception date predating the current fiscal year, the Company is maintaining status quo accounting treatment of finance lease transactions that do not transfer ownership.

This change's impact on earnings in the first three quarters of the current fiscal year is immaterial.

(5) Adoption of accounting standard for lease transactions (lessor transactions)

Effective from the first quarter of the current fiscal year, the Company has adopted the Accounting Standard for Lease Transactions (ASBJ Statement No. 13, issued June 17, 1993; last revised March 30, 2007) and accompanying Guidance on Accounting Standard for Lease Transactions (ASBJ Guidance No. 16, issued January 18, 1994; last revised March 30, 2007) in conjunction with their applicability to quarterly financial statements from the first fiscal year beginning on or after April 1, 2008. As a result of their adoption, the Company has changed its accounting treatment of finance leases that do not transfer ownership. When it is the lessor in such lease transactions, the Company now treats the leases as ordinary sales transactions, whereas it previously treated them as operating leases.

For transactions with a lease inception date predating the current fiscal year, the Company is maintaining status quo accounting treatment of finance lease transactions that do not transfer ownership.

This change's impact on earnings in the first three quarters of the current fiscal year is immaterial.

*Additional information*

The Company and its domestic consolidated subsidiaries have revised machinery's useful life pursuant to 2008 amendments to the tax code. These revisions resulted in a ¥1.14 billion reduction in operating income, recurring profit, and pretax net income in the first three quarters of the current fiscal year.

The change's impact by segment is detailed below under “Segment Information” in the “Consolidated Financial Statements” section.

## 5. Consolidated Financial Statements

### (1) Consolidated Balance Sheets

| | Millions of yen | |
|---|---|---|
| | As of December 31, 2008 | As of March 31, 2008 |
| **Assets** | | |
| Current assets | | |
| Cash on hand and in banks | 52,050 | 39,875 |
| Trade receivables | 330,733 | 417,934 |
| Merchandise and finished products | 70,033 | 62,386 |
| Work in process | 368,983 | 296,265 |
| Raw materials and supplies | 83,661 | 80,656 |
| Other current assets | 107,713 | 89,303 |
| Allowance for doubtful receivables | (3,291) | (4,140) |
| Total current assets | 1,009,885 | 982,282 |
| Fixed assets | | |
| Net property, plant and equipment | 279,851 | 259,927 |
| Intangible assets | | |
| Goodwill | 1,166 | 41 |
| Other | 16,927 | 16,012 |
| Total intangible assets | 18,093 | 16,053 |
| Investments and other assets | | |
| Other | 118,652 | 121,851 |
| Allowance for doubtful receivables | (1,454) | (1,344) |
| Total investments and other assets | 117,197 | 120,506 |
| Total fixed assets | 415,142 | 396,487 |
| **Total assets** | 1,425,028 | 1,378,769 |
| | | |
| **Liabilities** | | |
| Current liabilities | | |
| Trade payables | 346,182 | 430,999 |
| Short-term borrowings | 170,198 | 120,162 |
| Income taxes payable | 3,949 | 16,836 |
| Accrued bonuses | 10,981 | 19,263 |
| Provision for losses on construction contracts | 16,025 | 8,836 |
| Other allowances | 13,518 | 8,978 |
| Advances from customers | 142,010 | 124,679 |
| Other current liabilities | 143,868 | 94,785 |
| Total current liabilities | 846,734 | 824,541 |
| Long-term liabilities | | |
| Bonds payable | 40,990 | 60,990 |
| Long-term debt | 133,982 | 77,776 |
| Employees' retirement and severance benefits | 86,211 | 81,927 |
| Other allowances | 2,169 | 2,167 |
| Other | 11,578 | 12,328 |
| Total long-term liabilities | 274,930 | 235,190 |
| **Total liabilities** | 1,121,665 | 1,059,732 |

| | Millions of yen | |
|---|---|---|
| | As of December 31, 2008 | As of March 31, 2008 |
| **Net assets** | | |
| Shareholders' equity | | |
| Common stock | 104,328 | 104,328 |
| Capital surplus | 54,282 | 54,290 |
| Retained earnings | 150,005 | 151,401 |
| Treasury stock | (465) | (459) |
| Total shareholders' equity | 308,151 | 309,560 |
| Valuation and translation adjustments | | |
| Net unrealized gains (losses) on securities | 1,393 | 10,292 |
| Gains (losses) on hedging items | 7,017 | 5,217 |
| Foreign currency translation adjustment | (19,211) | (11,878) |
| Total valuation and translation adjustments | (10,800) | 3,631 |
| Minority interests | 6,010 | 5,845 |
| **Total net assets** | 303,362 | 319,037 |
| **Total net assets and liabilities** | 1,425,028 | 1,378,769 |

## (2) Consolidated Statements of Income

| | Millions of yen |
|---|---|
| | Nine months ended December 31, 2008 |
| Net sales | 954,962 |
| Cost of sales | 819,888 |
| Gross profit | 135,074 |
| Selling, general and administrative expenses | |
| Salaries and benefits | 31,018 |
| R&D expenses | 26,465 |
| Other | 62,882 |
| Total selling, general and administrative expenses | 120,367 |
| Operating income | 14,706 |
| Non-operating income | |
| Interest income | 2,360 |
| Dividend income | 1,200 |
| Gain on sale of marketable and investment securities | 642 |
| Equity income of non-consolidated subsidiaries and affiliates | 6,512 |
| Foreign exchange gain, net | 2,629 |
| Other, net | 3,187 |
| Total non-operating income | 16,533 |
| Non-operating expenses | |
| Interest expense | 4,965 |
| Other, net | 4,695 |
| Total non-operating expenses | 9,660 |
| Recurring profit | 21,578 |
| Extraordinary income | |
| Gain on sale of business | 594 |
| Total extraordinary income | 594 |
| Extraordinary losses | |
| Provision for losses on damages suit | 5,165 |
| Total extraordinary losses | 5,165 |
| Income before income taxes and minority interests | 17,007 |
| Income taxes | 8,389 |
| Minority interests in net income of consolidated subsidiaries | 1,158 |
| Net income | 7,460 |

| | Millions of yen |
|---|---|
| | Three months ended December 31, 2008 |
| Net sales | 302,039 |
| Cost of sales | 272,225 |
| Gross profit | 29,813 |
| Selling, general and administrative expenses | |
| Salaries and benefits | 9,750 |
| R&D expenses | 8,778 |
| Other | 20,931 |
| Total selling, general and administrative expenses | 39,460 |
| Operating loss | (9,646) |
| Non-operating income | |
| Interest income | 548 |
| Dividend income | 511 |
| Equity income of non-consolidated subsidiaries and affiliates | 3,202 |
| Other, net | 869 |
| Total non-operating income | 5,130 |
| Non-operating expenses | |
| Interest expense | 1,536 |
| Loss on sale of marketable and investment securities | 232 |
| Foreign exchange loss, net | 392 |
| Other, net | 2,461 |
| Total non-operating expenses | 4,623 |
| Recurring loss | (9,139) |
| Extraordinary income | |
| Gain on sale of business | 594 |
| Total extraordinary income | 594 |
| Loss before income taxes and minority interests | (8,544) |
| Income taxes | (4,199) |
| Minority interests in net income of consolidated subsidiaries | 530 |
| Net loss | (4,875) |

## (3) Consolidated Cash flow Statement

| | Millions of yen<br>Nine months ended December 31, 2008 |
|---|---|
| Cash flow from operating activities | |
| Income before income taxes and minority interests | 17,007 |
| Depreciation and amortization | 31,472 |
| Increase (decrease) in allowance for doubtful receivables | 5,052 |
| Interest and dividend income | (3,560) |
| Interest expense | 4,965 |
| Investment gain on equity method | (6,512) |
| (Gain) loss on sale and disposal of property, plant, and equipment | (648) |
| (Increase) decrease in trade receivables | 76,647 |
| (Increase) decrease in inventories | (99,794) |
| Increase (decrease) in trade payables | (73,204) |
| Increase (decrease) in advances received | 19,247 |
| Other | (17,033) |
| Subtotal | (46,361) |
| Cash received for interest and dividends | 3,690 |
| Cash paid for interest | (4,955) |
| Cash paid for income taxes | (25,588) |
| Net cash provided by (used in) operating activities | (73,215) |
| Cash flow from investing activities | |
| Acquisition of property, plant and equipment and intangible assets | (48,674) |
| Proceeds from sale of property, plant and equipment and intangible assets | 2,580 |
| Acquisition of investments in securities | (3,033) |
| Proceeds from sale of investments in securities | 1,635 |
| Acquisition of equity interest in subsidiaries resulting in change in scope of consolidation | (943) |
| (Increase) decrease in short-term loans receivable | (131) |
| Additions to long-term loans receivable | (31) |
| Proceeds from collection of long-term loans receivable | 1,453 |
| Other | 260 |
| Net cash used in investing activities | (46,885) |
| Cash flow from financing activities | |
| Increase (decrease) in short-term borrowings, net | 104,030 |
| Proceeds from long-term debt | 61,508 |
| Repayment of long-term debt | (3,973) |
| Redemption of bonds payable | (17,518) |
| Acquisition of treasury stock | (13) |
| Cash dividends paid | (8,308) |
| Cash dividends paid to minority interests | (340) |
| Net cash used in financing activities | 135,384 |
| Effect of foreign exchange rate changes on cash and cash equivalents | (1,866) |
| Increase (decrease) in cash and cash equivalents | 13,416 |
| Cash and cash equivalents at beginning of period | 38,169 |
| Cash and cash equivalents at end of period | 51,586 |

Effective this consolidated fiscal year, Kawasaki Heavy Industries, Ltd. has adopted the Accounting Standard for Quarterly Financial Reporting (Accounting Standards Board of Japan (ASBJ) Statement No. 12) and its accompanying Guidance on Accounting Standard for Quarterly Financial Reporting (ASBJ Guidance No. 14). The consolidated financial statements for nine months ended December 31, 2008, were prepared in accord with the Regulations on Terminology, Format and Preparation of Quarterly Financial Statements.

## (4) Notes on the going-concern assumption: Not applicable

## (5) Segment Information

### 1) Information by industry segment

Nine months ended December 31, 2008 (April 1, 2008 – December 31, 2008)
Millions of yen

| | External sales | Intersegment sales | Total sales | Operating income (loss) |
|---|---|---|---|---|
| Shipbuilding | 95,805 | 1,064 | 96,869 | (2,577) |
| Rolling Stock & Construction Machinery | 131,801 | 1,049 | 132,851 | 7,707 |
| Aerospace | 126,484 | 1,294 | 127,778 | (4,333) |
| Gas Turbines & Machinery | 138,835 | 13,208 | 152,044 | 6,740 |
| Plant & Infrastructure Engineering | 66,122 | 8,610 | 74,732 | 5,328 |
| Consumer Products & Machinery | 247,844 | 5,232 | 253,077 | (7,752) |
| Hydraulic Machinery | 68,216 | 6,384 | 74,600 | 7,000 |
| Other | 79,852 | 30,420 | 110,272 | 2,682 |
| Total | 954,962 | 67,265 | 1,022,228 | 14,796 |
| Eliminations/corporation | — | (67,265) | (67,265) | (89) |
| Consolidated total | 954,962 | — | 954,962 | 14,706 |

Notes: 1. Method of segmentation
Business segmentation is based on the categorization used by management.

2. Major products by industry segment

| Industry segment | Major products |
|---|---|
| Shipbuilding | Ships and vessels |
| Rolling Stock & Construction Machinery | Rolling stock, construction machinery, snowplows, crushing machines |
| Aerospace | Aircrafts |
| Gas Turbines & Machinery | Jet engines, general-purpose gas turbine generators, movers |
| Plant & Infrastructure Engineering | Industrial equipment, boilers, environmental equipment, steel structures |
| Consumer Products & Machinery | Motorcycles, personal watercraft, all-terrain vehicles (ATV), utility vehicles, general-purpose gasoline engines, industrial robots |
| Hydraulic Machinery | Industrial hydraulic products |
| Other | Commercial activities, sales/order agency and intermediary activities, management of welfare facilities |

3. Change in inventory valuation standard and method

As stated in section 4.–3)–(2) of the “Qualitative Information and Financial Statements” section, the Company previously valued ordinary held-for-sale inventories mainly at cost by the specific identification, moving average, and FIFO methods. Effective from the first quarter of the fiscal year ending March 31, 2009, the Company switched to valuing inventories mainly at the lower of cost or market (i.e., writing down inventories’ carrying value to reflect impairment of the goods’ utility) by the specific identification, moving average, and FIFO methods in conjunction with adoption of Accounting Standard for Measurement of Inventories (ASBJ Statement No. 9, as revised July 5, 2006). In the first three quarters of the current fiscal year, this change resulted in a reduction in operating income of ¥383 million for Rolling Stock & Construction Machinery, ¥2,881 million for Aerospace, ¥757 million for Gas Turbines & Machinery, ¥26 million for Plant & Infrastructure Engineering, ¥393 million for Consumer Products & Machinery, ¥127 million for Hydraulic Machinery, and ¥7 million for Other Operations.

4. Change in useful life for property, plant and equipment

As stated under “Additional information” in section 4.–3 of the “Qualitative Information and Financial Statements” section, the Company and its domestic consolidated subsidiaries have revised machinery's useful life and asset groupings pursuant to 2008 amendments to the tax code. In the first three quarters of the fiscal year ending March 31, 2009, these revisions resulted in a reduction in operating income of ¥399 million for Shipbuilding, ¥307 million for Rolling Stock & Construction Machinery, ¥180 million for Aerospace, ¥168 million for Gas Turbines & Machinery, ¥39 million for Plant & Infrastructure Engineering, ¥123 million for Consumer Products & Machinery, and ¥31 million for Other Operations, while operating income increased ¥109 million in Hydraulic Machinery.

**2) Information by geographic area**

Nine months ended December 31, 2008 (April 1, 2008 – December 31, 2008)

Millions of yen

| | External sales | Intersegment sales | Total sales | Operating income (loss) |
|---|---|---|---|---|
| Japan | 686,945 | 188,150 | 875,095 | 7,993 |
| North America | 160,015 | 19,067 | 179,083 | (1,187) |
| Europe | 68,830 | 3,491 | 72,321 | (16) |
| Asia | 32,179 | 29,061 | 61,241 | 3,553 |
| Other areas | 6,991 | 187 | 7,179 | 373 |
| Total | 954,962 | 239,958 | 1,194,921 | 10,718 |
| Eliminations/corporate | — | (239,958) | (239,958) | 3,988 |
| Consolidated total | 954,962 | — | 954,962 | 14,706 |

Notes: 1. Classification method of geographic segment: by geographic proximity

2. Major countries or regions in each segment other than Japan:

| | |
|---|---|
| North America | U.S.A. and Canada |
| Europe | Netherlands, United Kingdom, and Germany |
| Asia | Thailand, Indonesia, Philippines, and Korea |
| Other areas | Australia and Brazil |

3. Change in inventory valuation standard and method

As stated in section 4.–3)–(2) of the “Qualitative Information and Financial Statements” section, the Company has previously valued ordinary held-for-sale inventories mainly at cost by the specific identification, moving average, and FIFO methods. Effective from the first quarter of the fiscal year ending March 31, 2009, the Company has switched to valuing inventories mainly at the lower of cost or market (i.e., writing down inventories' carrying value to reflect impairment of the goods’ utility) by the specific identification, moving average, and

FIFO methods in conjunction with adoption of the Accounting Standard for Measurement of Inventories (ASBJ Statement No. 9, as revised July 5, 2006). In the first three quarters of the fiscal year ending March 31, 2009, this change resulted in a ¥4,577 million reduction in operating income for Japan.

4. Change in useful life for property, plant and equipment

As stated under “Additional information” in section 4.–3) of the “Qualitative Information and Financial Statements” section, the Company and its domestic consolidated subsidiaries have revised machinery's useful life and asset groupings pursuant to 2008 amendments to the tax code.

In the first three quarters of the fiscal year ending March 31, 2009, this change resulted in a ¥1,140 million reduction in operating income for Japan.

**2. Overseas sales**

Nine months ended December 31, 2008 (April 1, 2008 – December 31, 2008)

Millions of yen

| | Overseas sales | Consolidated net sales | Ratio of overseas sales to consolidated sales (%) |
|---|---|---|---|
| North America | 215,893 | — | 22.6 |
| Europe | 88,772 | — | 9.2 |
| Asia | 108,776 | — | 11.3 |
| Other areas | 112,806 | — | 11.8 |
| Total | 526,248 | 954,962 | 55.1 |

Notes: 1. “Overseas sales” includes sales by the Company and its consolidated subsidiaries to the countries and regions other than Japan.

2. Classification method of geographic segment: by geographic proximity

3. Major countries or regions in each segment:

| | |
|---|---|
| North America | U.S.A. and Canada |
| Europe | United Kingdom, France, Netherlands, Germany, and Spain |
| Asia | China, Korea, Philippines, and Taiwan |
| Other areas | Panama, Bahamas, Brazil, and Australia |

## (6) Note on Significant Changes in the Amount of Shareholders’ Equity: Not applicable

**For reference:**

**Consolidated Financial Statements for the Nine Months ended December 31, 2007**

**(April 1, 2007 – December 31, 2007)**

## (1) Consolidated Statements of Income

| | Millions of yen<br>Nine months ended December 31, 2007 |
|---|---|
| Net sales | 1,051,155 |
| Cost of sales | 878,853 |
| Gross profit | 172,301 |
| Selling, general and administrative expenses | 118,530 |
| Operating income | 53,771 |
| Non-operating income | |
| Interest and dividend income | 3,881 |
| Equity income of unconsolidated subsidiaries and affiliates | 4,384 |
| Other, net | 5,040 |
| Total non-operating income | 13,307 |
| Non-operating expenses | |
| Interest expense | 6,031 |
| Other, net | 13,038 |
| Total non-operating expenses | 19,070 |
| Recurring profit | 48,008 |
| Extraordinary income | 292 |
| Extraordinary losses | 2,245 |
| Income before income taxes and minority interests | 46,055 |
| Income taxes | 16,244 |
| Minority interests in net income of consolidated subsidiaries | 849 |
| Net income | 28,962 |

## (2) Orders, net sales and order backlog by industry segment

### 1) Orders

| | Nine months ended December 31, 2007 | | Nine months ended December 31, 2008 | | Year ended March 31, 2008 | |
|---|---|---|---|---|---|---|
| | million yen | % of total | million yen | % of total | million yen | % of total |
| Shipbuilding | 183,510 | 16.0 | 64,117 | 5.8 | 251,331 | 15.6 |
| Rolling Stock & Construction Machinery | 158,351 | 13.8 | 186,497 | 17.1 | 183,254 | 11.3 |
| Aerospace | 125,604 | 10.9 | 87,737 | 8.0 | 202,505 | 12.5 |
| Gas Turbines & Machinery | 158,745 | 13.8 | 279,316 | 25.6 | 227,422 | 14.1 |
| Plant & Infrastructure Engineering | 66,083 | 5.7 | 61,629 | 5.6 | 106,045 | 6.5 |
| Consumer Products & Machinery | 305,579 | 26.7 | 247,844 | 22.7 | 433,962 | 26.9 |
| Hydraulic Machinery | 67,669 | 5.9 | 71,520 | 6.5 | 92,334 | 5.7 |
| Other | 78,110 | 6.8 | 88,629 | 8.1 | 113,900 | 7.0 |
| Total | 1,143,656 | 100.0 | 1,087,292 | 100.0 | 1,610,756 | 100.0 |

Note: The Consumer Products & Machinery segment's orders are equal to its net sales as production is based mainly on estimated demand.

### 2) Net sales

| | Nine months ended December 31, 2007 | | Nine months ended December 31, 2008 | | Year ended March 31, 2008 | |
|---|---|---|---|---|---|---|
| | million yen | % of total | million yen | % of total | million yen | % of total |
| Shipbuilding | 112,382 | 10.6 | 95,805 | 10.0 | 141,397 | 9.4 |
| Rolling Stock & Construction Machinery | 117,239 | 11.1 | 131,801 | 13.8 | 171,738 | 11.4 |
| Aerospace | 171,504 | 16.3 | 126,484 | 13.2 | 237,348 | 15.8 |
| Gas Turbines & Machinery | 130,384 | 12.4 | 138,835 | 14.5 | 185,486 | 12.3 |
| Plant & Infrastructure Engineering | 82,210 | 7.8 | 66,122 | 6.9 | 142,547 | 9.4 |
| Consumer Products & Machinery | 305,579 | 29.0 | 247,844 | 25.9 | 433,962 | 28.9 |
| Hydraulic Machinery | 61,035 | 5.8 | 68,216 | 7.1 | 84,027 | 5.5 |
| Other | 70,819 | 6.7 | 79,852 | 8.3 | 104,588 | 6.9 |
| Total | 1,051,155 | 100.0 | 954,962 | 100.0 | 1,501,097 | 100.0 |

### 3) Order backlog

| | Nine months ended December 31, 2007 | | Nine months ended December 31, 2008 | | Year ended March 31, 2008 | |
|---|---|---|---|---|---|---|
| | million yen | % of total | million yen | % of total | million yen | % of total |
| Shipbuilding | 414,175 | 27.0 | 376,865 | 23.0 | 382,663 | 24.8 |
| Rolling Stock & Construction Machinery | 431,376 | 28.1 | 474,205 | 28.9 | 465,839 | 30.2 |
| Aerospace | 248,332 | 16.1 | 206,017 | 12.5 | 239,653 | 15.5 |
| Gas Turbines & Machinery | 245,961 | 16.0 | 380,330 | 23.2 | 242,081 | 15.7 |
| Plant & Infrastructure Engineering | 135,288 | 8.8 | 128,972 | 7.8 | 155,882 | 10.1 |
| Consumer Products & Machinery | - | - | - | - | - | - |
| Hydraulic Machinery | 29,316 | 1.9 | 32,620 | 1.9 | 27,644 | 1.7 |
| Other | 29,211 | 1.9 | 37,988 | 2.3 | 27,190 | 1.7 |
| Total | 1,533,663 | 100.0 | 1,636,999 | 100.0 | 1,540,954 | 100.0 |

## Supplementary information on earnings forecasts for the fiscal year ending March 31, 2009

### (1) Consolidated earnings outlook

Billions of yen

| | Outlook for the year ending March 31, 2009 | | | Year ended March 31, 2008 |
|---|---|---|---|---|
| | Revised outlook | October 31,2009 | Change | |
| Net sales | 1,330 | 1,450 | (120) | 1,501.0 |
| Operating income | 18 | 44 | (26) | 76.9 |
| Recurring profit | 28 | 55 | (27) | 63.9 |
| Net income | 11 | 26 | (15) | 35.1 |
| Orders | 1,580 | 1,600 | (20) | 1,610.7 |
| Before-tax ROIC (%) | 4.9 | 8.8 | (3.9) | 11.2 |

Notes: 1. The expected foreign exchange rate used for the outlook: ¥90=US$1, ¥120=1 Euro
2. Before-tax ROIC = (income before income taxes + interest expense) / invested capital

### (2) Outlook by industry segment

#### 1) Net sales and operating income (loss)

Billions of yen

| | Outlook for the year ending March 31, 2009 | | | | | | Year ended March 31, 2008 | |
|---|---|---|---|---|---|---|---|---|
| | Revised outlook | | October 31,2009 | | Change | | | |
| | Net sales | Operating income (loss) | Net sales | Operating income (loss) | Net sales | Operating income (loss) | Net sales | Operating income (loss) |
| Shipbuilding | 120 | (7) | 120 | (1) | - | (6) | 141.3 | 3.2 |
| Rolling Stock & Construction Machinery | 190 | 7 | 210 | 9 | (20) | (2) | 171.7 | 7.1 |
| Aerospace | 180 | 0 | 190 | 4 | (10) | (4) | 237.3 | 10.8 |
| Gas Turbines & Machinery | 200 | 11 | 210 | 11 | (10) | - | 185.4 | 13.3 |
| Plant & Infrastructure Engineering | 110 | 10 | 120 | 11 | (10) | (1) | 142.5 | 10.8 |
| Consumer Products & Machinery | 340 | (14) | 380 | (2) | (40) | (12) | 433.9 | 19.6 |
| Hydraulic Machinery | 80 | 8 | 100 | 9 | (20) | (1) | 84.0 | 9.1 |
| Other | 110 | 3 | 120 | 3 | (10) | - | 104.5 | 2.5 |
| Total | 1,330 | 18 | 1,450 | 44 | (120) | (26) | 1,501.0 | 76.9 |

### 2) Orders

Billions of yen

| | Outlook for the year ending March 31, 2009 | | | Year ended March 31, 2008 |
|---|---|---|---|---|
| | Revised outlook | October 31,2009 | Change | |
| Shipbuilding | 70 | 110 | (40) | 251.3 |
| Rolling Stock & Construction Machinery | 280 | 300 | (20) | 183.2 |
| Aerospace | 220 | 220 | - | 202.5 |
| Gas Turbines & Machinery | 340 | 250 | 90 | 227.4 |
| Plant & Infrastructure Engineering | 120 | 120 | - | 106.0 |
| Consumer Products & Machinery | 340 | 380 | (40) | 433.9 |
| Hydraulic Machinery | 100 | 110 | (10) | 92.3 |
| Other | 110 | 110 | - | 113.9 |
| Total | 1,580 | 1,600 | (20) | 1,610.7 |