

## PART III

### Item 17. Financial Statements

Consolidated Financial Statements of Hitachi, Ltd. and Subsidiaries:

	<u>Page Number</u>
Independent Auditors' Report	47
Consolidated Balance Sheets as of March 31, 2001 and 2000	48
Consolidated Statements of Income for the years ended March 31, 2001, 2000 and 1999	49
Consolidated Statements of Stockholders' Equity for the years ended March 31, 2001, 2000 and 1999	50
Consolidated Statements of Cash Flows for the years ended March 31, 2001, 2000 and 1999	51
Notes to Consolidated Financial Statements	52

Schedule:

Independent Auditors' Report	47
Schedule II      Reserves for the years ended March 31, 2001, 2000 and 1999	89

All other schedules are omitted as permitted by the rules and regulations of the Securities and Exchange Commission, as the required information is presented in the notes to consolidated financial statements, or the schedules are not applicable.

Financial statements of affiliates are omitted because none of these meets the 20% level tests.

## Independent Auditors' Report

The Board of Directors and Stockholders  
Hitachi, Ltd.:

We have audited the consolidated financial statements of Hitachi, Ltd. and subsidiaries as listed in the accompanying index. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

The segment information required to be disclosed in financial statements under accounting principles generally accepted in the United States of America is not presented in the accompanying consolidated financial statements. Foreign issuers are presently exempted from such disclosure requirement in Securities Exchange Act filings with the United States Securities and Exchange Commission.

In our report dated May 17, 2000, our opinion on the consolidated financial statements of Hitachi, Ltd. and subsidiaries as of and for the years ended March 31, 2000 and 1999 was qualified because (1) the Company had stated investments in certain debt and equity securities at the lower of cost or fair value and (2) the Company omitted the segment information. As described in Note 1(e) to the consolidated financial statements, Hitachi, Ltd. and subsidiaries have changed their method of accounting for such investments in debt and equity securities and restated the consolidated financial statements as of and for the years ended March 31, 2000 and 1999 to conform with accounting principles generally accepted in the United States of America. Accordingly, our present opinion on the accompanying consolidated financial statements as of and for the years ended March 31, 2000 and 1999, as presented herein, is different from that expressed in our previous report.

In our opinion, except for the omission of segment information, as discussed in the third paragraph, the consolidated financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of Hitachi, Ltd. and subsidiaries as of March 31, 2001 and 2000, and the results of their operations and their cash flows for each of the years in the three-year period ended March 31, 2001 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

KPMG  
Tokyo, Japan  
May 17, 2001, except as to Note 1 (p) (ii) and (iii), which are as of July 31, 2001

HITACHI, LTD.  
AND SUBSIDIARIES

Consolidated Balance Sheets

March 31, 2001 and 2000

Assets	Yen (millions)		Liabilities and Stockholders' Equity	Yen (millions)	
	2001	2000		2001	2000
Cash and cash equivalents	¥ 1,381,603	1,357,432	Short-term debt (note 7)	¥ 1,199,209	1,046,571
Short-term investments (note 2)	433,650	632,434	Current installments of long-term debt (note 7)	412,646	259,099
Trade receivables:			Trade payables:		
Notes	309,459	298,866	Notes	138,161	98,058
Accounts	2,212,133	1,927,549	Accounts	1,160,789	974,721
Allowance for doubtful receivables and unearned income	(22,259)	(22,197)	Accrued expenses	786,813	706,647
Net trade receivables	<u>2,499,333</u>	<u>2,204,218</u>	Income taxes (note 6)	106,727	76,969
Inventories (note 4)	1,514,163	1,416,878	Advances received	385,741	382,085
Prepaid expenses and other current assets (note 6)	391,963	354,581	Other current liabilities (note 6)	432,571	395,686
Investment in leases (note 3)	623,789	-	Long-term debt (note 7)	1,881,270	1,482,810
Noncurrent receivables and restricted funds (note 5)	163,003	160,583	Retirement and severance benefits (note 8)	982,332	699,385
Investments and advances, including affiliated companies (note 2)	885,669	817,436	Other liabilities (notes 6 and 9)	73,689	81,718
Property, plant and equipment (notes 3 and 7):			Total liabilities	<u>7,559,948</u>	<u>6,203,749</u>
Land	386,785	380,076	Minority interests	825,158	791,925
Buildings	1,801,731	1,731,561	Stockholders' equity:		
Machinery and equipment	5,622,410	4,887,088	Common stock (notes 7 and 10)	281,754	281,738
Construction in progress	95,663	71,184	Capital surplus (note 10)	501,243	499,081
	<u>7,906,589</u>	<u>7,069,909</u>	Legal reserve (note 11)	109,815	106,885
Less accumulated depreciation	<u>5,231,632</u>	<u>4,515,160</u>	Retained earnings (notes 7 and 11)	2,157,136	2,082,541
Net property, plant and equipment	<u>2,674,957</u>	<u>2,554,749</u>	Accumulated other comprehensive income (loss) (note 12)	(188,446)	17,442
			Total stockholders' equity	<u>2,861,502</u>	<u>2,987,687</u>
Other assets (note 6)	678,478	485,050	Commitments and contingencies (note 13)		
	<u>11,246,608</u>	<u>9,983,361</u>		<u>11,246,608</u>	<u>9,983,361</u>

See accompanying notes to consolidated financial statements.

HITACHI, LTD.  
AND SUBSIDIARIES

Consolidated Statements of Income

Years ended March 31, 2001, 2000 and 1999

	Yen (millions)		
	2001	2000	1999
Revenues:			
Net sales (note 5)	¥ 8,416,982	8,001,203	7,977,374
Interest income	32,428	35,380	40,178
Dividends received	9,641	6,662	7,060
Other income (note 14)	27,544	30,059	1,144
Total revenues	8,486,595	8,073,304	8,025,756
Costs and expenses:			
Cost of sales	6,155,023	5,898,756	6,052,345
Selling, general and administrative expenses	1,919,647	1,928,083	1,959,103
Interest charges	58,759	52,015	59,028
Other deductions (note 14)	29,511	115,215	176,454
Total costs and expenses	8,162,940	7,994,069	8,246,930
Income (loss) before income taxes and minority interests	323,655	79,235	(221,174)
Income taxes (note 6)	164,861	47,502	97,660
Income (loss) before minority interests	158,794	31,733	(318,834)
Minority interests	54,414	14,811	8,777
Net income (loss)	¥ 104,380	16,922	(327,611)
Net income (loss) per share (note 15):		Yen	
Basic	¥ <u>31.27</u>	<u>5.07</u>	<u>(98.15)</u>
Diluted	¥ <u>30.32</u>	<u>4.99</u>	<u>(98.15)</u>

See accompanying notes to consolidated financial statements.

HITACHI, LTD.  
AND SUBSIDIARIES

Consolidated Statements of Stockholders' Equity  
Years ended March 31, 2001, 2000 and 1999

	Yen (millions)		
	2001	2000	1999
Common stock (notes 7 and 10):			
Balance at beginning of year	¥ 281,738	281,735	281,735
Conversion of convertible debentures	16	3	-
Balance at end of year	¥ <u>281,754</u>	<u>281,738</u>	<u>281,735</u>
Capital surplus (note 10):			
Balance at beginning of year	¥ 499,081	494,782	492,272
Conversion of convertible debentures	1,069	3,954	2,190
Increase arising from sale of subsidiaries' common stock and other	1,093	345	320
Balance at end of year	¥ <u>501,243</u>	<u>499,081</u>	<u>494,782</u>
Legal reserve (note 11):			
Balance at beginning of year	¥ 106,885	105,905	104,370
Transfers from retained earnings	2,971	1,271	1,591
Transfers to minority interests arising from conversion of subsidiaries' convertible debentures	(17)	(94)	(37)
Transfers to minority interests arising from sale of subsidiaries' common stock and other	(24)	(197)	(19)
Balance at end of year	¥ <u>109,815</u>	<u>106,885</u>	<u>105,905</u>
Retained earnings (notes 7 and 11):			
Balance at beginning of year as previously reported	¥ 2,066,085	2,083,936	2,443,886
Restatement (note 1(e))	16,456	16,456	7,151
Balance at beginning of year as restated	2,082,541	2,100,392	2,451,037
Net income (loss)	104,380	16,922	(327,611)
Cash dividends	(28,371)	(28,371)	(18,358)
Transfers to legal reserve	(2,971)	(1,271)	(1,591)
Transfers to minority interests arising from conversion of subsidiaries' Convertible debentures	(347)	(2,291)	(727)
Transfers from (to) minority interests arising from sale of subsidiaries' common stock and other	1,904	(2,840)	(2,358)
Balance at end of year	¥ <u>2,157,136</u>	<u>2,082,541</u>	<u>2,100,392</u>
Accumulated other comprehensive income (loss) (note 12):			
Balance at beginning of year as previously reported	¥ (77,577)	(58,065)	(43,860)
Restatement (note 1(e))	95,019	81,266	94,957
Balance at beginning of year as restated	17,442	23,201	51,097
Other comprehensive loss, net of reclassification adjustments	(205,111)	(5,343)	(28,273)
Transfers from (to) minority interests arising from conversion of subsidiaries' convertible debentures	(9)	(4)	1
Transfers from (to) minority interests arising from sale of subsidiaries' common stock and other	(768)	(412)	376
Balance at end of year	¥ <u>(188,446)</u>	<u>17,442</u>	<u>23,201</u>
Total stockholders' equity	¥ <u>2,861,502</u>	<u>2,987,687</u>	<u>3,006,015</u>
Comprehensive income (loss)(note 12):			
Net income (loss)	¥ 104,380	16,922	(327,611)
Other comprehensive loss arising during the year	(194,560)	(2,066)	(32,556)
Reclassification adjustments for net loss (gain) included in net income (loss)	(10,551)	(3,277)	4,283
Comprehensive income (loss)	¥ <u>(100,731)</u>	<u>11,579</u>	<u>(355,884)</u>

See accompanying notes to consolidated financial statements.

HITACHI, LTD.  
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended March 31, 2001, 2000 and 1999

	Yen (millions)		
	2001	2000	1999
Cash flows from operating activities (note 17):			
Net income (loss)	¥ 104,380	16,922	(327,611)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation	505,507	541,253	547,022
Impairment loss for long-lived assets	-	9,310	2,740
Deferred income taxes	12,505	(67,179)	(22,976)
Gain on sale of investments and subsidiaries' common stock	(17,437)	(36,215)	(3,938)
Loss on disposal of rental assets and other property	19,165	19,921	69,996
Income applicable to minority interests	54,414	14,811	8,777
Increase in receivables	(72,035)	(107,685)	(2,549)
(Increase) decrease in inventories	(128,477)	(26,273)	127,802
Increase in prepaid expenses and other current assets	(38,234)	(9,931)	(1,133)
Increase (decrease) in payables	95,855	78,728	(45,274)
Increase in accrued expenses and retirement and severance benefits	8,171	3,846	19,400
Increase (decrease) in accrued income taxes	26,337	15,884	(25,135)
Increase (decrease) in other liabilities	(62,858)	(41,385)	25,338
Other	28,140	39,443	16,420
Net cash provided by operating activities	535,433	451,450	388,879
Cash flows from investing activities (note 17):			
(Increase) decrease in short-term investments	198,610	(15,155)	153,382
Capital expenditures	(463,585)	(365,744)	(406,685)
Purchase of assets to be leased	(532,142)	(211,185)	(212,657)
Collection of investment in leases	421,527	-	-
Proceeds from disposition of rental assets and other property	70,442	133,806	26,427
Proceeds from sale of investments and subsidiaries' common stock	50,473	67,971	16,542
Purchase of investments and subsidiaries' common stock	(125,473)	(40,463)	(13,837)
Other	9,431	(4,821)	(13,721)
Net cash used in investing activities	(370,717)	(435,591)	(450,549)
Cash flows from financing activities (note 17):			
Increase (decrease) in short-term debt	(5,153)	43,155	(1,845)
Proceeds from long-term debt	518,872	315,408	375,344
Payments on long-term debt	(642,594)	(194,038)	(230,273)
Proceeds from sale of common stock by subsidiaries	13,342	9,046	701
Dividends paid to stockholders	(28,235)	(27,762)	(18,412)
Dividends paid to minority stockholders of subsidiaries	(15,739)	(12,033)	(11,722)
Purchase and retirement of common shares by subsidiaries	-	(7,946)	-
Net cash provided by (used in) financing activities	(159,507)	125,830	113,793
Effect of exchange rate changes on cash and cash equivalents	18,962	(21,784)	(14,136)
Net increase in cash and cash equivalents	24,171	119,905	37,987
Cash and cash equivalents at beginning of year	1,357,432	1,237,527	1,199,540
Cash and cash equivalents at end of year	¥ 1,381,603	1,357,432	1,237,527

See accompanying notes to consolidated financial statements.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(1) Basis of Presentation and Summary of Significant Accounting Policies

(a) Basis of Presentation

Hitachi, Ltd. (the Company) and its domestic subsidiaries maintain their books of account in conformity with the financial accounting standards of Japan, and its foreign subsidiaries in conformity with those of the countries of their domicile.

The consolidated financial statements presented herein have been prepared in a manner and reflect the adjustments which are necessary to conform them with accounting principles generally accepted in the United States of America. Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements. Actual results could differ from those estimates.

The Company changed its balance sheet presentation from classified to unclassified balance sheets in the current year. The change was implemented with the Company's acquisition of Hitachi Leasing, Ltd., a financing company, as it believes that unclassified balance sheets more appropriately reflect its financial position.

(b) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and those of its majority-owned subsidiaries, whether directly or indirectly controlled. Intercompany accounts and significant intercompany transactions have been eliminated in consolidation. The investments in affiliated companies are stated at their underlying equity value, and the appropriate portion of the earnings of such companies is included in consolidated income.

(c) Cash Equivalents

For the purpose of the statement of cash flows, the Company considers all highly liquid investments with insignificant risk of changes in value which have maturities of generally three months or less when purchased to be cash equivalents.

(d) Foreign Currency Translation

Foreign currency financial statements have been translated in accordance with Statement of Financial Accounting Standards (SFAS) No. 52, "Foreign Currency Translation." Under this standard, the assets and liabilities of the Company's subsidiaries located outside Japan are translated into Japanese yen at the rates of exchange in effect at the balance sheet date. Income and expense items are translated at the average exchange rates prevailing during the year. Gains and losses resulting from foreign currency transactions are included in other income (deductions), and those resulting from translation of financial statements are excluded from the consolidated statements of income and are reported in other comprehensive income (loss).

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(e) Investment in Securities

Effective April 1, 2000, the Company adopted SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Prior to the adoption of SFAS No. 115, the Company disclosed the effect of the departure from SFAS No. 115 in a footnote to the consolidated financial statements. The United States Securities and Exchange Commission (SEC) Division of Corporation Finance approved this presentation in a letter dated August 16, 1993.

With the adoption of SFAS No. 115, the Company's prior period financial statements have been restated to reflect the change in accounting principle. As a result of the restatement, total assets increased ¥146,163 million, stockholders' equity increased ¥111,475 million and comprehensive income increased ¥13,747 million in the consolidated financial statements as of and for the year ended March 31, 2000, and comprehensive loss increased ¥4,365 million in the consolidated financial statements for the year ended March 31, 1999. There was no effect and a gain of ¥9,305 million on previously reported net income (loss) for the years ended March 31, 2000 and 1999, respectively. Under SFAS No. 115, investments in equity securities that have readily determinable fair values and all investments in debt securities are to be classified in three categories and accounted for as follows:

- Debt securities that the company has the positive intent and ability to hold to maturity are classified as held-to-maturity securities and reported at amortized cost.
- Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings.
- Debt and equity securities not classified as either held-to-maturity securities or trading securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

A decline in fair value of any available-for-sale or held-to-maturity security below the amortized cost basis that is deemed to be other than temporary results in a write-down of the cost basis to fair value as a new cost basis and the amount of the write-down is included in earnings. The cost of a security sold or the amount reclassified out of accumulated other comprehensive income into earnings was determined by the average method.

(f) Inventories

Inventories are stated at the lower of cost or market. Cost is determined by the specific identification method for job order inventories and generally by the average method for raw materials and other inventories.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(g) Property, Plant and Equipment

Property, plant and equipment are stated at cost. Property, plant and equipment are principally depreciated by the declining-balance method, except for some assets which are depreciated by the straight-line method, over the following estimated useful lives:

Buildings	3 to 60 years
Machinery and equipment	2 to 20 years

Effective April 1, 1998, the Company and certain domestic subsidiaries changed their method of depreciation for buildings placed in service after April 1, 1998 to the straight-line method. The Company believes that the straight-line method more appropriately reflects its financial results by better allocating costs of new buildings over the useful lives of these assets. The change was applied on a prospective basis to buildings acquired after that date. The effect of this change on net loss for the year ended March 31, 1999 was not material.

(h) Derivative Financial Instruments

The Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" for the year ended March 31, 2001. SFAS No. 133 requires that all derivative financial instruments, such as forward exchange and interest rate swap contracts, be recognized in the financial statements and measured at fair value regardless of the purpose or intent for holding them and recognized as either assets or liabilities. The accounting for changes in fair value depends on the intended use of the derivative financial instruments and its resulting hedge designation. The adoption of SFAS No. 133 did not have a material effect on the Company's consolidated financial statements.

All derivatives are recognized on the balance sheet at their fair value. The Company designates and accounts for the derivative as follows:

- "Fair value" hedge: a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment. The changes in fair value of the recognized assets or liabilities or unrecognized firm commitment and the derivatives are recorded in earnings if the hedge is considered highly effective.
- "Cash flow" hedge: a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability. The changes in the fair value of the derivatives designated as cash flow hedges are recorded as other comprehensive income if the hedge is considered highly effective. This treatment is continued until earnings are affected by the variability in cash flows or the unrecognized firm commitment of the designated hedged item. The ineffective portion of the hedge is reported in earnings immediately.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

- “Foreign currency” hedge: a hedge of foreign-currency fair value or cash flow. The changes in fair value of the recognized assets or liabilities or unrecognized firm commitment and the derivatives are recorded as either earnings or other comprehensive income if the hedge is considered highly effective. Recognition as earnings or other comprehensive income is dependent on the treatment of foreign currency hedges as fair value or cash flow hedges.

The Company meets the documentation requirements as prescribed by the standard, which includes risk management objective and strategy for undertaking various hedge transactions. In addition, a formal assessment is made periodically at the hedge’s inception and on an ongoing basis, as to whether the derivative used in hedging activities is highly effective in offsetting changes in fair values or cash flows of hedged items. Hedge accounting is discontinued for ineffective hedges, if any. Discontinued hedges are recognized in earnings immediately.

(i) Revenue Recognition

Staff Accounting Bulletin No. 101 (SAB 101) expresses certain of the SEC’s views in applying generally accepted accounting principles to revenue recognition in the financial statements. Under SAB 101, revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred or services are rendered, the sales price is fixed and determinable and collectibility is probable.

These criteria are met for the Company’s sales and related cost of sales and revenue is generally recognized when products are shipped, delivered and services are rendered. The timing of revenue recognition varies among the Company’s products. Sales and related cost of sales under certain long-term construction contracts are recognized under the percentage of completion method. The Company’s products are generally subject to warranty and the Company provides for the estimated future costs of repair and replacement in cost of sales when sales are recognized. Income on financing leases is recognized by a method which produces a constant periodic rate of return on the outstanding investment in the lease.

(j) Advertising

The Company expenses advertising costs as incurred.

(k) Income Taxes

Deferred income taxes are accounted for under the asset and liability method in accordance with SFAS No. 109, “Accounting for Income Taxes.” Deferred tax assets and liabilities are recognized for the expected future tax consequences of events that have been included in the consolidated financial statements or tax returns. Under this method, deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under SFAS No. 109, the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(l) Sales of Stock by Subsidiaries

The change in the Company's proportionate share of subsidiary equity resulting from issuance of stock by the subsidiaries is accounted for as an equity transaction.

(m) Net Income (Loss) Per Share

Net income (loss) per share amounts are computed in accordance with SFAS No. 128, "Earnings per Share." This standard requires a dual presentation of basic and diluted net income (loss) per share amounts on the face of the statement of income. Under this standard, basic net income (loss) per share is computed based upon the weighted average number of shares of common stock outstanding during each year. Diluted net income (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock.

(n) Stock-based Compensation

The Company accounts for its stock option plan in accordance with Accounting Principles Board Opinion No. 25 (APB 25), "Accounting for Stock Issued to Employees." Under APB 25, the Company recognizes no compensation expense related to employee stock options, as no options are granted at a price below the market price on the day of grant.

SFAS No. 123, "Accounting for Stock-based Compensation," prescribes the recognition of compensation expense based on the fair value of options on the grant date. Continuous application of APB 25 is allowed under this standard if certain pro forma disclosures are made assuming hypothetical fair value method application. The Company elected to continue applying APB 25 and provide pro forma disclosure in accordance with SFAS No. 123.

(o) Disclosures about Segments of an Enterprise and Related Information

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," was issued in June 1997. This standard establishes standards for the manner in which a public business enterprise is required to report financial and descriptive information about its operating segments. This standard defines operating segments as components of an enterprise for which separate financial information is available and evaluated regularly as a means for assessing segment performance and allocating resources to segments. A measure of profit or loss, total assets and other related information is required to be disclosed for each operating segment. Further, this standard requires the disclosure of information concerning revenues derived from the enterprise's products or services, countries in which it earns revenue or holds assets and major customers. This standard is effective for the Company's fiscal year ended March 31, 1999. However, foreign issuers are presently exempted from the segment disclosure requirements of SFAS No. 131 in Securities Exchange Act filings with the SEC, and the Company has not presented the segment information required to be disclosed in the footnotes to the consolidated financial statements under SFAS No. 131.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(p) New Accounting Standards

- (i) SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities – a replacement of FASB No. 125" was issued in September 2000. This statement revises the standards for accounting for securitizations and other transfers of financial assets and collateral and requires certain financial statement disclosures. SFAS No. 140 is effective for transactions occurring after March 31, 2001. The management does not anticipate a material effect on the Company's financial position or results of operations with the adoption of this statement.
- (ii) In June 2001, the Financial Accounting Standards Board (FASB) issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001 as well as all purchase method business combinations completed after June 30, 2001. SFAS No. 141 also specifies criteria intangible assets acquired in a purchase method business combination must meet to be recognized and reported apart from goodwill, noting that any purchase price allocable to an assembled workforce may not be accounted for separately. SFAS No. 142 will require that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142. SFAS No. 142 will also require that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of."

The Company is required to adopt the provisions of SFAS No. 141 immediately, except with regard to business combinations initiated prior to July 1, 2001, which it expects to account for using the pooling-of-interests method, and SFAS No. 142 effective April 1, 2002. Companies with fiscal year ends beginning after March 15, 2001, who have not yet issued financial statements for their first interim period may early adopt SFAS No. 142. Furthermore, goodwill and intangible assets determined to have an indefinite useful life acquired in a purchase business combination completed after June 30, 2001, but before SFAS No. 142 is adopted in full will not be amortized, but will continue to be evaluated for impairment in accordance with the appropriate pre- SFAS No. 142 accounting literature. Goodwill and intangible assets acquired in business combinations completed before July 1, 2001 will continue to be amortized and tested for impairment in accordance with the appropriate pre- SFAS No. 142 accounting requirements prior to the adoption of SFAS No. 142.

SFAS No. 141 will require upon adoption of SFAS No. 142, that the Company evaluate its existing intangible assets and goodwill that were acquired in a prior purchase business combination, and to make any necessary reclassifications in order to conform with the new criteria in SFAS No. 141 for recognition apart from goodwill. Upon adoption of SFAS No. 142, the Company will be required to reassess the useful lives and residual values of all intangible assets acquired, and make any necessary amortization period adjustments by the end of the first interim period after adoption. In addition, to the extent an intangible asset is identified as having an indefinite useful life, the Company will be required to test the intangible asset for impairment in accordance with the provisions of SFAS No. 142 within the first interim period. Any impairment loss will be measured as of the date of adoption and recognized as the cumulative effect of a change in accounting principle in the first interim period.

In connection with SFAS No. 142's transitional goodwill impairment evaluation, the SFAS No. 142 will require the Company to perform an assessment of whether there is an indication that goodwill and

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

equity-method goodwill is impaired as of the date of adoption. To accomplish this, the Company must identify its reporting units and determine the carrying value of each reporting unit by assigning the assets and liabilities, including the existing goodwill and intangible assets, to those reporting units as of the date of adoption. The Company will then have up to six months from the date of adoption to determine the fair value of each reporting unit and compare it to the reporting unit's carrying amount. To the extent a reporting unit's carrying amount exceeds its fair value, an indication exists that the reporting unit's goodwill may be impaired and the Company must perform the second step of the transitional impairment test. In the second step, the Company must compare the implied fair value of the reporting unit's goodwill, determined by allocating the reporting unit's fair value to all of its assets (recognized and unrecognized) and liabilities in a manner similar to a purchase price allocation in accordance with SFAS No. 141, to its carrying amount, both of which would be measured as of the date of adoption. This second step is required to be completed as soon as possible, but no later than the end of the year of adoption. Any transitional impairment loss will be recognized as the cumulative effect of a change in accounting principle in the Company's statement of earnings. And finally, any unamortized negative goodwill and equity-method negative goodwill existing at the date SFAS No. 142 is adopted must be written off as the cumulative effect of a change in accounting principle. The Company is currently assessing the impact of implementing these statements.

(iii) In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations," which addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The standard applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and (or) normal use of the asset.

SFAS No. 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The fair value of the liability is added to the carrying amount of the associated asset and this additional carrying amount is depreciated over the life of the asset. The liability is accreted at the end of each period through charges to operating expense. If the obligation is settled for other than the carrying amount of the liability, the Company will recognize a gain or loss on settlement.

The Company is required and plans to adopt the provisions of SFAS No. 143 for the fiscal years beginning after June 15, 2002. Because of the effort necessary to comply with the adoption of SFAS No. 143, it is not practicable for management to estimate the impact of adopting this Statement at the date of this report.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(2) Investment in Securities

The following is a summary of the amortized cost basis, gross unrealized holding gains, gross unrealized holding losses and aggregate fair value of available-for-sale securities by the consolidated balance sheets classification as of March 31, 2001 and 2000.

		Yen (millions)							
		2001				2000			
		Amortized <u>cost basis</u>	Gross <u>gains</u>	Gross <u>losses</u>	Aggregate <u>fair value</u>	Amortized <u>cost basis</u>	Gross <u>gains</u>	Gross <u>losses</u>	Aggregate <u>fair value</u>
Short-term investments:									
Equity securities	¥	-	-	-	-	34,480	63,204	-	97,684
Bonds and debentures		116,423	69	159	116,333	175,126	406	-	175,532
Other securities		<u>63,500</u>	<u>49</u>	<u>104</u>	<u>63,445</u>	<u>102,502</u>	<u>190</u>	<u>-</u>	<u>102,692</u>
		179,923	118	263	179,778	312,108	63,800	-	375,908
Investments and advances:									
Equity securities		263,396	150,648	23,055	390,989	208,668	155,140	-	363,808
Bonds and debentures		117,348	984	1,453	116,879	87,230	175	-	87,405
Other securities		<u>36,588</u>	<u>1,280</u>	<u>680</u>	<u>37,188</u>	<u>14,846</u>	<u>18</u>	<u>-</u>	<u>14,864</u>
		<u>417,332</u>	<u>152,912</u>	<u>25,188</u>	<u>545,056</u>	<u>310,744</u>	<u>155,333</u>	<u>-</u>	<u>466,077</u>
	¥	<u>597,255</u>	<u>153,030</u>	<u>25,451</u>	<u>724,834</u>	<u>622,852</u>	<u>219,133</u>	<u>-</u>	<u>841,985</u>

As of March 31, 2001, certain subsidiaries hold held-to-maturity securities, which consist mainly of bonds and debentures amounting to ¥10,414 million and ¥9,508 million in Short-term investments and Investments and advances in the consolidated balance sheet, respectively. Gross unrealized holding gains and losses of these securities are not material.

Trading securities classified as Short-term investments as of March 31, 2001, which consist mainly of investment in trust accounts, are ¥243,458 million.

Bonds and debentures consist mainly of national, local and foreign governmental bonds, debentures issued by banks and corporate bonds. Other securities consist mainly of trust funds.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The contractual maturities of bonds and debentures and other securities classified as Investment and advances in the consolidated balance sheet as of March 31, 2001 are as follows:

		Yen (millions)		
		<u>2001</u>		
		<u>Held-to- maturity</u>	<u>Available- for-sale</u>	<u>Total</u>
Due within five years	¥	9,176	74,105	83,281
Due after five years		<u>332</u>	<u>79,962</u>	<u>80,294</u>
	¥	<u>9,508</u>	<u>154,067</u>	<u>163,575</u>

Expected redemptions differ from contractual maturities because these securities are redeemable at the option of the issuers.

The proceeds from sale of available-for-sale securities for the years ended March 31, 2001, 2000 and 1999 are ¥167,923 million, ¥117,476 million and ¥123,647 million, respectively, the gross realized gains on those sales for the years then ended are ¥10,525 million, ¥16,481 million and ¥14,168 million, respectively, and the gross realized losses on those sales for the year ended March 31, 2001 are ¥460 million. In addition, during the year ended March 31, 2001, certain subsidiaries contributed their available-for-sale securities, in the amount of ¥25,684 million at fair value, to pension fund trusts. Gross realized gains on those contributions for the year ended March 31, 2001 are ¥15,651 million.

The change in net unrealized holding gain on available-for-sale securities which has been included in accumulated other comprehensive income for the years ended March 31, 2001, 2000 and 1999 is a decrease of ¥43,978 million, an increase of ¥13,753 million and a decrease of ¥13,691 million, respectively. The change in net unrealized holding loss on trading securities which has been included in earnings for the year ended March 31, 2001 is an increase of ¥13,659 million.

The aggregate fair value of investments in affiliated companies based on the quoted market price as of March 31, 2001 and 2000 is ¥210,890 million and ¥239,070 million, respectively. The aggregate carrying amount of such investments as of March 31, 2001 and 2000 is ¥158,719 million and ¥146,448 million, respectively.

(3) Leases

Certain subsidiaries are the lessor of manufacturing machinery and equipment under financing and operating leasing arrangements with terms ranging from 3 to 6 years.

Machinery and equipment at cost under operating leases and accumulated depreciation as of March 31, 2001 amounted to ¥1,084,159 million and ¥792,176 million, respectively. The leased assets are recorded at cost and depreciated using the straight-line method over their estimated useful lives.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The following table shows the future minimum lease receivables of financing and non-cancelable operating leases as of March 31, 2001:

<u>Years ending March 31</u>	<u>Yen (millions)</u>	
	<u>2001</u>	
	<u>Financing</u>	<u>Operating</u>
	<u>leases</u>	<u>leases</u>
2002	¥ 271,715	42,436
2003	183,834	32,265
2004	123,317	21,934
2005	72,812	10,803
2006	27,967	1,606
Thereafter	<u>26,415</u>	<u>22</u>
Total minimum payments to be received	706,060	<u>109,066</u>
Amount representing executory costs	(37,474)	
Minimum lease payments receivable	668,586	
Unearned income	<u>(44,797)</u>	
Net investment in financing leases	¥ <u><u>623,789</u></u>	

Provisions for losses on lease investments are determined on the basis of loss experience and assessment of inherent risks. Resulting adjustments to the allowance for losses are made to adjust the net investment in financing leases to an estimated collectible amount.

The Company and its subsidiaries are the lessee of certain manufacturing machinery and equipment. Amount of leased assets at cost under capital leases and accumulated depreciation amounted to ¥18,649 million and ¥9,699 million, respectively.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The following table shows the future minimum lease payments of capital and non-cancelable operating leases as of March 31, 2001:

<u>Years ending March 31</u>	<u>Yen (millions)</u>	
	<u>2001</u>	
	<u>Capital</u>	<u>Operating</u>
	<u>leases</u>	<u>leases</u>
2002	¥ 3,447	6,222
2003	2,943	3,695
2004	1,702	2,723
2005	1,112	2,171
2006	562	1,919
Thereafter	<u>3,145</u>	<u>8,185</u>
Total minimum lease payments	12,911	<u>24,915</u>
Amount representing executory costs	(277)	
Amount representing interest	<u>(1,419)</u>	
Present value of net minimum lease payments	11,215	
Less current portion of capital lease obligations	<u>3,127</u>	
Long-term capital lease obligations	¥ <u><u>8,088</u></u>	

(4) Inventories

Inventories as of March 31, 2001 and 2000 are summarized as follows:

	<u>Yen (millions)</u>	
	<u>2001</u>	<u>2000</u>
Finished goods	¥ 448,853	364,553
Work in process	873,324	885,189
Raw materials	<u>191,986</u>	<u>167,136</u>
	¥ <u><u>1,514,163</u></u>	<u><u>1,416,878</u></u>

Inventories include items associated with major contracts which, because of long-term processing requirements, have been or are expected to be performed over a period of more than 12 months. Those items as of March 31, 2001 and 2000 aggregated ¥284,305 million and ¥288,270 million, respectively.

(5) Noncurrent Receivables and Restricted Funds

Noncurrent receivables and restricted funds as of March 31, 2001 and 2000 are summarized as follows:

	<u>Yen (millions)</u>	
	<u>2001</u>	<u>2000</u>
Housing loans to employees	¥ 23,242	24,094
Trade receivables not due within one year, interest-bearing	29,230	27,854
Other receivables and restricted funds	<u>110,531</u>	<u>108,635</u>
	¥ <u><u>163,003</u></u>	<u><u>160,583</u></u>

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

Housing loans to employees are made with repayment terms ranging from 10 to 25 years.

The aggregated annual maturities of the noncurrent trade receivables after March 31, 2002 are as follows:

<u>Years ending March 31</u>	Yen (millions)
2003	¥ 13,757
2004	5,884
2005	2,156
2006	1,420
Thereafter	<u>6,013</u>
	¥ <u>29,230</u>

Sales on an installment contract basis for the years ended March 31, 2001, 2000 and 1999 totaled ¥11,663 million, ¥11,736 million and ¥12,317 million, respectively.

(6) Income Taxes

Significant components of income tax expense (benefit) attributable to continuing operations and other comprehensive income (loss), net of reclassification adjustments, for the years ended March 31, 2001, 2000 and 1999 are as follows:

	<u>Yen (millions)</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
Continuing operations:			
Current tax expense	¥ 152,356	114,681	120,636
Deferred tax benefit (exclusive of the effects of other components listed below)	(892)	(84,085)	(173,071)
Adjustment to deferred tax assets and liabilities for enacted changes in tax laws and rates in Japan	-	-	57,365
Change in valuation allowance	<u>13,397</u>	<u>16,906</u>	<u>92,730</u>
	164,861	47,502	97,660
Other comprehensive income (loss), net of reclassification adjustments:			
Minimum pension liability adjustments	(149,588)	-	-
Net unrealized holding gain on available-for-sale securities	(37,832)	10,845	(14,900)
Cash flow hedges	<u>490</u>	<u>-</u>	<u>-</u>
	<u>(186,930)</u>	<u>10,845</u>	<u>(14,900)</u>
	¥ <u>(22,069)</u>	<u>58,347</u>	<u>82,760</u>

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The Company and its subsidiaries are subject to a number of taxes based on income. The aggregated normal tax rate for domestic companies was 41.8% in 2001 and 2000 and 47.4% in 1999. In accordance with SFAS No. 109, the effect of a change in the normal tax rate on deferred tax assets, liabilities and related valuation allowance, which amounted to ¥47,700 million for the year ended March 31, 1999, was charged to income.

Reconciliations between the normal income tax rate and the effective income tax rate as a percentage of income (loss) before income taxes and minority interests are as follows:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Normal income tax rate	41.8%	41.8%	(47.4)%
Equity in earnings of affiliated companies	(0.3)	3.4	1.5
Adjustment of net gain (loss) on sale of subsidiaries' common stock	(0.1)	(8.1)	2.2
Expenses not deductible for tax purposes	6.0	14.6	9.7
Adjustment to deferred tax assets and liabilities for enacted changes in tax laws and rates in Japan	-	-	25.9
Change in valuation allowance	4.1	21.3	41.9
Difference in statutory tax rates of foreign subsidiaries	(2.3)	(14.7)	10.5
Other	<u>1.7</u>	<u>1.7</u>	<u>(0.1)</u>
Effective income tax rate	<u>50.9%</u>	<u>60.0%</u>	<u>44.2%</u>

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities as of March 31, 2001 and 2000 are presented below:

	Yen (millions)	
	2001	2000
Total gross deferred tax assets:		
Retirement and severance benefits	¥ 341,827	207,686
Accrued expenses	124,759	88,791
Net intercompany profit on inventories, property, plant and equipment, and others	76,231	54,685
Depreciation	32,317	32,336
Net operating loss carryforwards	176,103	201,836
Other	187,480	194,733
	938,717	780,067
Valuation allowance	(157,621)	(142,839)
	781,096	637,228
Total gross deferred tax liabilities:		
Deferred profit on sale of properties	(36,030)	(36,868)
Tax purpose reserves regulated by Japanese tax law	(37,442)	(37,008)
Net unrealized gain on securities	(56,590)	(89,506)
Other	(15,762)	(9,860)
	(145,824)	(173,242)
Net deferred tax assets	¥ 635,272	463,986

Net deferred tax assets and liabilities as of March 31, 2001 and 2000 are reflected in the accompanying consolidated balance sheets under the following captions:

	Yen (millions)	
	2001	2000
Prepaid expenses and other current assets	¥ 187,409	157,576
Other assets	484,433	347,242
Other current liabilities	(22,946)	(27,782)
Other liabilities	(13,624)	(13,050)
Net deferred tax assets	¥ 635,272	463,986

Under the tax laws of various jurisdictions in which the Company and its subsidiaries operate, the valuation allowance was recorded against deferred tax assets for deductible temporary differences, net operating loss carryforwards and tax credit carryforwards. The net change in the total valuation allowance for the years ended March 31, 2001 and 2000 was an increase of ¥14,782 million and ¥11,335 million, respectively.

As of March 31, 2001, the Company and various subsidiaries have net operating loss carryforwards for income tax purposes of ¥452,114 million which are available to offset future taxable income, if any. Most of these net operating loss carryforwards expire by March 31, 2005.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

In assessing the realizability of deferred tax assets, management of the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is entirely dependent upon the generation of future taxable income in specific tax jurisdictions during the periods in which these deductible differences become deductible. Although realization is not assured, management considered the scheduled reversals of deferred tax liabilities and projected future taxable income in making this assessment. Based on these factors, management believes it is more likely than not the Company will realize the benefits of these deductible differences, net of the existing valuation allowance as of March 31, 2001.

The Company has not provided for deferred income tax liabilities on undistributed earnings of foreign subsidiaries and affiliated companies that are considered to be reinvested indefinitely. Such undistributed earnings, if remitted, generally would not result in material additional Japanese income taxes because of available foreign tax credits.

(7) Short-term and Long-term Debt

The components of short-term debt as of March 31, 2001 and 2000 are summarized as follows:

	Yen (millions)	
	2001	2000
Borrowings mainly from banks	¥ 1,033,638	840,468
Commercial paper	<u>165,571</u>	<u>206,103</u>
	¥ <u><u>1,199,209</u></u>	<u><u>1,046,571</u></u>

The weighted average interest rates on short-term debt outstanding as of March 31, 2001 and 2000 are 0.5% and 0.2%, respectively.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The components of long-term debt as of March 31, 2001 and 2000 are summarized as follows:

	Yen (millions)	
	2001	2000
Mortgage debentures:		
Due 2002 - 2004, interest 2.1 - 2.8%, issued by a subsidiary	¥ 400	400
Unsecured notes and debentures:		
Due 2006, interest 3.45% debenture	200,000	200,000
Due 2001 - 2011, interest 0.35 - 7.0%, issued by subsidiaries	814,720	826,152
Unsecured convertible debentures:		
5th series, due 2002, interest 1.7%	28,790	28,822
6th series, due 2003, interest 1.3%	92,828	92,828
7th series, due 2004, interest 1.4%	218,471	218,471
Due 2002 - 2004, interest 0.5 - 2.25%, issued by subsidiaries	73,309	88,026
Loans, principally from banks and insurance companies:		
Secured by various assets and mortgages on property, plant and equipment, maturing 2001 - 2013, interest 1.65 - 5.95%	15,591	20,983
Unsecured, maturing 2001 - 2015, interest 0.6 - 6.96%	838,592	266,227
Capital lease obligations	11,215	-
	2,293,916	1,741,909
Less current installments	412,646	259,099
	¥ 1,881,270	1,482,810

The aggregate annual maturities of long-term debt after March 31, 2002 are as follows:

Years ending March 31	Yen (millions)
2003	¥ 349,613
2004	394,602
2005	382,249
2006	380,692
Thereafter	374,114
	¥ 1,881,270

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The Company and its subsidiaries provide their investment in certain subsidiaries as collateral for bank loans of ¥45,271 million. The collateralized number of shares and their fair values as of March 31, 2001 are as follows:

<u>Subsidiary name</u>	<u>Number of shares owned in thousand</u>	<u>Percent of ownership</u>	<u>Collateralized number of shares in thousand</u>	<u>Yen (millions) Fair value as of March 31, 2001</u>
Hitachi Capital Corporation	71,150	53.0%	20,500	¥ 52,685
Hitachi Software Engineering Co., Ltd.	33,258	52.6	1,200	8,820
Hitachi Maxell, Ltd.	51,797	52.4	4,800	7,584
Hitachi Powdered Metals Co., Ltd.	17,072	53.4	7,750	6,200
Hitachi Metals Techno, Ltd.	11,863	65.5	450	230

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

Generally, the mortgage debenture trust agreements and certain secured and unsecured loan agreements provide, among other things, that the lenders or trustees shall have the right to have any distribution of earnings, including the payment of dividends and the issuance of additional capital stock, submitted to them for prior approval and also grant them the right to request additional security or mortgages on property, plant and equipment.

The unsecured convertible debentures due in 2002 are currently convertible into approximately 28,437,000 shares of common stock.

The unsecured convertible debentures due in 2003 are redeemable in whole or in part, at the option of the Company, from October 1, 1996 to September 30, 2002 at premiums ranging from 6% to 1%, and at par thereafter. The debentures are currently convertible into approximately 49,503,000 shares of common stock. Commencing September 30, 1999, the Company is required to make annual payments to the Trustee of ¥10 billion less the aggregate amounts of the debentures converted, repurchased or redeemed which have not been deducted before.

The unsecured convertible debentures due in 2004 are redeemable in whole or in part, at the option of the Company, from October 1, 1997 to September 30, 2003 at premiums ranging from 6% to 1%, and at par thereafter. The debentures are currently convertible into approximately 128,945,000 shares of common stock. Commencing September 30, 1999, the Company is required to make annual payments to the Trustee of ¥20 billion less the aggregate amounts of the debentures converted, repurchased or redeemed which have not been deducted before.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

In accordance with Trustee agreements for the unsecured debentures due in 2003 and 2004 as mentioned above, the 6,729 thousand shares of investments in Hitachi Software Engineering Co., Ltd. are held in trust. The fair value of the shares held in trust is ¥49,458 million as of March 31, 2001.

Pursuant to the terms of the indentures under which the unsecured convertible debentures due in 2004 were issued, accumulated cash dividends (including interim dividends) paid by the Company for the fiscal years beginning after March 31, 1989 may not exceed accumulated net income in the audited consolidated statements of income for the fiscal years beginning after March 31, 1989 plus ¥65,000 million as long as these debentures are outstanding. In determining the accumulated cash dividends, interim cash dividends to be paid on and after April 1, 1990 are considered to be a part of the cash dividends of the previous fiscal year.

(8) Retirement and Severance Benefits

The Company and its domestic subsidiaries have a number of contributory and noncontributory pension plans to provide retirement and severance benefits to substantially all employees.

Prior to April 1, 2000, the Company did not apply the accounting for single-employer defined benefit pension plans under SFAS No. 87 for these plans as the effects on the consolidated financial statements for the implementation of SFAS No. 87 were not significant.

Principal pension plans are unfunded defined benefit pension plans. Under the plans, employees are entitled to lump-sum payments based on the current rate of pay and the length of service upon retirement or termination of employment for reasons other than dismissal for cause. Prior to April 1, 2000, the projected benefit obligation which was made equal to the larger vested benefit obligation was recognized as the retirement and severance benefits in the Company's balance sheet. The pension cost for the year was computed as the retirement and severance benefits paid plus or minus the change in the vested benefit obligation. For the years ended March 31, 2000 and 1999, the net periodic pension cost consisted of service costs of ¥97,386 million and ¥147,234 million, respectively.

Directors and certain employees are not covered by the programs described above. Benefits paid to such persons and meritorious service awards paid to employees in excess of the prescribed formula are charged to income as paid as it is not practicable to compute the liability for future payments since amounts vary with circumstance.

In addition to unfunded defined benefit pension plans, the Company and certain of its subsidiaries contribute to each Employees Pension Fund (EPF) as is stipulated by the Japanese Welfare Pension Insurance Law and other pension plans. The pension plans under the EPF are composed of the substitutional portion of Japanese Welfare Pension Insurance and the corporate portion which is the contributory defined benefit pension plan covering substantially all of their employees and provides benefits in addition to the substitutional portion. The Company, certain of its subsidiaries and their employees contribute the pension premiums for the substitutional portion and the corporate portion to each EPF. The plan assets of each EPF cannot be specifically allocated to the individual participants nor to the substitutional and corporate portions.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The benefits for the substitutional portion are based on standard remuneration scheduled by the Welfare Pension Insurance Law and the length of participation. The benefits of the corporate portion are based on the current rate of pay and the length of service. Under EPF pension plans, the participants are eligible for these benefits after a one-month period of participation in the plan. EPF contributions and cost for the substitutional portion were determined in accordance with the open aggregate cost method (actuarial funding method) as stipulated by the Welfare Pension Insurance Law. Contributions and cost for the corporate portion were determined in accordance with the entry age normal cost method (actuarial funding method). The pension cost of the corporate portion for the years ended March 31, 2000 and 1999 totaled ¥63,401 million and ¥66,021 million, respectively.

Funding status of the Company's plan as of March 31, 2000 and 1999 was as follows:

	Yen (millions)	
	2000	1999
The liability reserve calculated using:		
Aggregate cost method - discount rate at 5.5% and assumed rates of compensation increase at 0.6 - 2.3%	¥ (379,678)	(397,959)
Entry age normal cost method - discount rate at 4.5% and assumed rate of compensation increase at 3.8%	(577,764)	(541,297)
Fair value of plan assets, primarily fixed income securities and contract receivables from insurance companies	1,156,735	943,271
	¥ <u>199,293</u>	<u>4,015</u>

The fair value of plan assets and liability reserve of certain domestic subsidiaries' plans as of March 31, 2000 and 1999 were as follows:

	Yen (millions)	
	2000	1999
Liability reserve	¥ (547,784)	(517,861)
Fair value of plan assets	<u>588,420</u>	<u>512,753</u>
	¥ <u>40,636</u>	<u>(5,108)</u>

Provision for retirement and severance benefits and pension expense for the years ended March 31, 2000 and 1999 totaled to ¥203,893 million and ¥246,750 million, respectively.

Effective April 1, 2000, the Company adopted SFAS No. 87, "Employers' Accounting for Pensions" and SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits" for the funded benefit pension plans and the unfunded lump-sum payment plans, as the effect of the current discount rate of actuarial assumptions on the pension funded status is expected to have a material effect in subsequent years. However, the effect of this change on consolidated financial statements for the year ended March 31, 2001 was not significant. Prior year consolidated financial statements have not been restated as the effects of the implementation of SFAS No. 87 and SFAS No. 132 are immaterial.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

Net periodic benefit cost for the funded benefit pension plans and the unfunded lump-sum payment plans for the year ended March 31, 2001 consists of the following components:

	<u>Yen (millions)</u> <u>2001</u>
Service cost	¥ 117,104
Interest cost	115,163
Expected return on plan assets for the period	(86,879)
Amortization of transition asset	(421)
Amortization of prior service cost	218
Recognized actuarial loss	25,869
Employees' contributions	<u>(18,111)</u>
Net periodic benefit cost	¥ <u>152,943</u>

Unrecognized transition asset, unrecognized prior service benefit and cost and unrecognized actuarial gain and loss are amortized using the straight-line method over the average remaining service period of active employees.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

Reconciliation of beginning and ending balances of the benefit obligation of the funded defined benefit pension plans and the unfunded defined benefit pension plans and the fair value of the plan assets, and actuarial assumptions used at March 31, 2001 are as follows:

	<u>Yen (millions)</u>
	<u>2001</u>
Change in benefit obligation:	
Benefit obligation at beginning of year	¥ 2,869,822
Service cost	117,104
Interest cost	115,163
Plan amendments	(24,636)
Actuarial loss	114,338
Benefits paid	(146,916)
Acquisitions and divestitures	(32,525)
Foreign currency exchange rate changes	<u>4,170</u>
Benefit obligation at end of year	<u><u>3,016,520</u></u>
Change in plan assets:	
Fair value of plan assets at beginning of year	2,045,352
Actual return on plan assets	(277,056)
Employers' contributions	151,334
Employees' contributions	18,111
Benefits paid	(83,473)
Acquisitions and divestitures	(21,940)
Foreign currency exchange rate changes	<u>3,205</u>
Fair value of plan assets at end of year	<u><u>1,835,533</u></u>
Funded status	(1,180,987)
Unrecognized transition asset	(1,673)
Unrecognized prior service benefit	(53,166)
Unrecognized actuarial loss	<u>612,936</u>
Net amount recognized in the consolidated balance sheet	¥ <u><u>(622,890)</u></u>
Amounts recognized in the consolidated balance sheet consist of:	
Prepaid benefit cost	¥ 906
Accrued benefit cost	(982,332)
Intangible asset	437
Accumulated other comprehensive loss	<u>358,099</u>
Net amount recognized	¥ <u><u>(622,890)</u></u>
Actuarial assumptions on a weighted-average basis:	
Discount rate	3.9%
Expected rate of return on plan assets	4.3%
Rate of compensation increase	3.1%

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The components of the net periodic benefit cost are determined using the assumptions as of the beginning of the fiscal year, and the components of benefit obligation are determined using the assumptions as of the end of the fiscal year. Discount rate, expected rate of return on plan assets and rate of compensation increase on a weighted-average basis as of March 31, 2000 was 4.1%, 4.3% and 3.1%, respectively.

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for the pension plan with accumulated benefit obligations in excess of plan assets is ¥2,658,330 million, ¥2,481,424 million and ¥1,651,888 million, respectively, as of March 31, 2001.

(9) Other Liabilities

Other liabilities as of March 31, 2001 and 2000 consist of the following:

	Yen (millions)	
	2001	2000
Deferred tax liabilities	¥ 13,624	13,050
Long-term payables for property	49,896	66,435
Other	10,169	2,233
	¥ 73,689	81,718

(10) Common Stock

The Company has authorized for issuance 10 billion shares of common stock with a ¥50 par value. Issued and outstanding shares, changes in shares and the amount of common stock for the years ended March 31, 2001, 2000 and 1999 are summarized as follows:

		Yen (millions)
	<u>Issued and outstanding shares</u>	<u>Amount</u>
Balance as of March 31, 1998	3,337,894,780	¥ 281,735
Issued upon conversion of convertible debentures	-	-
Balance as of March 31, 1999	3,337,894,780	281,735
Issued upon conversion of convertible debentures	5,471	3
Balance as of March 31, 2000	3,337,900,251	281,738
Issued upon conversion of convertible debentures	31,606	16
Balance as of March 31, 2001	3,337,931,857	¥ 281,754

Conversions of convertible debt issued subsequent to October 1, 1982 into common stock were accounted for in accordance with the provisions of the Japanese Commercial Code by crediting one-half of the conversion price to each of the common stock account and the capital surplus account.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(11) Legal Reserve and Cash Dividends

The Japanese Commercial Code provides that earnings in an amount equal to at least 10% of appropriations of retained earnings to be paid in cash be appropriated as a legal reserve until such reserve equals 25% of stated common stock. This legal reserve is not available for dividends but may be used to reduce a deficit or may be transferred to stated common stock.

Cash dividends and appropriations to the legal reserve charged to retained earnings during the years ended March 31, 2001, 2000 and 1999 represent dividends paid out during those years and the related appropriations to the legal reserve. The accompanying financial statements do not include any provision for the semi-annual dividend of ¥5.5 per share totaling ¥18,358 million subsequently proposed by the Board of Directors in respect of the year ended March 31, 2001.

(12) Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss), net of related tax effects, displayed in the consolidated statements of stockholders' equity is classified as follows:

	<u>Yen (millions)</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
Foreign currency translation adjustments:			
Balance at beginning of year	¥ (77,577)	(58,065)	(43,860)
Other comprehensive income (loss), net of reclassification adjustments	20,804	(19,090)	(14,603)
Transfers from (to) minority interests arising from conversion of subsidiaries' convertible debentures	(3)	3	1
Transfers from (to) minority interests arising from sale of subsidiaries' common stock and other	<u>(871)</u>	<u>(425)</u>	<u>397</u>
Balance at end of year	¥ <u><u>(57,647)</u></u>	<u><u>(77,577)</u></u>	<u><u>(58,065)</u></u>
Minimum pension liability adjustments:			
Balance at beginning of year	¥ -	-	-
Other comprehensive loss	<u>(182,936)</u>	-	-
Balance at end of year	¥ <u><u>(182,936)</u></u>	<u><u>-</u></u>	<u><u>-</u></u>
Net unrealized holding gain on available-for-sale securities:			
Balance at beginning of year as previously reported	¥ -	-	-
Restatement (note 1(e))	95,019	81,266	94,957
Balance at beginning of year as restated	95,019	81,266	94,957
Other comprehensive income (loss), net of reclassification adjustments	(43,991)	13,747	(13,670)
Transfers to minority interests arising from conversion of subsidiaries' convertible debentures	(6)	(7)	-
Transfers from (to) minority interests arising from sale of subsidiaries' common stock and other	<u>19</u>	<u>13</u>	<u>(21)</u>
Balance at end of year	¥ <u><u>51,041</u></u>	<u><u>95,019</u></u>	<u><u>81,266</u></u>

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

	<u>Yen (millions)</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
Cash flow hedges:			
Balance at beginning of year	¥ -	-	-
Other comprehensive income, net of reclassification adjustments	1,012	-	-
Transfers to minority interests arising from conversion of subsidiaries' convertible debentures	-	-	-
Transfers from minority interests arising from sale of subsidiaries' common stock and other	<u>84</u>	<u>-</u>	<u>-</u>
Balance at end of year	¥ <u>1,096</u>	<u>-</u>	<u>-</u>
Total accumulated other comprehensive income (loss):			
Balance at beginning of year as previously reported	¥ (77,577)	(58,065)	(43,860)
Restatement (note 1(e))	95,019	81,266	94,957
Balance at beginning of year as restated	17,442	23,201	51,097
Other comprehensive loss, net of reclassification adjustments	(205,111)	(5,343)	(28,273)
Transfers from (to) minority interests arising from conversion of subsidiaries' convertible debentures	(9)	(4)	1
Transfers from (to) minority interests arising from sale of subsidiaries' common stock and other	<u>(768)</u>	<u>(412)</u>	<u>376</u>
Balance at end of year	¥ <u>(188,446)</u>	<u>17,442</u>	<u>23,201</u>

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The following is a summary of reclassification adjustments by each classification of other comprehensive income (loss) arising during the years ended March 31, 2001, 2000 and 1999 and the amounts of income tax expense or benefit allocated to each component of other comprehensive income (loss), including reclassification adjustments.

	Yen (millions)		
	2001		
	Before-tax amount	Tax benefit (expense)	Net-of-tax amount
Other comprehensive income (loss) arising during the year:			
Foreign currency translation adjustments	¥ 18,990	-	18,990
Minimum pension liability adjustments	(314,158)	131,222	(182,936)
Net unrealized holding gain on available-for-sale securities	(55,311)	22,759	(32,552)
Cash flow hedges	<u>2,742</u>	<u>(804)</u>	<u>1,938</u>
	(347,737)	153,177	(194,560)
Reclassification adjustments for net loss (gain) included in net income:			
Foreign currency translation adjustments	1,814	-	1,814
Net unrealized holding gain on available-for-sale securities	(19,652)	8,213	(11,439)
Cash flow hedges	<u>(1,670)</u>	<u>744</u>	<u>(926)</u>
	(19,508)	8,957	(10,551)
Other comprehensive income (loss), net of reclassification adjustments:			
Foreign currency translation adjustments	20,804	-	20,804
Minimum pension liability adjustments	(314,158)	131,222	(182,936)
Net unrealized holding gain on available-for-sale securities	(74,963)	30,972	(43,991)
Cash flow hedges	<u>1,072</u>	<u>(60)</u>	<u>1,012</u>
	¥ <u>(367,245)</u>	<u>162,134</u>	<u>(205,111)</u>

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

		Yen (millions)		
		2000		
		Before-tax amount	Tax benefit (expense)	Net-of-tax amount
Other comprehensive income (loss) arising during the year:				
Foreign currency translation adjustments	¥	(19,183)	-	(19,183)
Net unrealized holding gain on available-for-sale securities		29,539	(12,422)	17,117
		10,356	(12,422)	(2,066)
Reclassification adjustments for net loss (gain) included in net income:				
Foreign currency translation adjustments		93	-	93
Net unrealized holding gain on available-for-sale securities		(5,823)	2,453	(3,370)
		(5,730)	2,453	(3,277)
Other comprehensive income (loss), net of reclassification adjustments:				
Foreign currency translation adjustments		(19,090)	-	(19,090)
Net unrealized holding gain on available-for-sale securities		23,716	(9,969)	13,747
	¥	4,626	(9,969)	(5,343)
		Yen (millions)		
		1999		
		Before-tax amount	Tax benefit (expense)	Net-of-tax amount
Other comprehensive income (loss) arising during the year:				
Foreign currency translation adjustments	¥	(18,364)	-	(18,364)
Net unrealized holding gain on available-for-sale securities		(27,582)	13,390	(14,192)
		(45,946)	13,390	(32,556)
Reclassification adjustments for net loss included in net loss:				
Foreign currency translation adjustments		3,761	-	3,761
Net unrealized holding gain on available-for-sale securities		1,002	(480)	522
		4,763	(480)	4,283
Other comprehensive income (loss), net of reclassification adjustments:				
Foreign currency translation adjustments		(14,603)	-	(14,603)
Net unrealized holding gain on available-for-sale securities		(26,580)	12,910	(13,670)
	¥	(41,183)	12,910	(28,273)

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(13) Commitments and Contingencies

As of March 31, 2001, outstanding commitments for the purchase of property, plant and equipment were approximately ¥53,497 million.

The Company and its operating subsidiaries are contingently liable for loan guarantees in the amount of approximately ¥41,572 million as of March 31, 2001. In addition, Hitachi Capital Corporation, a financing subsidiary, is the guarantor of consumer loans totaling ¥673,196 million as of March 31, 2001.

It is common practice in Japan for companies, in the ordinary course of business, to receive promissory notes in the settlement of trade accounts receivable and to subsequently discount such notes to banks or to transfer them by endorsement to suppliers in the settlement of accounts payable. As of March 31, 2001 and 2000, the companies are contingently liable for trade notes discounted and endorsed in the following amounts:

	Yen (millions)	
	2001	2000
Notes discounted	¥ 6,464	5,170
Notes endorsed	<u>55,457</u>	<u>51,310</u>
	¥ <u>61,921</u>	<u>56,480</u>

The Company and certain subsidiaries are subject to several legal proceedings and claims which have arisen in the ordinary course of business and have not been finally adjudicated. These actions when ultimately concluded and determined will not, in the opinion of management, have a material adverse effect on the financial position and results of operations of the Company and certain subsidiaries.

(14) Other Income and Other Deductions

For the year ended March 31, 2001, the Company recorded a restructuring charge of ¥8,814 million as other deductions, primarily associated with reorganization and streamlining domestic and overseas business in Consumer Products and Power & Industrial Systems divisions. Included in this total are special termination benefits of ¥5,275 million. The special termination benefits accrual of ¥2,371 million as of March 31, 2001, which is related to the voluntary termination of approximately 340 employees, is expected to be paid by March 31, 2002.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

For the year ended March 31, 2000, the Company recorded a restructuring charge of ¥65,977 million as other deductions primarily associated with Information Systems & Electronics division and Materials division, including the integration, reorganization and streamlining of domestic and overseas subsidiaries. Included in this total are special termination benefits of ¥23,344 million, losses of ¥17,702 million on the sale or disposal of assets, impairment losses on machinery and equipment of ¥9,310 million and various other restructuring related charges of ¥15,621 million. The special termination benefits accrual of ¥18,545 million as of March 31, 2000, which was related to the voluntary termination of approximately 6,100 employees, was paid by March 31, 2001. The competitive market of hard disk drives caused its significant price decline during the year ended March 31, 2000. Under such situation, the Company recognized an impairment loss on the machinery and equipment mainly for the magnetic heads manufacturing, which are the main parts of hard disk drives, based on the comparison of the future net cash flows expected to be generated by the machinery and equipment and their carrying amounts. The present value of estimated future cash flows using a discount rate inherent to the Company was used as the fair value of those assets. Losses on the sale or disposal of assets amounted to ¥12,979 million in Information Systems & Electronics division and ¥3,895 million in Materials division.

For the year ended March 31, 1999, the Company recorded a restructuring charge of ¥132,505 million as other deductions primarily associated with the integration, reorganization and streamlining of the operations, especially in the Information Systems & Electronics division, the Consumer Products division and the Power & Industrial Systems division. Included in this total are special termination benefits of ¥71,706 million, losses of ¥42,103 million on the sale or disposal of assets, principally property, plant and equipment and various other restructuring related charges of ¥18,696 million. The special termination benefits related to the voluntary termination of approximately 9,700 employees from the above divisions. Approximately 5,200 employees had separated or been reallocated as of March 31, 1999, and the employee reduction or reallocation plan was substantially completed in the year ended March 31, 2000. Accordingly, special termination benefits and severance pay of ¥48,126 million was paid during the year ended March 31, 1999 and ¥54,301 million, the remainder of the special termination benefits accrual for the year ended March 31, 1999, was paid in the year ended March 31, 2000.

“Other income” for the years ended March 31, 2001, 2000 and 1999 includes the net gain on securities in the amount of ¥9,334 million, ¥30,059 million and ¥1,144 million, respectively. In addition, ¥15,651 million of gross realized gains on contributions of available-for-sale securities to pension fund trusts is included in “Other income” for the year ended March 31, 2001. Equity in earnings of affiliated companies included in “Other income” for the year ended March 31, 2001 and “Other deductions” for the years ended March 31, 2000 and 1999 is a gain of ¥2,559 million and a loss of ¥6,426 million and ¥6,935 million, respectively.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(15) Net Income (Loss) Per Share Information

The reconciliation of the numbers and the amounts used in the basic and diluted net income (loss) per share computations is as follows:

	Number of shares		
	2001	2000	1999
Weighted average number of shares on which basic net income (loss) per share is calculated	3,337,926,578	3,337,895,280	3,337,894,780
Effect of dilutive securities:			
5th series convertible debentures	28,442,656	28,473,510	-
6th series convertible debentures	49,502,986	-	-
7th series convertible debentures	128,944,696	-	-
Number of shares on which diluted net income (loss) per share is calculated	<u>3,544,816,916</u>	<u>3,366,368,790</u>	<u>3,337,894,780</u>
	Yen (millions)		
	2001	2000	1999
Net income (loss) applicable to common Stockholders	¥ 104,380	16,922	(327,611)
Effect of dilutive securities:			
5th series convertible debentures	325	325	-
6th series convertible debentures	831	-	-
7th series convertible debentures	2,065	-	-
Other	(119)	(463)	-
Net income (loss) on which diluted net income (loss) per share is calculated	¥ <u>107,482</u>	<u>16,784</u>	<u>(327,611)</u>
	Yen		
	2001	2000	1999
Net income (loss) per share:			
Basic	¥ 31.27	5.07	(98.15)
Diluted	30.32	4.99	(98.15)

The net income per share computation for the year ended March 31, 2000 excludes 6th and 7th series convertible debentures because their effect would have been antidilutive. The net loss per share computation for the year ended March 31, 1999 excludes all series convertible debentures because their effect would have been antidilutive.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(16) Supplementary Income Information

	Yen (millions)		
	2001	2000	1999
Taxes other than income taxes consist of the following:			
Property	¥ 43,825	36,251	36,286
Welfare	198,447	209,377	216,952
Other	<u>15,828</u>	<u>16,816</u>	<u>14,629</u>
	¥ <u>258,100</u>	<u>262,444</u>	<u>267,867</u>
Maintenance and repairs	¥ 106,542	100,903	97,469
Research and development expense	435,579	432,342	496,728
Provision for retirement and severance benefits and pension expense	152,943	203,893	246,750
Advertising expense	50,940	44,648	44,695
Rent	148,463	202,420	192,144
Exchange loss	11,307	34,292	22,463

(17) Supplementary Cash Flows Information

	Yen (millions)		
	2001	2000	1999
Cash paid during the year for:			
Interest	¥ 50,073	52,046	61,935
Income taxes	126,019	98,797	145,771

Convertible debentures issued by the Company of ¥32 million in 2001 and ¥6 million in 2000 were converted into common stock. Convertible debentures issued by subsidiaries of ¥2,305 million in 2001, ¥13,462 million in 2000 and ¥5,915 million in 1999 were converted into subsidiaries' common stock. Capital lease assets of ¥4,672 million were capitalized in 2001.

During the year ended March 31, 2001, the Company made an acquisition and integrated some of its subsidiaries and affiliates through exchange offer procedure as shown in note 22.

The proceeds from sale of securities classified as available-for-sale discussed in note 2 are included in both "(Increase) decrease in short-term investments" and "Proceeds from sale of investments and subsidiaries' common stock" on the consolidated statements of cash flows.

(18) Financial Instruments, Derivative Financial Instruments and Risk Management (prior to SFAS No. 133)

The Company and its subsidiaries operate globally, are exposed to market risk from changes in foreign currency exchange rates and interest rates and enter into financial instruments and derivative financial instruments for the purpose of reducing such risk. The Company and its subsidiaries do not hold or issue derivative financial instruments for the purpose of trading.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The Company and its subsidiaries are exposed to credit-related losses in the event of non-performance by counterparties to financial instruments and derivative financial instruments, but it is not expected that any counterparties will fail to meet their obligations, because most of the counterparties are authentic financial institutions.

The contract or notional amounts of derivative financial instruments held as of March 31, 2000 are summarized as follows:

	<u>Yen (millions)</u>	
	<u>2000</u>	
Forward exchange contracts:		
To sell foreign currencies	¥	188,200
To buy foreign currencies		22,070
Cross currency swap agreements:		
To sell foreign currencies		50,270
To buy foreign currencies		225,058

As discussed in note 13, as of March 31, 2000, the Company and its subsidiaries were liable for trade notes discounted and endorsed, which were ¥5,170 million and ¥51,310 million, respectively, and for loan guarantees in the amount of approximately ¥37,592 million. In addition, Hitachi Capital Corporation (former Hitachi Credit Corporation), a financing subsidiary, was the guarantor of consumer loans totaling ¥637,626 million as of March 31, 2000. In relation to these, credit-related losses in the event of non-performance were not expected to be material. The Company and its subsidiaries sometimes required collateral of the counterparties for the purpose of reducing credit risk in appropriate cases.

(19) Derivative Instruments and Hedging Activities

Overall risk profile

The Company and its subsidiaries operate globally and are exposed to market risks from changes in foreign currency exchange rates and interest rates. In order to reduce these market risks, the Company and its subsidiaries utilize certain derivative financial instruments.

The major manufacturing bases of the Company are located in Japan and Asia. The Company and its subsidiaries generate approximate 30% of their sales from overseas. These sales are mainly denominated in U.S. dollar or Euro. In order to mitigate the foreign currency exchange exposure, the Company and its subsidiaries purchase forward exchange contracts.

The financing subsidiaries in London, New York and Singapore issue U.S. dollar denominated, variable rate, medium-term notes mainly through the Euro markets to finance its overseas long-term operating capital. The Company and its subsidiaries utilize cross currency swap agreements and interest rate swaps in order to hedge the foreign currency and interest rate volatility risks.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The Company and its subsidiaries are also exposed to credit-related losses in the event of non-performance by counterparties to derivative financial instruments, but it is not expected that any counterparties will fail to meet their obligations, because most of the counterparties are internationally recognized financial institutions and contracts are diversified into a number of major financial institutions.

Foreign currency exchange rate risk management

The Company and its subsidiaries have assets and liabilities which are exposed to foreign currency exchange rate risk and, as a result, they enter into forward exchange contracts and cross currency swap agreements for the purpose of hedging these risk exposures.

The Company and its subsidiaries principally use forward exchange contracts to manage certain foreign currency exchange exposures principally from the exchange of U.S. dollar and Euro into Japanese yen. These contracts are primarily used to fix the future net cash flows principally from trade receivables and payables recognized, and forecasted transactions, which are denominated in foreign currencies. The Company and its subsidiaries measure the volume and due date of future net cash flows by currencies every month. In accordance with their policy, a certain portion of measured net cash flows is covered using forward exchange contracts, which principally mature within one year.

The Company and its subsidiaries enter into cross currency swap agreements with the same maturities as underlying debts to fix cash flows from long-term debts denominated in foreign currencies. The hedging relationship between the derivative financial instrument and its hedged item is highly effective in achieving offsetting changes in foreign exchange rates.

Interest rate risk management

The Company's and its subsidiaries' exposure to interest rate risk is related principally to debt obligations. These debt obligations expose the Company and its subsidiaries to variability in the future cash outflow of interest payments due to changes in interest rates. Management believes it is prudent to minimize the variability caused by interest rate risk.

To meet this objective, the Company and its subsidiaries principally enter into interest rate swaps to manage fluctuations in cash flows resulting from interest rate risk. The interest rate swaps principally change the variable-rate cash flows on debt obligations to fixed-rate cash flows principally associated with medium-term notes by entering into receive-variable, pay-fixed interest rate swaps. Under the interest rate swaps, the Company and its subsidiaries receive variable interest rate payments and make fixed interest rate payments, thereby creating fixed-rate long-term debt. The hedging relationship between the interest rate swaps and its hedged item is highly effective in achieving offsetting changes in cash flows resulting from interest rate risk.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

Risk management policy

The Company and its subsidiaries assess foreign currency exchange rate risk and interest rate risk by continually monitoring changes in these exposures and by evaluating hedging opportunities. It is the Company's policy that the Company and its subsidiaries do not enter into derivative financial instruments for any purpose other than hedging purposes.

Fair value hedge

Changes in fair value of both recognized assets and liabilities, and derivative instruments designated as fair value hedges of these assets and liabilities are recognized in other income (deductions). Derivative financial instruments designated as fair value hedges include forward exchange contracts associated with operating transactions and cross currency swap agreements associated with financing transactions.

The sum of the amount of the hedging ineffectiveness and net gain or loss excluded from the assessment of hedge effectiveness is not material for the year ended March 31, 2001.

Cash flow hedge

Foreign Currency Exposure

Changes in fair value of forward exchange contracts designated and qualifying as cash flow hedges of forecasted transactions and recognized assets and liabilities are reported in accumulated other comprehensive income (AOCI). These amounts are reclassified into earnings in the same period as the hedged items affect earnings.

The sum of the amount of the hedging ineffectiveness and net gain or loss excluded from the assessment of hedge effectiveness is not material for the year ended March 31, 2001.

It is expected that approximately ¥429 million of AOCI relating to existing forward exchange contracts will be reclassified into other deductions during the year ended March 31, 2002.

As of March 31, 2001, the maximum length of time over which the Company and its subsidiaries are hedging their exposure to the variability in future cash flows associated with foreign currency forecasted transactions is approximately 38 months.

Interest Rate Exposure

Changes in fair values of interest rate swaps designated as hedging instruments for the variability of cash flows associated with long-term debt obligations are reported in AOCI. These amounts subsequently are reclassified into interest expense as a yield adjustment in the same period in which the hedged debt obligations affect earnings.

Interest expense for the year ended March 31, 2001, includes losses of ¥1,357 million which represents the component excluded from the assessment of hedge effectiveness.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

During the year ended March 31, 2002, approximately ¥676 million of AOCI related to the interest rate swaps are expected to be reclassified as an offset to interest expense as a yield adjustment of the hedged debt obligations.

The contract or notional amounts of derivative financial instruments held as of March 31, 2001 are summarized as follows:

	<u>Yen (millions)</u>
	<u>2001</u>
Forward exchange contracts:	
To sell foreign currencies	¥ 206,660
To buy foreign currencies	18,225
Cross currency swap agreements:	
To sell foreign currencies	99,830
To buy foreign currencies	209,573
Interest rate swaps	775,144

(20) Concentrations of Credit Risk

The Company and its subsidiaries generally do not have significant concentrations of credit risk to any counterparties nor any regions, because those are diversified and spread globally.

(21) Fair Value of Financial Instruments

The following methods and assumptions are used to estimate the fair values of financial instruments:

Investment in securities

The fair value of investment securities is estimated based on quoted market prices for these or similar securities.

Long-term debt

The fair value of long-term debt is estimated based on quoted market prices or the present value of future cash flows using the companies' incremental borrowing rates for similar borrowing arrangements.

Cash and cash equivalents, Trade receivables, Short-term debt and Trade payables

The carrying amount approximates the fair value because of the short maturity of these instruments.

Derivative financial instruments

The fair values of forward exchange contracts, cross currency swap agreements and interest rate swaps are estimated on the basis of the market prices of derivative financial instruments with similar contract conditions.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The carrying amounts and estimated fair values of the financial instruments as of March 31, 2001 and 2000 are as follows:

	Yen (millions)			
	2001		2000	
	<u>Carrying amounts</u>	<u>Estimated fair values</u>	<u>Carrying amounts</u>	<u>Estimated fair values</u>
Investment in securities:				
Short-term investments	¥ 433,650	433,575	632,434	632,434
Investments and advances	554,564	554,560	466,077	466,077
Derivatives (Assets):				
Forward exchange contracts	295	295	4,003	4,172
Cross currency swap agreements	3,298	3,298	19,223	42,217
Interest rate swaps	7,690	7,690	-	-
Long-term debt	(2,293,916)	(2,398,899)	(1,741,909)	(1,843,702)
Derivatives (Liabilities):				
Forward exchange contracts	(13,512)	(13,512)	(254)	(121)
Cross currency swap agreements	(6,860)	(6,860)	(12,579)	(22,264)
Interest rate swaps	(2,516)	(2,516)	-	-

Short-term investments as of March 31, 2000 include investment in trust accounts totaling ¥256,526 million, which approximate fair value.

It is not practicable to estimate the fair value of investments in unlisted common stock because of the lack of a market price and difficulty in estimating fair value without incurring excessive cost. The carrying amounts of these investments at March 31, 2001 and 2000 totaled ¥57,795 million and ¥60,882 million, respectively.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(22) Merger and Acquisition

On October 1, 2000, Hitachi Credit Corporation acquired all common stock of Hitachi Leasing, Ltd. in exchange for 13,386,240 shares of Hitachi Credit Corporation's common stock. Prior to this transaction, the ownership of Hitachi Credit Corporation, a core financial service business, and Hitachi Leasing, Ltd., a leasing and other corporate financing service business, were 53.4% and 50.0%, respectively. Consequently, the surviving entity changed its name to Hitachi Capital Corporation and became the Company's 53.0% owned subsidiary. The merger was accounted for using the purchase method and the Company consolidated Hitachi Leasing, Ltd. and its subsidiaries as if it had been merged effective April 1, 2000. The excess of purchase price over net assets acquired of the 50% interest in Hitachi Leasing, Ltd. not previously owned by the Company was not material. The effects of the purchase to the balance sheet as of April 1, 2000 are as follows:

	<u>Yen (millions)</u>
Cash and cash equivalent	¥ 49,768
Investment in leases	736,505
Other assets	73,018
Short-term and long-term debt	(743,985)
Other liabilities	(90,532)

On a pro forma basis, revenue, net income and earnings per share of the Company, with the assumed acquisition of April 1, 1999, would not differ materially from the amount reported in the accompanying consolidated financial statements as of and for the year ended March 31, 2000.

On October 1, 2000, Kokusai Electric Co., Ltd. merged into Yagi Antenna Co., Ltd. and Hitachi Denshi, Ltd. and changed its name to Hitachi Kokusai Electric Inc. Prior to the merger, Kokusai Electric Co., Ltd. and Yagi Antenna Co., Ltd., manufacturers and distributors of wireless telecommunication equipment, were 26.7% and 40.9% owned affiliates of the Company. Hitachi Denshi Co., Ltd., a manufacturer and distributor of broadcasting and telecommunication equipment, was a 63.7% owned subsidiary of the Company. Kokusai Electric Co., Ltd. issued common stock in exchange for common stock of Yagi Antenna Co., Ltd. and Hitachi Denshi, Ltd. As a result, Hitachi Kokusai Electric Inc. became a 37.4% owned affiliate of the Company and is accounted for using the equity method. Total assets and net assets of Hitachi Denshi, Ltd. and its subsidiaries as of September 30, 2000 amounted to approximately ¥56,959 million and ¥23,237 million, respectively.

On October 31, 2000, Experio Solutions Corporation (Experio), a wholly owned subsidiary of the Company, acquired the e-business consulting department of Grant Thornton LLP for ¥15,674 million in cash. In addition, Experio issued its common stock valued at ¥1,601 million to the department partners in lieu of a cash payment, and accordingly became a 91.4% owned subsidiary of the Company. The acquisition was recorded under the purchase method and the results of operations of the acquired e-business consulting have been included in the consolidated financial statements since the date of acquisition. This transaction resulted in an excess of purchase price over net assets acquired of ¥15,895 million, which is being amortized on the straight-line method over 10 years.

HITACHI, LTD.  
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

The allocation of acquisition costs to the assets and liabilities acquired is as follows:

	<u>Yen (millions)</u>
Assets acquired	¥ 2,009
Goodwill	15,895
Liabilities assumed	(263)
Common stock issued to department partners	(1,601)
Direct acquisition costs	(366)
Cash paid to Grant Thornton	(15,674)

On a pro forma basis, revenue, net income and earnings per share of the Company with the assumed acquisition of April 1, 2000 and 1999 would not differ materially from the amount reported in the accompanying consolidated financial statements as of and for the years ended March 31, 2001 and 2000.

(23) Stock Option Plans

The Company granted stock options to non-employee directors and certain employees during the year ended March 31, 2001. Under these stock option plans, options to purchase common stock were granted at prices not less than market value at date of grant, are exercisable from one year after the date of grant and expire 5 years after the date of grant. Under APB 25, the Company recognized no compensation expense related to employee stock options, as no options was granted at a price below the market price on the day of grant.

A summary of stock option plans activity for the year shown is as follows:

	<u>Stock options</u> <u>(shares)</u>	<u>Exercise price</u>
Outstanding at March 31, 2000	-	¥ -
Granted	527,000	1,451
Exercised	<u>-</u>	<u>-</u>
Outstanding at March 31, 2001	<u>527,000</u>	¥ <u>1,451</u>

The remaining contractual life is 4.3 years, and no exercisable stock options were outstanding as of March 31, 2001. The pro forma effect of applying SFAS No. 123 on net income and earnings per share for the year ended March 31, 2001 was not material.

In addition, in April 2001, the board of directors of the Company decided to propose the adoption of stock option plans for non-employee directors and certain employees to their shareholders' meeting to be held in June 2001. In accordance with the proposals, options to purchase the Company's common stock less than 1,090,000 shares were granted at prices not less than market value at date of grant, are exercisable from one year after the date of grant and expire 5 years after the date of grant.

HITACHI, LTD.  
AND SUBSIDIARIES

## Reserves

Years ended March 31, 2001, 2000 and 1999

(In millions of yen)

		Balance at beginning of period	Charged to income	Net decrease in unearned income	Bad debts written off	Balance at end of period
Year ended March 31, 2001:						
Allowance for doubtful receivables	¥	14,430	11,307	-	(4,709)	21,028
Unearned income- installment financing		<u>7,767</u>	<u>-</u>	<u>(6,536)</u>	<u>-</u>	<u>1,231</u>
	¥	<u>22,197</u>	<u>11,307</u>	<u>(6,536)</u>	<u>(4,709)</u>	<u>22,259</u>
Year ended March 31, 2000:						
Allowance for doubtful receivables	¥	17,233	(763)	-	(2,040)	14,430
Unearned income- installment financing		<u>8,710</u>	<u>-</u>	<u>(943)</u>	<u>-</u>	<u>7,767</u>
	¥	<u>25,943</u>	<u>(763)</u>	<u>(943)</u>	<u>(2,040)</u>	<u>22,197</u>
Year ended March 31, 1999:						
Allowance for doubtful receivables	¥	14,474	6,458	-	(3,699)	17,233
Unearned income- installment financing		<u>9,332</u>	<u>-</u>	<u>(622)</u>	<u>-</u>	<u>8,710</u>
	¥	<u>23,806</u>	<u>6,458</u>	<u>(622)</u>	<u>(3,699)</u>	<u>25,943</u>