

# Risk Factors

Among the risks stated in this annual report, the following are those risks deemed to have a potentially critical impact on investment decisions. In addition, information related to future events as described in the text are based on judgments made by the Yamaha Group at the end of the fiscal year under review.

## 1. Economic Conditions

The Yamaha Group operates its business activities globally and therefore is subject to the influence of economic conditions in Japan and other countries. Recessions in world markets and accompanying declines in demand may have an adverse effect on the Group's business results and the development of its business activities.

## 2. Price Competition

The Yamaha Group faces severe competition in each of its business segments. For example, in the musical instruments segment, the Group is a comprehensive manufacturer of musical instruments and sells high-quality, high-performance instruments covering a broad price spectrum. However, the Group has competitors in each musical instruments field and, especially in recent years, competition in the lower price segments has become more intense.

Also, in the AV/IT segment, products manufactured in China are gaining a stronger presence in the market, as are competitors, leading to heightened price competition. Depending on reforms in distribution and trends in new technology, this business may be exposed to even more intense price competition, which could have an adverse effect on the Group's current strong position in this area.

## 3. Development of New Technologies

The Yamaha Group is focusing management resources on "The Sound Company" business domain and endeavors to create an unassailably strong position as the world's leading full-line musical instrument manufacturer. Meanwhile, the Group also operates an AV/IT segment, focusing mainly on HiFi AV products, and an electronic devices segment, concentrating on the semiconductor business centered on sound generators.

Differentiating the Group's technologies in the fields of sound, music and networks is indispensable for the Group's further development and growth. If, in its technological development activities, the Group does not continue to forecast future market needs correctly and meet these needs accurately, the added value of its products in the musical instruments segment could decline, and it may have to deal with price competition. The Group could also face the additional problem of being unable to stimulate new demand for its products and, as a result, may find it difficult to continue its AV/IT and electronic devices businesses.

## 4. Business Investment

The Yamaha Group makes investments in its businesses to promote their expansion. In making such investment decisions the Group understands the potential risks and returns qualitatively and quantitatively and makes careful, considered judgments. Nonetheless, under certain circumstances, the Group may be unable to recover a portion or the full amount of its investments or may decide to withdraw from the business. In such cases, the value of assets invested in such businesses may have to be written down.

## 5. Business Alliances

The Yamaha Group forms alliances with other companies, makes investments in other companies, forms joint ventures, and conducts other similar activities and, in recent years, the partnerships with other companies have grown in importance. In some cases, the anticipated beneficial effects of such partnerships may not materialize because of conflicts of interest with the partners, changes in the business strategies of such partners, or other reasons.

## 6. Reliance on Customers in Selling Materials and Parts

The Yamaha Group's manufacturing and sale of its products—including semiconductors, lifestyle-related products such as system kitchens, automobile interior wood components, and materials and parts—are dependent on the performance of its customers. When the bonds of trust between such customers and Group companies are impaired by disagreement over delivery schedules, quality, or other issues, this could have an adverse impact on future orders. Moreover, Group companies may be requested by customers to pay compensation in the event of quality problems or other defects.

## 7. Expansion of Business Operations Into International Markets

The Yamaha Group has established manufacturing and marketing bases in various parts of the world and operates its businesses globally. Of the Group's 88 consolidated subsidiaries, 46 are foreign corporations, and of this total, 19 companies are manufacturers. Principal manufacturing bases are concentrated in China, Indonesia and Malaysia, and 48.9% of the Group's net sales are generated overseas.

There are a number of risks inherent in these overseas operations.

If such risks should materialize, the difficulties of having manufacturing facilities concentrated in certain regions could mean that the Group may not be able to continue providing products in a stable manner. Such risks include:

- (a) Political and economic turmoil, terrorism and war
- (b) The introduction of disadvantageous government policies, new regulations or changes in existing regulations
- (c) Unexpected changes in laws and regulations
- (d) Difficulty in recruiting personnel
- (e) Difficulty in procuring raw materials and parts as well as issues related to the level of technology
- (f) Logistics problems due to harbor strikes, etc.

## **8. Increases in Raw Material Prices, Adequacy of Raw Material Supplies and Rising Logistics Costs**

The Yamaha Group makes use of raw materials in manufacturing its products, including lumber, metals such as copper, and plastics for parts. Increases in the prices of these materials can cause increases in manufacturing costs. In addition, certain kinds of material are obtained from specified suppliers. Unfavorable supply conditions for such materials may have an adverse effect on the Group's manufacturing activities.

Moreover, if logistics costs rise as a result of an increase in crude oil prices, this may cause increases in manufacturing costs and the cost of sales.

## **9. Effects of Declining Birthrate**

In the Yamaha Group's core business of musical instruments, regular schools constitute an important sales channel in addition to the Group's music schools and English language schools, which are primarily attended by children. Going forward, declining birthrates, particularly in Japan, may lead to a decline in sales through these channels.

## **10. Recruitment and Training of Personnel**

The average age of the Yamaha Group's workforce is relatively high, with a significant number of workers in the upper age brackets and a great number of employees approaching the official retirement age. The Group therefore faces some important issues: transferring skills in manufacturing musical instruments and other products to the next generation; recruiting and training the next generation of employees; and dealing with changes in the Group's employment structure. If the Group is unable to respond sufficiently to changes in its employment structure, the future growth of its business activities may be impeded.

## **11. Protection and Use of Intellectual Property**

The Yamaha Group has rights to intellectual property—including patents related to its proprietary technology—as well as operating know-how. Some of this intellectual property cannot be fully protected, or can only be partially protected, due to the limitations of legal systems in certain regions. Therefore, there may be instances where the Group cannot effectively prevent third parties from misusing its intellectual property. As a result, some products of other companies may appear in the market that are similar to or are copies of those of Group companies, thus leading to impaired sales for the Group. In addition, there may be cases where third parties point out that the Group's products infringe on their own intellectual property rights. As a result, sales of Group products that use the intellectual property in question may be delayed or suspended.

There are also instances where the Group is licensed in the intellectual property of third parties to produce key components for its products. Any increases in royalties paid for such intellectual property will result in higher manufacturing costs and may have an effect on price-competitiveness. Moreover, when the Group is unable to obtain licenses for certain intellectual property, it may be unable to manufacture the related products.

## **12. Defects in Products and Services**

The Yamaha Group supervises the quality of its products in accordance with its corporate rules for quality assurance. However, there is no guarantee that all products will be free of defects. Moreover, the Group takes out insurance against product liability claims, but there is no guarantee that this insurance will be sufficient to cover payment of damages. If issues related to product liability arise, then it is likely that insurance rates will increase. In addition, if costs related to product recovery, exchange and repair, and design changes increase significantly, or the reputation of the Group in society should be damaged, a decline in sales may result. Such circumstances may have an adverse effect on the Group's performance and financial position.

Furthermore, the Group pays careful attention to safety and sanitation at the retail stores, music schools, recreation establishments and other facilities that it operates. In the unlikely event that an accident should occur, the Group anticipates that temporary cessation of operations at the store, music school, or facility in question could be required, and the reputation of the Group in society could be damaged, resulting in a decline in sales.

## **13. Legal Regulations**

All the Yamaha Group's business operations around the world are subject to the laws and regulations of the countries where they are located. Examples of such regulations include laws that cover overseas investment, restrictions on exports and imports that may have an effect on national security, commercial activity, anti-trust issues, consumer protection regulations, tax systems and environmental protection. In addition, the Group must handle personal information about its customers safely and confidentially. The Yamaha Group takes special care to ensure that its activities are in compliance with legal regulations, but in the event that it unexpectedly fails to comply with certain laws, the Group's activities may be restricted and costs may increase as a result.

## 14. Environmental Regulations

There is a trend toward more stringent environmental regulations governing business activities, and corporations are being requested to fulfill their corporate social responsibilities by implementing voluntary environmental programs. The Yamaha Group works to implement policies that exceed the requirements of environmental regulations as regards products, packaging materials, energy conservation and the processing of industrial waste. However, there is no guarantee that the Group can completely prevent or reduce the occurrence of accidents in which restricted substances are released into the environment at levels exceeding established regulations.

Moreover, in cases where soil pollution has occurred on the land formerly occupied by industrial plants, it may be necessary to spend substantial amounts of money for soil remediation when the land is sold in the future, or it may be impossible to sell the land. There is also a possibility that the soil on land that has already been sold to third parties may release restricted substances, thus resulting in pollution of the air or underground water and requiring expenditures for cleaning and remediation.

## 15. Information Leakage

The Yamaha Group has important information regarding management and business matters as well as personal information related to a wide range of individuals including its customers. To manage this important information properly, the Group has prepared policies and rules and put into place systems for guarding its security. In the unlikely event that this information is mistakenly leaked outside the Group, this may have a major impact on the Group's business activities or result in a decline in the general public's confidence in the Group.

## 16. Fluctuations in Foreign Currency Exchange Rates

The Yamaha Group conducts manufacturing and sales activities in many parts of the world, and Group company transactions denominated in foreign currencies may be affected by fluctuations in currency rates. The Group makes use of forward currency hedge transactions to minimize the impact of foreign exchange rate fluctuations in the short term. However, there may be instances where the Group cannot achieve its initial business plans due to exchange rate fluctuations. Especially in the case of profit and loss, the euro-yen exchange rate has a strong influence: a one-yen change will have an impact on profitability of about ¥0.4 billion.

## 17. Earthquakes and Other Natural Disasters

In the event of earthquakes and other natural disasters, the production plants of the Yamaha Group may be damaged. In particular, the Company's headquarters, domestic plants, and major subsidiaries are concentrated in Shizuoka Prefecture, which is located in the Tokai region of Japan, where a major earthquake has been forecast for some years. In addition, the Group's overseas manufacturing plants are concentrated in China, Indonesia and Malaysia, where there is concern about the occurrence of unexpected natural disasters. In the event of such natural disasters, the Yamaha Group may suffer damage to its

facilities and may also be obliged to suspend or postpone operations as well as incur major costs for returning these facilities to operating condition.

## 18. Matters Related to Changes in Financial Position

### a. Valuation of Investment Securities

The companies of the Yamaha Group hold stock and other securities issued by their corporate customers and other companies that have quoted market values (representing acquisition costs of ¥17.1 billion and recorded on the consolidated balance sheets as ¥49.9 billion as of March 31, 2009). Since other securities with quoted market values are revalued at each balance sheet date based on the mark-to-market valuation method, there is a possibility that the value of such securities may fluctuate from period to period. As a result, this may have an impact on the Company's net assets. Moreover, in cases where the market value of these securities falls markedly in comparison to their acquisition cost, the value of such securities may have to be written down.

### b. Unrecognized Losses on Land Valuation

At the end of the fiscal year under review, the market value of the Group's land, revalued in accordance with relevant legal regulations, including the Law Concerning Revaluation of Land, was ¥12.1 billion below the carrying value of such land on the Group's balance sheets. In the event of the sale, or other disposal, of such land, this unrealized loss will be recognized and this may have an adverse effect on the Yamaha Group's business results and financial position.

### c. Retirement Benefit Obligation and Related Expenses

The Yamaha Group computes its obligation and expenses for retirement and severance based on its retirement and severance systems, a discount rate, and an expected rate of return on pension plan assets. In certain cases, the retirement and severance systems may be changed and the estimate of such obligation may change every accounting period. As a result, retirement benefit obligation and related expenses may increase.

Especially in the event that expected returns on management of such assets cannot be realized because of declines in stock prices and other factors, unrealized actuarial losses may arise, and expenses for retirement and severance purposes may increase.