

## Risk Factors

Listed below are the principal business risks of Sharp that may have a significant influence on investors' decisions. Note that in addition to these, there exist certain other risks that are difficult to foresee. Each of these risks has the potential to impact the operations, business results and financial position of Sharp. All references to possible future developments in the following text were made by Sharp as of March 31, 2013 (or June 25, 2013 as appropriate).

### (1) Global Market Trends

Sharp conducts its business in different regions around the world. Business results and financial position are thus subject to economic and consumer trends (especially trends in private consumption and corporate capital investment), competition with other companies, product demand, raw material supply and price fluctuations in each region, including Japan. The political and economic situation in respective areas may also exert an influence on business results and financial position.

### (2) Exchange Rate Fluctuations

The proportion of consolidated net sales accounted for by overseas sales was 47.3% in fiscal 2010, 51.9% in fiscal 2011 and 59.4% in fiscal 2012. Although Sharp hedges the risk of exchange rate fluctuations by employing forward exchange contracts and expanding and strengthening overseas production, such fluctuations may affect its business results.

### (3) Medium-Term Management Plan

Sharp is currently devoting relentless efforts toward realizing its Medium-Term Management Plan, announced on May 14, 2013. However, the plan is based on various assumptions concerning external factors, including customer demand for Sharp's products and services, foreign exchange rates, interest rates and the overall economic growth rate. Moreover, there is no guarantee that business initiatives outlined in the plan will be executed. Accordingly, it is possible that Sharp may not be able to achieve targets set under the plan. Moreover, enforcement of business restructuring may result in additional losses.

### (4) Dependence on Certain Products and Clients

Sales of LCDs and digital information equipments account for more than half of Sharp's total net sales. Accordingly, Sharp's business results may be impacted due to reasons including a decline in customer demand for such products, the arrival of alternative or competing products of other companies, and intensified competition stemming from the entry of new companies into the market. Because the sales of our LCDs and mobile phones are dominated by only a small number of clients, Sharp's business results and financial position could be affected if sales to such important clients languish due to, for example, its prod-

uct-related issues or the clients' sales strategies. Also, maintaining and developing business with such a small number of clients may lead to various limitations on Sharp's business operations.

### (5) Strategic Alliances and Collaborations

Sharp implements strategic alliances and collaborations as well as capital alliances with other companies—including the Samsung Group and the Qualcomm Group—in order to enhance corporate competitiveness, to improve profitability and to bolster the development of new technologies and products in various business fields. Moreover, Sharp's policy is to continue actively pursuing such alliances. If, however, any strategic or other business issues arise, or objectives change, it may become difficult to maintain such alliances and collaborative ties with these companies, or to generate adequate results. In such cases, Sharp's business results and financial position may be impacted. In addition, there is a possibility that alliances and collaborations could restrict the freedom of Sharp's business, or that shares issued under a capital alliance could dilute the value of existing shares. On March 27, 2012, Sharp Corporation entered into an agreement to execute capital and business alliance with four companies of the Hon Hai Group. However, subscription payment for shares to be issued under the agreement was not executed. Under the agreement, Sharp Corporation is to issue 121,649 thousand shares of common stock, to be purchased by the Hon Hai Group for ¥550.00 per share. The agreement is valid for three years.

### (6) Business Partners

Sharp procures materials and receives services from a large number of business partners, and transactions are made once a detailed credit check of the company has been completed. However, there is a risk that business partners may suffer deterioration in performance due to slumping demand or severe price erosion, or face an unexpected M&A, or be impacted by natural disasters or accidents, or become involved in a corporate scandal such as a breach of the law, or be affected by legal regulations concerning human rights or environmental issues such as the problem of "conflict minerals" in the supply chain. Due to these and other factors, Sharp may be unable to access sufficient supplies of materials/parts from procurement sources, or the quality of such materials/parts may be inadequate. Any of these factors may affect Sharp's business results and financial position.

### (7) Other Factors Affected by Financial Position

Sharp procures funds through borrowings from financial institutions, such as banks and life insurance companies, and through bond issues. As of March 31, 2013, the balance of such debt was equivalent to 54.8% of total assets. Accordingly, Sharp might become subject to restrictions on how it uses its cash flows in order to repay such debt, and also faces the possibility

of an increase in expenses due to rising interest rates. Moreover, Sharp has possibility of increase in fund procurement costs as well as limitations on fund procurement. This may be that necessary funds cannot be obtained at required time with adequate conditions, including for the refinancing of existing debt. These factors may affect Sharp's business results and financial position. Sharp has borrowing agreements with multiple financial institutions, and such agreements entail financial covenants. If its consolidated net assets, operating income or net income fall below the levels specified under such financial covenants, Sharp may forfeit the benefit of time at the lender's request. Moreover, Sharp may also forfeit the benefit of time on bonds and other borrowings if it violates the relevant financial covenants. In addition, dependence on borrowings, a credit ratings reduction caused by it, or deterioration of Sharp's financial position may work to its disadvantage with respect to competition with other companies with robust financial positions, and contract-related issues could also arise between Sharp and its lenders or business partners.

### **(8) Technological Innovation**

New technologies are emerging rapidly in the markets where Sharp operates. Resultant changes in social infrastructure, intensified market competition, changes in technology standards, obsolescence of technologies, or the appearance of substitute technologies may lead to an increase in inventories or the inability to recover product development costs. These and other factors may impact Sharp's business results and financial position.

### **(9) Intellectual Property Rights**

Sharp strives to protect its proprietary technologies by acquiring patents, trademarks, and other intellectual property rights in Japan and in other countries, and by concluding contracts with other companies. However, there is a risk that rights may not be granted, or a third party may demand invalidation of an application, such that Sharp may be unable to obtain sufficient legal protection of its proprietary technologies. In addition, intellectual property that Sharp holds may not result in a superior competitive advantage, or Sharp may not be able to make effective use of such intellectual property, such as when a third party infringes on the intellectual property rights of Sharp. There may also be instances where a third party launches litigation against Sharp, claiming infringement of intellectual property rights. Resolution of such cases may place a significant financial burden on Sharp. Furthermore, if such a third-party claim against Sharp is recognized, Sharp may have to pay a large amount of compensation, and may incur further damage by having to cease using the technology in question. Also, as a result of an M&A, a third party previously unlicensed to use Sharp's intellectual property may acquire such license, with the result that Sharp's intellec-

tual property may lose its superiority. Alternatively, an M&A with a third party could result in Sharp's business becoming subject to new restrictions to which it had not previously been subject, the resolution of which may require Sharp to pay additional compensation. Furthermore, although compensation is given to employees for innovations that they make in the course of their work pursuant to a patent reward system governed by internal regulations, an employee may consider such payment inadequate and initiate legal action. If any of the above problems related to intellectual property were to occur, it could impact Sharp's business results and financial position.

### **(10) Long-Term Investments and Agreements**

Sharp actively invests in manufacturing equipment and the like and has a large amount of noncurrent assets. Various factors related to such manufacturing equipment may prevent Sharp from securing anticipated income and require it to book impairment losses, which could impact its business results and financial position. These factors include equipment not functioning as expected and difficulty converting for other products due to equipment performance problems or contractual limitations. Sharp also has goodwill and other noncurrent assets. Sharp may be required to apply impairment treatment to such assets if its profitability declines or if the market prices of its asset holdings decline significantly. Such factors may affect Sharp's business results and financial position. In addition, Sharp has a large number of long-term contractual agreements in place, and fluctuations in prices and costs during the periods of such agreements may have a major negative effect on Sharp's business. In particular, there are such agreements covering raw materials for solar panels. These include a contract that obligates Sharp to purchase a total of 25,775 tons of polysilicon by the end of 2020 at a rate substantially higher than recent market prices (the weighted average price under the contracts exceeded the market price as of June 19, 2013 by around ¥2,500 per kilogram). Sharp's Medium-Term Management Plan, announced on May 14, 2013, incorporates the assumption that Sharp is obligated to purchase polysilicon at higher than market rates throughout the period covered by the plan.

### **(11) Product Liability**

Sharp manufactures products in accordance with strict quality control standards to ensure the utmost in quality. In order to fulfill its responsibility as a manufacturer in case product defects do arise, Sharp has taken out insurance to cover compensations based on product liability. Nonetheless, there is still a risk of a large-scale product recall or litigation caused by unforeseen events, which may adversely affect Sharp's brand image or influence its business results and financial position.

## (12) Laws and Regulations

The business activities of Sharp are subject to various regulations in countries where it operates, including business and investment approval, export regulations, tariffs, accounting standards and taxation. Sharp must also adhere to various laws and regulations concerning trading, antitrust practices, product liability, consumer protection, intellectual property rights, product safety, the environment, recycling and internal control, and labor regulations. Changes in such laws and regulations, or additional expenses to comply with the amendments, or the occurrence of violations of legal rules by persons in Sharp may affect Sharp's business results and financial position. Furthermore, in a case where an accident occurs related to one of Sharp's products, report of said incident, based on the Consumer Product Safety Law and related regulations in Japan, and disclosure of the accident information based on a system for public announcements could diminish Sharp's brand image.

## (13) Litigation and Other Legal Proceedings

Sharp conducts business activities around the world, and as such, there is a risk that Sharp could become involved with litigation and other legal proceedings in each country. If Sharp becomes involved in litigation or other legal proceedings, with the different legal and judicial systems in each country, depending on the case, Sharp may be ordered to pay a significant amount in damages or fines. Sharp is subject to investigations conducted by the Directorate-General for Competition of the European Commission, etc., with respect to its TFT LCD business. In addition, civil lawsuits seeking monetary damages resulting from alleged anticompetitive behavior have been filed in North America and Europe against Sharp. Sharp also received a cease and desist order and a surcharge payment order from the Japan Fair Trade Commission. However, Sharp has submitted a complaint to the Commission and the complaint is pending. With respect to the result of these proceedings and litigation, Sharp has made a reasonable estimate of potential future losses and provided a reserve in the amount deemed necessary. However, it is difficult to predict or estimate all results at this stage. An adverse result could affect Sharp's business results and financial position.

## (14) Leakage of Personal Data and Other Information

Sharp retains personal data and other confidential information concerning its customers, business partners and employees. Extreme care is taken to protect this information. A company-wide management system promotes employee education, internal auditing, and other measures aimed at ensuring compliance with management regulations. If information is leaked, however, it may reduce confidence in Sharp or result in substantial costs (associated with leakage prevention measures or indemnification

for damages, for instance), which may affect Sharp's business results and financial position.

## (15) Large-Scale Natural Disasters

Sharp has created and adopted preventative/emergency measures and a business continuity plan aimed at rapid recovery/restoration in order to be prepared and limit damage in the event of large-scale natural disasters such as earthquakes and typhoons. However, if Sharp or its partners' business activities are impaired due to the occurrence of a large-scale natural disaster, it may affect Sharp's business results and financial position.

## (16) Risks Accompanying the Nuclear Power Plant Disaster

The Tokyo Electric Power (TEPCO) Fukushima Daiichi Nuclear Power Plant accident accompanying the Great East Japan Earthquake on March 11, 2011, has had various adverse effects on both Japanese and overseas markets, which is affecting Sharp's business results and financial position. Moreover, in response to electricity usage restrictions in the areas served by TEPCO and Tohoku Electric Power, and energy-conservation requests in the areas served by Kansai Electric Power (KEPCO) and elsewhere in 2011, we are promoting company-wide energy-saving efforts. In the summer of 2012, Sharp responded to an energy-conservation request based on specific numerical targets determined by KEPCO. In the winter of 2012, Sharp responded to an energy-conservation request without numerical targets. In the future, if electricity supply shortages escalate due to electricity usage restrictions by the government or energy-conservation requests from power companies, and Sharp is requested to significantly reduce electricity usage amounts, or if a situation such as rolling blackouts occurs, plant operations will be reduced or production temporarily suspended, which may affect Sharp's business results and financial position. Moreover, substantial increases in electricity prices by electric power companies may also affect Sharp's business results and financial position.

## (17) Competition to Secure Skilled Personnel

To achieve future success, Sharp relies heavily on its ability to secure exceptional human resources in such fields as science, technology, and management. However, since demand for talented personnel in various fields exceeds supply, competition to secure human resources is increasing. In the event that Sharp is unable to attract personnel or prevent the departure of existing employees, its business results and financial position may be affected.

## (18) Other Key Variable Factors

In addition to the aforementioned risks, Sharp's business results may be significantly affected by human-induced calamities such as accidents, conflicts, insurrections or terrorism; the spread of

a new strain of influenza or other infectious disease; or major fluctuations in the stock and bond markets.

### **(19) Outline of Significant Events Relating to Assumed Going Concern**

The operating results for the six months ended March 31, 2013, turned positive due to sales increase of distinctive devices and products such as smartphones and tablet terminals with IGZO LCDs as well as Black Solar high-efficiency solar cells. Also, company-wide measures, including reductions in inventories and slashing total costs primarily focused on labor costs through such schemes as a voluntary retirement program, have largely contributed to the turnaround. Continuing from the previous fiscal year, Sharp's consolidated financial performance for fiscal 2012 resulted in substantial operating and net losses, as well as substantial negative cash flows from operating activities. In addition, concerns have been expressed that Sharp might face difficulties in redemption of the 20th unsecured convertible bonds with subscription rights to shares, due on September 30, 2013. Although there are events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, we believe that these conditions will not cast a material uncertainty about Sharp's ability to continue as a going concern, due to implementation of various measures to resolve these and other major issues as described below. Therefore, no further disclosure for the "Going Concern Assumption" in the notes to the consolidated financial statements is necessary.

Sharp has received continued support and cooperation from financial institutions. With respect to a ¥360.0 billion syndicated loan due in June 2013, the agreement was amended on June 25, 2013 to extend the loan with the consent of the two main banks—Mizuho Corporate Bank, Ltd. and The Bank of Tokyo-Mitsubishi UFJ, Ltd.—and other participating banks. On the same day, an agreement was reached with the two main banks to provide an additional borrowing facility of ¥150.0 billion, which will be used to redeem Sharp's 20th unsecured convertible bonds with subscription rights to shares, due on September 30, 2013. Accordingly, there is no problem with the redemption of those bonds. As a corporate strategy for steady achievement of "recovery and growth," Sharp has developed a Medium-Term Management Plan incorporating five strategic measures: "Restructuring its Business Portfolio," "Improving the Profitability of its LCD Business," "Expanding Overseas Businesses Focusing on the ASEAN Market," "Reducing Fixed Costs by Reforming its Cost Structure," and "Improving its Financial Position." Also, in order to strengthen headquarters control and governance function, as well as action forces to complete the Medium-Term Management Plan, Sharp newly set up the "Corporate Management Group" and "Structural Reform Group." Through steady implementation of the Medium-Term Management Plan and

financial arrangements, Sharp aims to improve its financial position, while at the same time reinforcing management foundation, to realize sustainable growth and a stable net income.