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, 2015 (or June 23, 2015 as appropriate).

(1) Global Market Trends and Overseas Businesses

Sharp conducts its business not only in Japan but also in different regions around the world, mainly in countries of the U.S., Europe, and Asia. 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. Moreover, difficulty in monitoring and adjusting its operations in various regions; the growing impact of world economic recession; risks related to regulations and taxation in foreign countries; various standards and customs related to doing business; trade restrictions; political instability and business uncertainty; changes in political and economic relations with Japan; social turmoil; rising personnel costs; and labor issues, etc. may affect Sharp's business results and financial position.

(2) Exchange Rate Fluctuations

The proportion of consolidated net sales accounted for by overseas sales was 59.4% in fiscal 2012, 60.7% in fiscal 2013, and 65.2% in fiscal 2014. In addition, Sharp sells products made overseas in the Japanese market, and also sells products in countries where it does not manufacture the products. Although Sharp hedges the risk of exchange rate fluctuations by employing forward exchange contracts and expanding and strengthening optimally located production, such fluctuations may affect its business results.

(3) Medium-Term Management Plan

On May 14, 2015, Sharp announced its new Medium-Term Management Plan, which it is now working diligently to implement. 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 in Japan and abroad. 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 its 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 equipment 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, falling product prices, the arrival of alternative or competing products of other companies, and intensified competition stemming from the entry of new companies into the market. Sales of Sharp's LCDs and mobile phones are dominated by only a small number of clients, who thus account for a considerable share of sales. Sharp's business results and financial position could be affected if sales to such important clients languish due not to only factors related to Sharp's products but reasons outside of Sharp's control. These include declining demand for the clients' products, changes in product specifications, and changes in the clients' sales strategies. In addition, if such clients have concerns about Sharp's financial position, they may reduce the scale of transactions with Sharp, and prioritize transactions with their own affiliated companies for certain products. Moreover, 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, limitations could be placed on alliances and collaborations with other companies in the same industry, or conditions could be placed on alliances and collaborations could restrict the freedom of Sharp's business. Also, shares issued under a capital alliance with a strategic partner could dilute the value of existing shares. For example, Sharp has an agreement with the Samsung Group giving Samsung preferential negotiating rights in the event that Sharp wishes to sell part of its business solutions business. (At present, Sharp has no intention of selling that business.) 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 and can be renewed. If certain conditions are fulfilled, including notification of the securities registration statement in Japan, and Sharp issues the aforementioned shares to the Hon Hai Group, Sharp's existing shares could be diluted. The Hon Hai Group has made an announcement to the effect that an agreement has been reached to change conditions for issuing the aforementioned shares, but Sharp believes this is not true.

(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"

Risk Factors

in the supply chain, or legal restrictions, or limited suppliers with capability of providing certain material provisions. 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. In such an event, Sharp may be forced to do business with alternative suppliers subject to conditions less favorable than with its current suppliers, or Sharp may be unable to find a supplier in a timely manner. Any of these factors could lead to a decline in the quality of Sharp's products, increases in costs, and/or delays in deliveries to customers, which may affect Sharp's business results and financial position. Under agreements with certain clients, Sharp receives advanced payments for the trading value of its products. At present, the obligation to repay such advances is offset by Sharp's accounts receivable in connection with said clients. Depending on Sharp's financial circumstances, however, under the agreements with said clients, Sharp may be requested to repay a major portion of the advances. If a request for repayment of advances is made, this could have a negative effect on Sharp's operating cash flows.

(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, 2015, the balance of such debt was equivalent to 48.6% of total assets, and short-term borrowings accounted for 88.1% of such debt. 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 increases in fund procurement costs as well as limitations on fund procurement. This may be because necessary funds cannot be obtained at the 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 some of the agreements entail financial covenants. If its consolidated net assets fall below the levels specified under such financial covenants, or if Sharp fails to undertake faithful consultations in the event that its consolidated operating income and net income fall below specified levels, 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. Sharp's major lending institutions are Mizuho Bank, Ltd. and The Bank of Tokyo-Mitsubishi UFJ, Ltd. As necessary, Sharp consults with both banks about ways to improve its financial position and other matters. In June 2013, one of member of each bank was appointed as a director of Sharp. In June 2015, moreover, two persons nominated by Japan Industrial Solutions Fund I—which will purchase Class B Shares in a subscription agreement with Sharp—have been elected as outside directors of Sharp. 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 make Sharp unable to introduce new products in a timely manner, or 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. Apart from technologies, Sharp faces intense competition from price and marketing perspectives as well, and winning against such competition is not guaranteed. Depending on the outcome of fierce competition with other companies, Sharp may be forced to downsize or withdraw from existing businesses, which could incur additional costs. Moreover, Sharp engages in R&D under collaborative development agreements with other companies, and it is possible that such relationships cannot be maintained, or that satisfactory outcomes cannot be produced, or that termination of such relationships cannot be handled smoothly.

(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, or may be unable to receive sufficient royalty income from the granting of licenses. 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 the period of a license received from a third party expires, or for some reason or other, is terminated, or 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, in the event that a company licensed to use Sharp's intellectual property is acquired by a third party, the third party, previously unlicensed to use Sharp's intellectual property, may acquire such license, with the result that Sharp's intellectual property may lose its superiority. Alternatively, the formation of an alliance with said 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. Moreover, the formation of such an alliance could result in claims for infringement of an existing licensing agreement with another third party, placing pressure on Sharp to cancel said alliance. 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

Risk Factors

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 to 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 many of those agreements include promises of fixed prices or price adjustments only at predetermined intervals during the agreement period. Accordingly, 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 20,779 tons of polysilicon (as of the end of March 2015) by the end of 2020 at a rate substantially higher than the most recent market price (the weighted average price under the contracts exceeded the market price as of March 31, 2015 by around ¥2,630 per kilogram). Sharp's business plan incorporates the assumption that Sharp is obligated to purchase polysilicon at higher rates than market prices. Nevertheless, intensified competition caused by the entry of overseas manufacturers, falling prices of solar panels stemming from reductions in electric power purchase prices, dramatic foreign exchange fluctuations, and other factors have caused Sharp's business environment to deteriorate, making it difficult to secure future profitability. In fiscal 2014, Sharp recorded a valuation reserve for inventory purchase commitments on polysilicon materials, to cover the difference between the contracted purchase price and the most recent market price. If the market price of polysilicon falls even further, Sharp may incur additional losses. Moreover, because some of the purchase contracts at year-end prohibit the resale of polysilicon, Sharp may have difficulty recovering its losses if the prospects for future use of the material deteriorates, which in turn could incur further additional losses. Meanwhile, Sharp has long-term contractual agreements with multiple suppliers covering the supply of electricity necessary to produce solar cells at its Sakai Plant. At the end of fiscal 2014, total amount of future payments of such contracts was ¥43,915 million (remaining terms of between 2.5 and 14 years), and none of the contracts can be cancelled prior to maturity. These long-term contracts cover the supply of electricity necessary to produce 480MW of solar cells annually. However, the actual production volume at the Sakai Plant is only 160MW per year, which is incurring considerably high production costs for the energy solutions business.

(11) Product Liability

Sharp manufactures products in accordance with strict quality control standards to ensure the utmost in quality. However, many of its products are for consumer use, and also incorporate innovative technologies. If defects arise in any of these products, Sharp may incur responsibility as a manufacturer and other obligations. 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, 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 elsewhere against Sharp. 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. In addition to proceedings already under way, new investigations by regulatory authorities or civil litigations may be filed in the future. Any adverse results 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 preventative/emergency measures and a business continuity plan aimed at rapid recovery/restoration in order to be prepared

Risk Factors

for and minimize damage in the event of large-scale natural disasters such as earthquakes and typhoons, and is working hard to avoid the impact of such disasters. However, if Sharp or its partners' business activities are impaired directly or indirectly due to the occurrence of an unprecedented large-scale natural disaster, it may affect Sharp's business results and financial position.

(16) Risks Accompanying the Nuclear Power Plant Disaster

Electric power generation problems, caused by the nuclear power plant accident accompanying the Great East Japan Earthquake, have had various adverse effects on both Japanese and overseas markets, which is affecting Sharp's business results and financial position. The Japanese government has signaled its intention to reinstate nuclear power generation following cabinet approval of a basic energy plan defining nuclear as an "important baseload power source." In the absence of a timeframe for reinstatement, however, power generation problems remain unsolved at the present time. Any possible future restrictions on electricity usage or hikes in electricity prices stemming from electricity shortages could cause plant operations to be reduced and/or costs to increase, which may affect Sharp's business results and financial position.

(17) Competition to Secure Skilled Personnel

Exceptional human resources in such fields as technology and management are crucial to Sharp's future growth and development. However, since demand for talented personnel in various fields exceeds supply, competition to secure human resources is intensifying. In the event that Sharp is unable to attract new personnel or prevent the departure of existing employees, or is unable to improve the skills of key personnel engaged in business management, 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

In the two-year period through fiscal 2012, Sharp consecutively posted large operating losses and net losses, as well as negative major operating cash flows, and its financial position weakened as a result. In response, Sharp formulated a Medium-Term Management Plan in May 2013 and has since worked diligently to achieve recovery and growth. With respect to performance, therefore, Sharp returned to profitability in fiscal 2013, with consolidated net income of ¥11,559 million. On the funding side, Sharp has received continuous support from financial institutions, including a syndicated loan, enabling redemption of bonds upon maturity. Sharp also secured funds and strengthened its financial base, by issuing new shares via public offering and third-party allotment, etc. In fiscal 2014, however, Sharp once again incurred a substantial operating loss and net loss due to falling prices of small- and medium-size LCDs, loss on related to valuation reserve for inventory purchase commitments, impairment losses, restructuring charges, and other measures aimed at improving its operational foundation. These factors made it difficult to achieve the targets of the Medium-Term Management Plan. Accordingly, consolidated net assets have declined significantly, to levels infringing on financial covenants of the syndicated loan agreement. Moreover, the term of the syndicated loan expires on March 31, 2016. 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 formulated a new Medium-Term Management Plan for Fiscal 2015 through 2017. Under the plan, Sharp will strive to build stable earnings foundation by steadily implementing three key strategies: (1) Restructure business portfolio, (2) Reduce fixed costs, and (3) Reorganize and strengthen corporate/governance systems. Furthermore, based on the premise of the plan's implementation, Sharp will issue preferred shares totaling ¥200.0 billion to two main banks—Mizuho Bank, Ltd. and The Bank of Tokyo-Mitsubishi UFJ, Ltd.—in order to reinforce deteriorated capital base. Sharp will also issue preferred shares totaling ¥25.0 billion to Japan Industrial Solutions Fund I, managed by Japan Industrial Solutions Co., Ltd., to raise investment capital. In both cases, Sharp concluded preferred share subscription agreements on May 14, 2015, and related proposals (change to Articles of Incorporation, type of shares issued, reduction in capital, etc.) received approval at the 121st Ordinary General Meeting of Shareholders, held on June 23, 2015. Reconciliation among financial institutions and other matters that reasonably satisfy the underwriting financial institutions are expected to be completed by the payment date. Sharp will work steadily to reinforce its capital base and implement its Medium-Term Management Plan while helping those institutions and other related parties reach an understanding of Sharp's initiatives as before. Moreover, despite financial covenants being infringed upon, Sharp's main financial institutions indicate that they are not considering enforcing forfeiture of the benefit of time. With respect to the expiration of the syndicated loan contract, as well, Sharp has received informal notice from the financial institutions that they will continue supporting Sharp during the period of the new Medium-Term Management Plan, subject to the successful completion of the preferred share underwritings. Accordingly, Sharp will avoid the risk of capital inadequacy and, thanks to the continued support of financial institutions, will implement specific measures outlined in its new Medium-Term Management Plan.