

3.D. RISK FACTORS

Risks Related to Advantest's Business

Advantest's business and results of operations are subject to significant demand volatility in the semiconductor industry

Advantest's business depends largely upon the capital expenditures of semiconductor industrial, design and manufacturing companies, fabless semiconductor companies, foundries and test houses. These companies, in turn, determine their capital expenditure and investment levels largely based on current and anticipated market demand for semiconductors and products incorporating semiconductors. Such demand is influenced significantly by the overall condition of the global economy. Historically, the percentage reduction in capital expenditures by semiconductor manufacturers during downturns in the semiconductor industry, including investment in semiconductor test systems, has typically been much greater than the percentage reduction in worldwide sales of semiconductors. The semiconductor industry has been highly cyclical with recurring periods of excess inventory, which often have had a severe effect on the semiconductor industry's demand for semiconductor test systems, including those of Advantest. In particular, the market for memory semiconductors shows higher demand volatility as compared to the market for non memory semiconductors. Advantest derives significant sales from test systems for memory semiconductors in the Semiconductor and Component Test Systems; in fiscal 2013, net sales of test systems for memory semiconductors increased by 14.5% to 32.1% from 17.6% in fiscal 2012. Therefore, any downturn in the memory semiconductor market may continue to adversely affect Advantest's business and results of operations.

The worldwide semiconductor market contracted by 9.0% in 2009 compared to the previous year, continuing to reflect the global economic downturn that stemmed from the financial crisis. After the negative growth in 2009, the market significantly recovered in 2010, growing by 31.8% compared to 2009, primarily due to a surge in demand for electronic equipment in developing nations. In 2011, due to the global economic recession and natural disasters such as the Great East Japan Earthquake and the floods in Thailand reducing production activities of electronic products, the semiconductor market only increased by 0.4% compared to 2010. In 2012, the semiconductor market decreased by 2.7% compared to 2011, due to factors such as the prolonged stagnation in the European economy caused by the debt crisis in the Southern European countries and the slowdown in the Chinese economy, which had been supporting the global economy. In 2013, the semiconductor market increased by 4.8% compared to 2012, due to an overall steady demand for semiconductors, despite some variations among products. Worldwide sales of non memory semiconductors in 2009 decreased by 10.3% compared to 2008, primarily as a result of the impact of the global economic downturn stemming from the financial crisis that started in 2008. In 2010, worldwide sales of non memory semiconductors increased by 26.0% compared to 2009, primarily due to robust demand for smartphones, tablet-type devices, and other consumer electronics. In 2011, worldwide sales of non memory semiconductors further increased by 4.4% compared to 2010, due to continuing robust demand for smartphones, tablet-type devices, and similar devices. In 2012, although sales of communications semiconductors and LCD drivers semiconductors, among others, remained strong due to continued robust demand in the mobile devices market, worldwide sales of non memory semiconductors decreased by 1.8% compared to 2011 due to the downturn in sales of other electronic devices. In 2013, worldwide sales of non memory semiconductors increased by 1.7% compared to 2012 due to a steady demand for tablet-type devices and smartphones. Although the markets for personal computers and cellular phones including smartphones remained steady in 2009, worldwide sale of memory semiconductors declined by 3.3% compared to 2008, reflecting the global economic downturn, resulting in negative growth. In 2010, primarily due to a steady demand for mobile DRAM test systems for mobile devices, worldwide sales of memory semiconductors increased by 55.4% compared to 2009. In 2011, worldwide sales decreased by 12.7% compared to 2010 due to a drop in the price of DRAM triggered by a downturn in demand for PCs and similar devices. In 2012, sales continued to decrease by 6.2% compared to 2011 due to the ongoing weakness in demand for PCs and similar devices. In 2013, sales increased by 17.6% compared to 2012 due to, among other factors, an increased demand for DRAM and LPDDR for products such as low end smartphones.

The significant volatility in demand for semiconductors is affected by various factors such as:

- the overall state of the global economy;
- levels of investment in communications infrastructure and trends of demand in communication devices such as tablet-type devices and smartphones;
- demand in personal computer and data server industries;
- consumer demand for digital consumer products such as flat-panel TVs, DVD/Blu-ray disc recorders, portable audio players and electronic books;
- demand in the automobile industry; and
- trends in the semiconductor industry.

In fiscal 2009, the semiconductor manufacturers gradually resumed capital expenditures as semiconductor prices rose and equipment utilization rates climbed. Despite the gradual recovery in fiscal 2009, Advantest's net sales in fiscal 2009 decreased by 30.6%, as compared to fiscal 2008, to ¥53,225 million, primarily due to the drop in orders seen in the second half of fiscal 2008. In fiscal 2010, despite a difficult business environment with factors such as continuing appreciation of the Japanese yen and intensified price competition, Advantest seized the positive growth opportunity in the semiconductor market and strived to expand orders and revenues. As a result of the above, Advantest's net sales in fiscal 2010 increased by 87.2% as compared to fiscal 2009, to ¥99,634 million, and Advantest recorded a net income of ¥3,163 million in fiscal 2010. In fiscal 2011, Advantest expanded sales to meet areas of increasing demand growth such as test equipment for application processors, CMOS image sensors, and other non memory semiconductor sectors. In addition, after the completion of the acquisition of Verigy Ltd. ("Verigy") in July 2011, Advantest has enhanced sales promotion to customers in the U.S. and Europe and has provided products tailored to better meet increasing customer demand in the communications semiconductor market. As a result of the above, Advantest's net sales in fiscal 2011 increased by 41.6%, as compared to fiscal 2010, to ¥141,048 million. However, cumulative costs associated with the Verigy acquisition and impairment losses on investment securities led to a year-on-year decline in earnings, and Advantest recorded a net loss in fiscal 2011 of ¥2,195 million. In this environment, Advantest actively marketed semiconductor testing equipment for mobile communications-related semiconductor applications—the largest segment for testing equipment—and as a result, the company successfully gained market share. However, the gain in market share could not fully offset the decrease in demand for semiconductor testing equipment resulting from capital expenditure constraints of semiconductor manufacturers experiencing a slowdown in the semiconductor market. As a result of the above, Advantest's net sales in fiscal 2012 decreased by 5.8%, as compared to fiscal 2011, to ¥132,903 million. The product mix in sales also worsened, leading to a net loss in fiscal 2012 of ¥3,821 million. In Advantest's core line of semiconductor test equipment, difficult business climate prevailed as a result of significant constraints in capital investments by some of Advantest's major customers since last summer, for non memory test systems. As a result of the above, Advantest's net sales in fiscal 2013 decreased by 15.8%, as compared to fiscal 2012, to ¥111,878 million. From a profit and loss perspective, in addition to the decline in net sales, an increase in costs denominated in foreign currency due to the continuing depreciation of the yen, and recognizing inventory valuation losses and impairment losses for long-lived assets due to changes in the business environment, resulted in a net loss of ¥35,540 million.

Advantest believes that its results are significantly affected by the significant volatility in demand in the semiconductor industry. While Advantest is unable to predict future trends in the semiconductor industry, if there is a significant downturn in the semiconductor industry, Advantest's financial condition and results of operations will be adversely affected. With respect to semiconductor prices in recent years, even though prices for certain products such as DRAM appear to have bottomed out, if the prices decline as a result of over-supply of semiconductors, semiconductor manufacturers' earnings could deteriorate, resulting in their further restraint towards capital expenditures, and Advantest's results of operations could be adversely affected.

If Advantest does not introduce new products meeting its customers' technical requirements in a timely manner and at competitive prices, its products may become obsolete and its financial condition and results of operations may suffer

Advantest sells its products to several industries that are characterized by rapid technological changes, frequent introduction of new products and services, varying and unpredictable product lifecycles and evolving industry standards. Advantest anticipates that future demand for its products will be driven, in large part, by technological innovation in semiconductor technology, which creates new testing requirements that are not adequately addressed by currently-installed semiconductor test systems. Customer needs in response to these technological innovations, and their need for greater cost-effectiveness and efficiency to respond to the market environment, include:

- test solutions of non memory semiconductors that incorporate more advanced memory semiconductors, logic and analog circuits;
- test solutions of power semiconductors that control small and large motor drives;
- solutions for complexed IC incorporating RF, logic and memory chips in a single package in order to achieve IC with advanced 3D integration as well as downsizing and technical advantages, with TSV technology;
- mechatronics-related products which transport devices faster, more accurately and more stably;
- test solutions of testing technologies that employ self-test circuit designs incorporated into semiconductor chips;
- test solutions of testing technologies that employ test circuit designs for Device Under Test (DUT);
- introduction of mechatronics products that respond to reduced testing time resulting from advances in customers' back-end testing;
- prompt response and quick repair in the event of failure;
- total solutions that allow customers to reduce their testing costs; and
- solutions for measurement and observation of state-of-the-art photomasks.

Advantest also believes demand for its products, including semiconductor and component test systems, is affected by the level of demand for personal computers, high-speed wireless and wireline data services, digital consumer products and communication devices, such as tablet-type devices and smartphones, and data servers. It is likely that advances in technologies used in those products and services will require new testing systems. Without the timely introduction of semiconductor test systems capable of effectively testing and measuring equipment that use these new technologies, Advantest's products and services may become technologically obsolete over time.

A failure by Advantest to meet its customers' technical requirements at competitive prices or to deliver conforming equipment in a timely manner may result in its products being replaced by those of a competitor or an alternative technology solution. Furthermore, Advantest's inability to provide a product that meets requested performance criteria at an acceptable price when required by its customers would severely damage its reputation with such customers and may adversely affect future sales efforts with respect to such customers.

Advantest's dependence on certain subcontractors and its dependence on a sole source or a limited number of suppliers for its components and parts may prevent it from delivering products that meet specifications on a timely basis

Advantest relies on subcontractors to perform some of the assembly requirements for its products. In addition, many of the components used in Advantest's semiconductor and component test systems and

mechatronics systems are produced by suppliers based on Advantest's specifications. Advantest's reliance on these subcontractors and suppliers gives it less control over the manufacturing process and exposes it to significant risks, especially inadequate manufacturing capacity, late delivery, substandard quality, lack of labor availability and high costs. In addition, Advantest depends on a sole source or a limited number of suppliers for a portion of its components and parts. Advantest does not maintain long-term supply agreements with most of its suppliers, and it purchases most of its components and parts through individual purchase orders. If a supplier becomes unable to provide components or parts in the volumes needed and at acceptable prices, or if a supplier withdraws from business thereby stopping production or sales of custom or general components and parts that Advantest uses or will use in the future, Advantest would have to identify and procure acceptable replacements. Advantest may lose its capacity to supply test systems if it becomes unable to procure acceptable replacements. Furthermore, the markets for semiconductors and other specialized components have, in the past, experienced periods of inadequate supply to meet demand. Moreover, there may be a shortage of components if a large scale natural disaster or electricity shortage occurs. The process of selecting subcontractors or suppliers and of identifying suitable replacement components and parts is lengthy and may result in Advantest being unable to deliver products meeting customer requirements in a timely manner. Advantest has, in the past, been unable to deliver its products according to production schedules primarily due to the inability of suppliers to supply components and parts based on Advantest's specifications and by other shortages in components and parts. Moreover, a deterioration in the financial position of Advantest's subcontractors or suppliers reflecting the decline in the economic environment may result in certain subcontractors and suppliers being unable to meet Advantest's requirements.

Advantest faces substantial competition in its businesses and, if Advantest does not maintain or expand its market share, its business may be harmed

Advantest faces substantial competition throughout the world. Advantest's primary competitors in the semiconductor and component test system market include, among others, Teradyne, Inc., LTX-Credence Corporation, UniTest Inc. and EXICON Ltd. In the mechatronics system related market, Advantest also competes with Delta Design, Inc., TechWing, Inc., Seiko Epson Corporation and Mirae Corporation in test handler devices, and with TSE Co., Ltd., Semes Co., Ltd. and SL-link Co., Ltd. in device interfaces. Some of Advantest's competitors have greater financial and other resources than Advantest.

Advantest faces many challenges in its businesses, including increased pressure from customers to produce semiconductor and component test systems and mechatronics systems that reduce testing costs. For device interfaces, acquisition of vendors that supply core technical components by Advantest's competitors, or leakage of the manufacturing technology of printed circuit boards, may result in reduced testing costs by customers or difficulty by Advantest to realize its products' full performance.

To compete effectively and maintain and expand its market share, Advantest must continue to enhance its business processes to lower the cost of its products, or introduce enhancements that lower overall testing costs. Advantest also expects its competitors to continue to introduce new products with improvements in price and performance, as well as increasing their customer service and support offerings, and Advantest expects new market participants to launch low-price testers. Significant increases in competition may erode Advantest's profit margin and weaken its earnings.

Advantest may not be able to meet the targets set in its strategies and medium-term business plan

Advantest had embarked on "ACT2014", a medium-term business plan setting certain goals for the fiscal year ending 31 March 2015, but as a result of the impact of the global economic recession, the volatility of the semiconductor industry and other factors that arose after the medium-term business plan's announcement, Advantest's results for fiscal 2014 is expected to significantly fall short of the plan's initial targets. The attainment of medium-term goals is subject to various internal and external factors, including the general economic and market conditions in which Advantest and its customers operate, the level of competition, the level

of corporate capital expenditure, the level of demand for Advantest's products and fluctuations in exchange rates. As a result, any announced goals and targets (as amended from time to time) should not be treated as forecasts of future results. There can be no assurance that Advantest's strategies to accomplish the medium-term business plan and implementation of such strategies will be successful, that the implementation of its strategies will have the intended effects, that the medium-term business plan or other targets (whether quantitative or qualitative, and as amended from time to time) will be met, or that such goals, targets and aims will not be changed in the future by Advantest's management.

Failure by Advantest to meet demand for its products upon a sudden expansion of the markets for semiconductor and component test systems and mechatronics systems may adversely affect its future market share and financial results

Advantest procures components and parts used in its products from suppliers, but such suppliers have typically adjusted their production capacity through the reduction of production lines and personnel. If the market for semiconductor and component test systems and mechatronics systems were to suddenly expand, Advantest would require significant increases in production capabilities including personnel, as well as materials, components and supplies from suppliers, in order to fully capitalize on such expansion. The failure of Advantest to adjust to such unanticipated increases in demand for its products during the period of recovery in demand could result in Advantest losing one or more of its existing large-volume customers or losing the opportunity to establish a strong relationship with potential large-volume customers with which it currently does little or no business. Such failure may adversely affect Advantest's future market share and its financial results.

Advantest's largest customers currently account for a significant part of its net sales and, in addition to the risk of Advantest's business being harmed by the loss of one or more of these customers or changes in their capital expenditures, Advantest may not be able to recover its accounts receivables if its largest customers experience a deterioration in their financial position

Advantest's success depends on its continued ability to develop and manage relationships with its major customers. A small number of such major customers currently account for a significant portion of its net sales. Sales to Advantest's largest customer as a percentage of its total sales were approximately 29% in fiscal 2011, approximately 14% in fiscal 2012 and approximately 15% in fiscal 2013. Sales to Advantest's five largest customers accounted for approximately 56% in fiscal 2011, approximately 37% in fiscal 2012 and approximately 36% in fiscal 2013. The loss of one or more of these major customers or changes in their capital expenditures could materially harm Advantest's business. Furthermore, if Advantest's major customers experience deterioration in their financial position and are unable to fulfill their payment obligations to Advantest in accordance with the applicable terms, Advantest's business, results of operations and financial position may be adversely affected.

Advantest's product lines are facing significant price pressure

Price pressure on Advantest's businesses is adversely affecting Advantest's operating margins. Irrespective of the trend in the demand for semiconductors, there is ongoing price pressure on semiconductors, which puts continuous pressure on the market price for products in the Semiconductor and Component Test System Segment and Mechatronics System Segment. Especially with the ongoing slowdown in the semiconductor industry, price pressure is salient. During these periods, semiconductor manufacturers and test houses, which are Advantest's customers, seek to increase their production capacities while minimizing their capital expenditures. In addition, increased competition in the market for digital consumer products, personal computers, mobile devices such as tablet-types devices and smartphones and the market for data servers have driven down prices of these goods, subsequently creating significant price pressure on Advantest's product lines. If prices of semiconductors continue to decline, customers may postpone capital expenditures on new equipment by remodeling or adapting the usage of existing equipment. If price pressure further increases in the future, Advantest's financial condition and results of operations may be adversely affected.

Advantest may not recoup costs incurred in the development of new products

Enhancements to existing products and the development of new generations of products are, in most cases, costly processes. Furthermore, because the decision to purchase semiconductor and component test systems products and mechatronics systems generally involves a significant commitment of capital, the sale of this equipment typically involves a lengthy sales period and requires Advantest to expend substantial funds and sales efforts to secure the sale. Advantest's enhancements or new generations of products may not generate net sales in excess of development and sales costs if, for example, these new enhancements or products are quickly rendered obsolete by changing customer preferences, the introduction by Advantest's competitors of products embodying new technologies or features, the introduction by Advantest's customers of new products that require different testing functions or the failure of the market for Advantest's customer's products to grow at the rate, or to the levels, anticipated by Advantest. This risk is believed to be particularly acute with respect to test systems for non memory semiconductors because, in general, new non memory semiconductor product lines are introduced to market more frequently than new memory semiconductor product lines. In some cases, Advantest must anticipate industry trends and develop products in advance of the commercialization of its customers' products. This requires Advantest to make significant investments in product development well before it determines the commercial viability of these innovations. If Advantest's customers fail to introduce their devices in a timely manner or the market rejects their devices, Advantest may not recover its investments in product development through sales in significant volume.

The market for Advantest's major products is highly concentrated, and Advantest may not be able to increase sales of its products because of limited opportunities

The market for test systems for memory semiconductors in the Semiconductor and Component Test System Segment is highly concentrated, with a small number of large semiconductor manufacturers, foundries and test houses accounting for a large portion of total sales in the semiconductor and component test system industry. Advantest believes that this market concentration could become even more severe in the future as larger semiconductor device manufacturers, foundries and test houses acquire smaller semiconductor market participants, and as corporate restructuring, such as elimination and consolidation of businesses, progresses. Advantest's ability to increase sales will depend in large part upon its ability to obtain or increase orders from large-volume customers. Furthermore, in the event there is an over-supply of semiconductor and component test system products on the second-hand market reflecting, among others, restructuring within the industry, Advantest faces an additional risk of losing its sales opportunities.

Fluctuations in exchange rates could reduce Advantest's profitability

The majority of Advantest's net sales derive from products sold to customers located outside of Japan. Of Advantest's fiscal 2013 net sales, 89.1% were from products sold to overseas customers. Most of Advantest's products are manufactured in Japan, but approximately 61% of Advantest's net sales in fiscal 2013 were derived from currencies other than the Japanese yen, predominantly the U.S. dollar. If the Japanese yen becomes strong relative to foreign currencies (mostly U.S. dollar and, to a much lesser extent, other currencies), it would increase the prices of Advantest products as stated in U.S. dollars and in those other currencies, which could hurt sales in those countries.

With respect to the Euro, if the weakening of the Japanese yen continues, there may be a negative impact on Advantest's profitability since there are currently more costs incurred in Euro than net sales derived in Euro.

In addition, significant fluctuations in the exchange rate between the Japanese yen and foreign currencies, especially the U.S. dollar, could require Advantest to lower its prices with respect to foreign sales of its products that are priced in Japanese yen, and reduce the Japanese yen equivalent amounts of its foreign sales for products that are based in U.S. dollars or other foreign currencies, thereby reducing its profitability overall. These fluctuations could also cause prospective customers to push out or delay orders because of the increased relative cost of Advantest's products. In the past, there have been significant fluctuations in the exchange rate between the Japanese yen and the foreign countries in which Advantest's sales are denominated.

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Furthermore, Advantest's consolidated financial statements for a particular period or for a particular date will be affected by changes in the prevailing exchange rates of the currencies in which subsidiaries of Advantest prepare their financial statements against the Japanese yen. Foreign exchange rate fluctuations may have an effect on those amounts not denominated in yen which are translated into yen in Advantest's consolidated financial statements, and depending on the direction of the foreign exchange fluctuation, may have an adverse effect on Advantest's reported financial position, results of operations and net assets.

If Advantest's main facilities for research and development, production or information technology systems for its businesses, or the facilities of its subcontractors and suppliers, were to experience catastrophic loss, its results of operations would be seriously harmed

Advantest's main facilities for research and development for its Semiconductor and Component Test Systems and Mechatronics System Segments production, as well as many of Advantest's service bases, are located in Japan and particularly concentrated in Gunma Prefecture and Saitama Prefecture. In addition, the main system server and the network hub are maintained in system centers approved by the Information System Management System, or ISMS, and local network servers are located in certain operations offices in Japan. As most recently evidenced by the Great East Japan Earthquake in March 2011, Japan is a region that is susceptible to frequent earthquakes.

If Advantest's facilities, particularly its semiconductor and component test system manufacturing factories, were to experience a catastrophic loss, it would materially disrupt Advantest's operations, delay production, shipments and revenue, and result in large expenses to repair or replace the facilities. Advantest has insurance to cover most potential losses at its manufacturing facilities, other than those that result from earthquakes. However, this insurance may not be adequate to cover all possible losses. Similar disruptions to Advantest's business may occur if the facilities of Advantest's subcontractors and suppliers or if the facilities of Advantest's information system network were to experience a catastrophic loss.

Advantest has prepared itself for crises such as large-scale natural disasters, and each department of Advantest has documented its own disaster-response procedures and manuals. Furthermore, in order to prevent any disruption of its core businesses, or in case of suspension, to re-start the suspended businesses, including the recovery of important facilities, in the shortest possible time, Advantest formulated and implemented a "Business Continuity Plan." However, if such Business Continuity Plan is not effective, Advantest's core businesses could be disrupted at a time of crisis, such as large-scale natural disasters, and could take a substantial amount of time to recover.

Advantest may not realize the full anticipated benefits of the integration with Verigy

Advantest acquired Verigy in July 2011 and fully integrated with Verigy in April 2012. Advantest believes that the integration with Verigy enables it to better satisfy customer needs through the development and sale of a wider variety of high quality products, and to better address customer needs through technological innovation that is supported by a stable financial base, leading to continued growth amidst a rapidly changing semiconductor market.

However, integrating the business of two different companies is complex, and unifying certain operating processes will require more time. Furthermore, the integration may not realize the anticipated benefits even if operating processes are successfully unified. The difficulties in integrating the two businesses may arise during various stages of the integration, including the following:

- consolidation of the two companies' differing research and development, manufacturing, sales, maintenance processes and their systems;
- the elimination of inefficiencies that may arise out of overlapping departments and processes between the two companies; and
- the integration of two companies with differing corporate cultures and languages.

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If difficulties arise in connection with the integration, including those mentioned above, Advantest's future financial results may be adversely affected.

Advantest has also granted stock options to employees that Advantest took over from Verigy in July 2011. If the employees exercise their stock options on a large scale, voting rights of Advantest's shareholders, total assets per share and share price may be diluted as a result.

Advantest's business is subject to economic, political and other risks associated with international operations and sales

Advantest's business is subject to risks associated with conducting business internationally because it manufactures and sells its products, and purchases parts and components from, around the world. In fiscal 2013, 73.0% of Advantest's total net sales came from Asia (excluding Japan), a majority of which consisted of sales in Taiwan, the People's Republic of China ("China") and Korea, 9.6% from the Americas and 6.5% from Europe. Advantest anticipates that net sales from international operations will continue to represent a substantial portion of its total net sales. In addition, some of Advantest's distribution and support subsidiaries are located in the Americas, Europe, and Asian countries, including Taiwan, Singapore, Korea and China, and some of Advantest's suppliers and factories are also located overseas, such as Korea and Malaysia. Accordingly, Advantest's future results could be harmed by a variety of factors, including:

- political and economic instability, including economic and political disruptions, disputes, natural calamities, epidemics or other risks related to countries where Advantest procures its components and parts or manufactures and sells its products;
- trade protection measures and import or export licensing requirements;
- potentially negative consequences from changes in tax laws;
- risks with respect to international taxation, including transfer pricing regulations;
- difficulty in staffing and managing widespread operations;
- differing protection of intellectual property;
- difficulties in collecting accounts receivable because of distance and different legal rules;
- risks with respect to social and political crises and issues resulting from terrorism, war and deterioration in the political and/or economic relationships between Japan and other countries, among others; and
- risks with respect to decline in the quality of procurement and manufacturing where Advantest's suppliers or manufacturing facilities are located in countries that do not have developed infrastructures in mechanical processing and assembly.

Advantest recorded a significant amount of goodwill and other long-lived assets which may become impaired in the future

Advantest may be required to record an impairment charge for the difference between the carrying amount of long-lived assets and the implied fair value of long-lived assets if circumstances indicate that impairment may have occurred and the carrying amount of the assets may not be recoverable.

In fiscal 2013, Advantest took into account its changing business environment and reconsidered its future expected cash flows. As a result, it recognized impairment losses relating to property, plant and equipment and intangible fixed assets in the amount of ¥13,495 million.

Advantest has recorded a significant amount of goodwill on its consolidated balance sheet in accordance with U.S. GAAP and goodwill is tested for impairment at least annually. If the testing performed indicates that

the carrying amount of reporting unit goodwill exceeds, the implied fair value of that goodwill, Advantest recalculates the fair value of each reporting unit goodwill and an impairment loss shall be recognized in an amount equal to that excess. Therefore, depending on the expected future cash flow of long-lived assets or business operations to which goodwill relates, Advantest may be required to record a significant impairment charge, which could have a material adverse effect on Advantest's financial condition and results of operations.

Advantest may not be able to recover its capital expenditures

Advantest continues to make capital expenditures. From fiscal 2012 through fiscal 2013, Advantest built a new factory in South Korea in order to increase its share of sales to major Korean customers. The factory began operating in May 2013. Advantest may not be able to recover the capital expenditures for such projects within the assumed timeframe, or at all, if it cannot achieve the assumed volume of sales due to customers cutting back on capital expenditures or if intense competition with competitors results in a reduction in unit prices. In such event, the asset would be subject to impairment, which may have an adverse impact on Advantest's profitability.

If a natural disaster comparable to the Great East Japan Earthquake were to occur, Advantest's business may suffer

If a natural disaster comparable to the Great East Japan Earthquake, which struck on March 11, 2011, were to occur, resulting in suppliers' facilities being destroyed, the supply of public utilities such as electricity, gas, and water to suppliers' facilities being cut, or there is a shortage of necessary energy supply for domestic industry, Advantest may not be able to procure necessary components or parts, and may be unable to meet market demand for the supply of its products. Furthermore, market trends for the semiconductor industry, and finished products that are closely related to semiconductors, such as household electrical appliances, various computer equipment and automobiles, may become uncertain. Advantest's business may be adversely affected as a result of these factors.

If a large quantity of radioactive material is released as a result of substantial damage to a nuclear power plant caused by an aftershock or a tsunami similar to the accident that occurred at the Fukushima Daiichi Nuclear Power Station, and Advantest's products are contaminated with radioactive substances, the radiation levels where Advantest's major production facilities are located exceed national radiation standards, or electricity supply becomes unstable for long periods of time due to a shut-down of nuclear plants, Advantest may be unable to meet market demand for the supply of its products, or the competitiveness of its products may be impaired and Advantest's business may be adversely affected.

Advantest's business may be negatively affected by factors relating to its marketing and sales capabilities and its branding

Advantest's business may be negatively affected by factors relating to its marketing and sales capabilities and its branding, including:

- the long selling process involved in the sale of semiconductor and component test systems and mechatronics system;
- the relatively small number of total units sold in the semiconductor and component test system and mechatronics system market;
- order cancellations or postponement of capital expenditures by customers;
- delays in collection of accounts receivable, increases in losses resulting from bad debt or increases in provisions for doubtful receivables, reflecting the financial condition of customers;
- increases in required provisions for product warranty costs and write-downs of inventory; and
- any real or perceived decrease in performance and reliability of Advantest products, which could lead to a decline in Advantest's reputation.

Chemicals used by Advantest may become subject to more stringent regulations, and Advantest may be required to incur significant costs in adapting to new requirements

Advantest uses chemicals in the manufacturing of its products, the manufacture, processing and distribution of which are subject to environmental related laws, regulations and rules of Japanese governmental agencies, as well as by various industry organizations and other regulatory bodies in other countries. These regulatory bodies may strengthen existing regulations governing chemicals used by Advantest and may also begin to regulate other chemicals used by Advantest. While Advantest is taking measures to eliminate toxic substances included in parts used to manufacture its products, Advantest uses solder, which contains lead for mounting electronic parts and components for its products, in order to ensure the reliability of its products as a matter of priority. Further, as a method to cool some of its semiconductor and component test systems and mechatronics systems, Advantest uses fluorinated liquid which use is not currently regulated by laws. Advantest believes that it is in compliance with regulations with respect to the use of chemicals by promoting environmental policies for its products with the focus on ensuring the safety and the reliability of its products; however, Advantest must be prepared to adapt to regulatory requirements in all relevant countries as requirements change. Advantest may be required to incur significant cost in adapting to new requirements. Any failure by Advantest to comply with applicable government or industry regulations could result in restrictions on its ability to carry on with or expand sales of its products.

Advantest could suffer significant liabilities, litigation costs or licensing expenses or be prevented from selling its products if it is infringing the intellectual property of third parties

Advantest may be unknowingly infringing the intellectual property rights of third parties and may be held responsible for that infringement. To date, Advantest has not been the subject of a material intellectual property claim. However, any future litigation regarding patents or other intellectual property infringement could be costly and time consuming and divert management and key personnel from Advantest's business operations. If Advantest loses a claim, it may be forced to pay significant damages, pay license fees, modify its products or processes, stop making products or stop using processes. A license could be very expensive to obtain or may not be available at all. Changing Advantest's products or processes to avoid infringing the rights of third parties may be costly or impractical.

Advantest may be unable to protect its proprietary rights due to the difficulty of Advantest gaining access to, and investigating, the products believed to infringe Advantest's intellectual property rights

Advantest relies on patents, utility model rights, design rights, trademarks and copyrights obtained in various countries to actively protect its proprietary rights. For instance, with respect to the device interface market, Advantest has taken legal action based on its patent and utility model rights against manufacturers that sell replicas of Advantest's products and, in some instances, has obtained injunctions against sales of such replicas. However, in general, it is difficult for Advantest to gain access to, and investigate, the products believed to infringe its intellectual property rights. Therefore, Advantest cannot ensure that its intellectual property rights will provide meaningful protection of its proprietary rights. Nevertheless, Advantest is focused on protecting its intellectual property rights from third party infringement and will continue to monitor and enforce its rights.

The technology labor market is very competitive, and Advantest's business may suffer if Advantest is unable to hire and retain engineers and other key personnel

Advantest's future success depends partly on its ability to attract and retain highly qualified engineers for its research and development and customer service and support divisions. If Advantest fails to hire and retain a sufficient number of these personnel, it may not be able to maintain and expand its business. Advantest may need to revise its compensation and other personnel related policies to retain its existing officers and employees and attract and retain the additional personnel that it expects to require.

Damage, interference or interruption to Advantest's information technology networks and systems could hinder business continuity and lead to substantial costs or harm Advantest's reputation

Advantest relies on various information technology networks and systems, some of which are managed by third parties, to process, transmit and store electronic information, including confidential data, and to carry out and support a variety of business activities, including manufacturing, research and development, supply chain management, sales and accounting. Advantest has the Information Security Committee and Legal and General Affairs Department to create policies on information security measures. The IT section builds and operates the information and technology network and system based on the above-mentioned policies. However, attacks by hackers or computer viruses, wrongful use of the information security system, careless use, accidents or disasters could undermine the defenses established by Advantest and disrupt business continuity, which could not only risk leakage or tampering of information but could also result in a legal claim, litigation, damages liability or an obligation to pay fines. If this were to occur, Advantest's reputation could be harmed, Advantest could incur substantial costs, and it may have a material adverse effect upon Advantest's financial condition and results of operation.

Product defects and any damages stemming from Advantest's product liability could harm Advantest's reputation among existing and potential customers and could have a material adverse effect upon Advantest's business results and financial condition

Advantest manufactures its products in accordance with internationally accepted quality control standards such as ISO 9000. However, Advantest cannot guarantee that there are no defects in its products. Advantest maintains product liability insurance, but cannot guarantee that such insurance will sufficiently cover the ultimate amount of damages with respect to Advantest's liabilities. Large scale accidents due to product defects or any discovery of defects in its products could harm Advantest's reputation for not adequately addressing defects, could cause Advantest to incur higher costs, could result in claims for damages and could have a material adverse effect upon Advantest's business results and financial condition.

Risks Related to Ownership of American Depositary Shares ("ADSs") or Common Stock

Japanese yen-dollar fluctuations could cause the market price of the ADSs to decline and reduce dividend amounts payable to ADS holders as expressed in U.S. dollars

Fluctuations in the exchange rate between the Japanese yen and the U.S. dollar may affect the U.S. dollar equivalent of the Japanese yen price of the shares on the Tokyo Stock Exchange and, primarily reflecting the foregoing, are likely to affect the market price of the ADSs. The Company has historically paid dividends on its shares twice a year. If the Company declares cash dividends, dividends on the shares represented by the ADSs will be paid to the depositary in Japanese yen and then converted by the depositary into U.S. dollars. Therefore, exchange rate fluctuations could also affect the dividend amounts payable to ADS holders following conversion into U.S. dollars of dividends paid in Japanese yen on the shares represented by the ADSs.

A holder of ADSs has fewer rights than a shareholder has, and must act through the depositary to exercise those rights

The rights of shareholders under Japanese law to take actions, including voting their shares, receiving dividends and distributions, bringing derivative actions, examining Advantest's accounting books and records and exercising appraisal rights, are available only to holders of record on the Company's register of shareholders. Because the depositary, through its custodian agents, is the registered holder of the shares underlying the ADSs, only the depositary can exercise those rights in connection with the deposited shares. The depositary will make efforts to vote the shares underlying a holder's ADSs as instructed by the holder and will pay to the holder the dividends and distributions collected from Advantest. However, in the holder's capacity as an ADS holder, that holder will not be able to bring a derivative action, examine Advantest's accounting books and records or exercise appraisal rights through the depositary.

There are restrictions on the withdrawal of shares from the Company's depositary receipt facility

Under the Company's ADS program, each ADS represents the right to receive one share. To withdraw any shares, a holder of ADSs has to surrender for cancellation American Depositary Receipts, or ADRs, evidencing 100 ADSs or any integral multiple thereof. Each ADR bears a legend to that effect. As a result, holders of ADSs are unable to withdraw fractions of shares or units or receive any cash settlement from the depositary in lieu of withdrawal of fractions of shares or units. Holders of shares representing less than one unit, or 100 shares, may require the Company to repurchase those shares, whereas holders of ADSs representing less than one unit of shares are unable to exercise this right because the holders of these ADSs are unable to withdraw the underlying shares. Under the Company's ADS program, an ADS holder cannot cause the depositary to require the Company to repurchase fractions of shares or units on its behalf. For a further discussion of the ADSs and the ADS program, see "Description of American Depositary Receipts" set forth in the Company's registration statement on Form F-1 filed with the Securities and Exchange Commission on July 22, 2002. For a further discussion of the Japanese unit share system, see "Additional Information-Memorandum and Articles of Association-The Unit Share System."

Enforcement of Civil Liabilities

The Company is a limited liability, joint-stock corporation incorporated under the laws of Japan. Almost all of the Company's directors, executive officers and audit & supervisory board members reside in Japan. Substantially all of the Company's assets and the assets of these persons are located in Japan. It may not be possible, therefore, for investors to effect service of process within the U.S. upon the Company or these persons or to enforce against the Company or these persons judgments obtained in U.S. courts predicated upon the civil liability provisions of the federal securities laws of the U.S. The Company's Japanese counsel, Nagashima Ohno & Tsunematsu, has advised the Company that there is doubt as to the enforceability in Japan, in original actions or in actions for enforcement of judgments of U.S. courts, of liabilities predicated solely upon the federal securities laws of the U.S.

ITEM 4. INFORMATION ON THE COMPANY

4.A. HISTORY AND DEVELOPMENT OF THE COMPANY

The Company commenced operations in July 1954, and was incorporated in December 1954 under the name Takeda Riken Industry Co., Ltd. as a limited liability, joint-stock company in Japan under the Commercial Code of Japan. At the time of incorporation, Takeda Riken's primary business was the design, manufacture and sale of measuring instruments for Japanese electronics manufacturers. Takeda Riken started focusing on semiconductor test equipment for the semiconductor industry in 1968 and was the first to domestically produce semiconductor test equipment in 1972. In 1971, Takeda Riken entered into its first distribution agreement with a foreign distributor and, in 1973, established its first representative office in the U.S. to gather information on technology and distribution and to establish dealer relationships. These two milestones launched the Company's long-term goal of becoming a global manufacturer of testing and measuring products. Takeda Riken has been listed on the Tokyo Stock Exchange since February 1983. Takeda Riken changed its registered name to Kabushiki Kaisha Advantest in October 1985.

Advantest applies its capital expenditures chiefly to developing new products, streamlining production, expanding its production capacity and capital leases to its customers. Advantest's capital expenditures were ¥7.0 billion, ¥12.6 billion and ¥5.6 billion in fiscal 2011, 2012 and 2013, respectively. The fiscal 2012 amount includes capital expenditures to build the new factory in Korea.

On July 4, 2011, Advantest acquired all of the outstanding shares of common stock of Verigy at US\$ 15.00 per share, pursuant to which Verigy became a wholly-owned subsidiary of Advantest. The total purchase price was ¥78.7 billion. In April 2012, Advantest reorganized its subsidiaries and fully integrated with Verigy.