Producers or Distributors of Films" issued by the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants ("AcSEC"). As a result, Sony's operating income, income before income taxes, and net income for the fiscal year ended March 31, 2001 each decreased by approximately 28.5 billion yen. Additionally, Sony's net income for the fiscal year ended March 31, 2001 decreased by approximately 101.7 billion yen, reflecting a one-time non-cash after-tax cumulative effect adjustment in the income statement directly above the caption of "net income" for a change in accounting principle.

3. As a result of the adoption of SOP 00-2, film costs related to theatrical and television product at prior year-ends, which were previously recorded in inventories in accordance with Statement of Financial Accounting Standards No. 53, have been reclassified to film costs which are included in non-current assets. Also as a result, net working capital figures at all prior year-ends have been restated to conform to the presentation at March 31, 2001.

4. Effective as of April 1, 2000, Sony adopted Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements", issued by the U.S. Securities and Exchange Commission. As a result, a one-time non-cash after-tax cumulative effect adjustment of approximately 2.8 billion yen was recorded in the income statement directly above the caption of "net income" for a change in accounting principle. The accounting change did not have a material effect on Sony's consolidated financial results.

5. Effective with the fiscal year ended March 31, 2001, net loss on sale, disposal or impairment of long-lived assets, which was previously included in other income and expense and shown below operating income, is included in selling, general and administrative expense and shown above operating income. As a result, operating income for all prior years has been restated to conform to the presentation for the fiscal year ended March 31, 2001.

6. Income before income taxes and net income figures for the fiscal year ended March 31, 1999 included gains of approximately 58.7 billion yen and approximately 30.7 billion yen, respectively, which resulted from a contribution of securities to an outside trust for employee retirement benefit purposes. Income before income taxes and net income figures for the fiscal year ended March 31, 2001 included gains of approximately 11.1 billion yen and approximately 6.4 billion yen, respectively, which resulted from a contribution of securities to an outside trust for employee retirement benefit purposes.

Risk Factors

This section contains forward-looking statements that are subject to the Cautionary Statement Regarding Forward-Looking Statements appearing elsewhere in this annual report. Risks to Sony are also discussed elsewhere in this annual report, including without limitation in the other sections of the annual report referred to in the "Cautionary Statement with Respect to Forward-Looking Statements."

Economic Trends in Sony's Major Markets May Adversely Affect Sony's Sales.

Purchases of Sony's products are to a very significant extent discretionary. Economic downturns and declines in consumption in Sony's major markets, including Japan, the U.S., Europe, and Asia/ Latin America may thus adversely affect the level of sales and Sony's consolidated financial results and condition.

Foreign Exchange Fluctuations Can Affect Sony's Reported Results Because of Translation of Results into Yen and Because Sales and Expenses in Different Currencies Can Affect Results. Hedging Is Not Fully Effective against These Factors.

Local currency denominated financial results in each of Sony's subsidiaries around the world are translated into yen by applying the average market rate during each financial period and recorded on Sony's consolidated profit and loss statement. Local currency-denominated assets and liabilities/ stockholder's equity are translated into yen by applying the market rate at the end of each financial period and recorded on Sony's consolidated balance sheets. Accordingly, the results, assets, and liabilities/ stockholder's equity in such worldwide businesses as Electronics, Game, Music, and Pictures are subject to foreign exchange fluctuations. In recent periods, operating results reported in yen in accordance with U.S. GAAP have generally been less favorable than those results in local currency.

In addition, especially in the Electronics and Game businesses, operating profits and losses are highly sensitive to the yen's appreciation because the research and development/ production activities and headquarter functions are concentrated in Japan so that the ratio of yen-denominated costs to total costs is higher than in other business segments. Profits and losses resulting from differences between hedged rates and market rates in the evaluation or execution of contracts entered for the purpose of currency hedging such as foreign exchange forward contracts and foreign currency option contracts by Sony Corporation and its subsidiaries such as Aiwa Co., Ltd., Sony Computer Entertainment Inc., and finance subsidiaries in the U.S., Europe, and Asia are recorded on a net basis in other income and expenses, and are not included in operating profits and losses. Although Sony engages in hedging transactions for actual requirements to minimize the negative effects from short-term fluctuations of foreign exchange rates among major invoicing currencies such as the U.S. dollar, euro and yen, mid-to-long-term volatile changes of the exchange rate levels make it difficult for Sony to execute planned procurement, production, logistics, and sales activities and may adversely affect Sony’s consolidated financial results and condition.

Stock Price Fluctuations Affect Sony’s Results Because of the Accounting Treatment of Its Stock-Linked Incentive Compensation Programs.

Sony has adopted stock-price linked incentive compensation programs for selected management employees, and such compensation costs are recognized in income based on the excess, if any, of the quoted market price of Sony Corporation’s stock at the grant date of the award or other measurement date over the stated exercise price of the award. Accordingly, a rise in the stock price of Sony Corporation may adversely affect Sony’s consolidated financial results and condition.

Sony Depends on Scarce Skilled Personnel for Its Continued Success in Designing, Developing and Introducing New Products and in Managing These Processes.

Continued technological superiority of Sony’s products and services is a critical element of Sony’s competitive success. An increasingly important factor in Sony’s competitiveness is the continuing performance of skilled managerial and technical personnel. Experienced personnel in the industries in which Sony competes are in high demand, and competition for their talents is intense. There can be no assurance that Sony will be successful in attracting and retaining the key personnel it needs, and the expenses in obtaining and retaining these personnel are expected to increase.

The Cooperation and Alliances with, and Strategic Investments in, Third Parties Undertaken by Sony May Not Produce Successful Results.

Sony carries out many activities with other companies such as alliances, joint ventures, and strategic investments, including investments in venture companies. Sony’s reliance on these strategies of partnering with third parties is increasing. These activities are important for Sony to introduce new products such as information and communication equipment, for which demand is increasing, and to introduce new services using digital network technologies. In addition, Sony may carry out a large amount of strategic investment in other entities in order to proceed with broadband network businesses in the future. However, because results from these activities are largely dependent on business trends as well as the financial condition of partner companies, weak trends or disappointing performance of such partners may adversely affect the success of these activities. In addition, the success of these activities may be adversely affected by the inability of Sony and its partners successfully to define and reach their common objectives. Although Sony strives to avoid business duplication among its group subsidiaries, by entering into alliances, joint ventures, and strategic investments which are designed to improve the corporate value of the Sony group by diversifying the businesses of its subsidiaries, business overlaps and inefficiencies may arise.

Reorganization of Businesses and Involvement of External Suppliers May Increase Financial, Reputational and Other Risks to Sony.

In order to properly allocate managerial resources and improve operating efficiency, Sony is undertaking the concentration/selection of its businesses, realignment of its facilities, and reduction in the number of its employees around the world. In connection with these actions, it is possible that there may be reorganization expenses which adversely affect Sony’s consolidated financial results and condition. Moreover, the intended beneficial effects from such reorganizations may not be achieved.

In addition, with the increasing necessity of pursuing quick business development and operating efficiency with limited managerial resources, Sony increasingly procures important technologies from external suppliers. Sony also increasingly consigns to external suppliers extensive activities including procurement, manufacturing, logistics, sales, and services, and procures from external suppliers infrastructures such as fixed assets and communications. Accordingly, Sony’s reliance on such external suppliers, including from strategic alliances or joint ventures, is increasing. Reliance on outside sources increases the chances that Sony cannot control or avoid the introduction of products incorporating defective or inferior third party technology or components, which can adversely affect Sony’s consolidated financial results and condition or its reputation for quality products. This reliance on third parties may also raise issues caused by suppliers’ insufficient compliance with applicable regulation or third-party intellectual property rights.

In Each of Its Businesses, Sony Is Subject to Intense Competitive Pressures, Including in Terms of Price, Technological Change, Product Development and Quality. Sony Must Also Successfully Compete in This Environment to Maintain Sales Necessary to Fund Research and Development, Capital Expenditures and Other Expenses That Are Necessary to Maintain Product and Technological Leadership.

Sony’s businesses face a broad range of competitors from large international companies to an increasing number of relatively small, rapidly growing, and highly specialized organizations. Sony has a portfolio of businesses in different industries while many of its competitors specialize in one or more of these business areas. As a result, Sony may not fund or invest in certain of its businesses to the same degree that its competitors do and these companies may have greater financial, technical, and marketing resources available to them than the businesses of Sony against which they compete.

Electronics Business

In the Electronics business, the environment is becoming more demanding due to a number of factors, including the following:

- an increase in the number of new market entrants that have new technologies,
- intensifying competition in the industry,
- rapid technological progress,
- oversupply of digital products such as PCs, which account for a growing proportion of Sony’s business, and of electronic devices such as semiconductors,
- a rise in the market penetration ratios of products, and
- global price erosion from such trends as the deregulation of export and import regimes and the establishment of new sales channels such as the Internet.

Sony continues to incur significant expenses, including depreciation expenses resulting from a high level of capital expenditures for critical devices including semiconductors, high levels of research and development expenses for development of digital equipment that requires new technologies and of basic technologies, royalty expenses to acquire technologies indispensable for the development and production of information and communication equipment, advertising expenses, and personnel expenses. However, Sony may face difficulties in adequately providing for such expenses and capital expenditures due to weak sales caused by such factors as a lack of products and services that appeal to customers, decreases in unit sales stemming from either a rise in the market penetration ratios of products or from increases in sales prices in response to volatile fluctuations of exchange rates, or supply shortages of core devices/other parts and inventory shortages of products, especially when product demand is the highest. Moreover, such factors as reductions in production/inventories in response to weak sales in certain areas or product categories may adversely affect Sony’s consolidated financial results and condition. Furthermore, regarding Aiwa Co., Ltd., an approximately 51 percent owned consolidated subsidiary of Sony Corporation, reorganization expenses, such as severance expenses and loss on sale and disposal of long-lived assets, relating to execution of the realignment of businesses which was announced in March 2001, will adversely affect Sony’s consolidated financial results and condition.

Game Business

In the Game business, the competitive environment is becoming more difficult due to competitors’ introduction of new hardware and software with various formats that can have increasing appeal to customers, rapid technological progress, a rise in the market penetration ratios of products, and diversification of customers’ preferences. Sony continues to incur significant expenses such as depreciation expenses resulting from a high level of capital expenditures to increase production of semiconductors for PlayStation 2 hardware, research and development expenses for semiconductors and software, advertising expenses, and personnel expenses. However, Sony may face difficulties in adequately providing for such expenses and capital expenditures due to weak sales caused by such factors as supply shortages of core devices/ other parts and inventory shortages of hardware, especially when product demand is the highest, delays in introductions or decreases in the number of software titles that appeal to customers, or decreases in hardware unit sales stemming from a rise in the market penetration ratios of products. Moreover, delays in either increasing the production of semiconductors for PlayStation 2 hardware or cost reductions and reductions in production/ inventories, in response to a changeover to new hardware or slow sales, may adversely affect Sony’s consolidated financial results and condition.

Music Business

In the Music business, the market growth rate has slowed worldwide due to the saturation of the CD market, the effects of piracy and other illegal duplication, parallel imports, diversification of customer preferences, and pricing pressures. In addition, a trend of increasing expenses for advertising and promotion as well as lower sales of previously released catalog due to the maturing of the CD configuration have made it more difficult for Sony to maintain profit margins. The Music business is highly dependent on establishing artists that appeal to customers, and the competition among record companies for such talent is intense. Therefore, if the Music business is unable to find and establish new talented artists, it may adversely affect Sony’s consolidated financial results and condition. Furthermore, advancements in technologies which allow for the transfer and downloading of digital music files from the Internet without authorization from rights owners may threaten the conventional copyright-based business model and may adversely affect Sony’s Music business.

Corresponding to this change in the business model, expenses to develop new services, which combine digital network technologies and music content, and other strategic investments may also adversely affect Sony's near-term consolidated financial results and condition.

Pictures Business

The Pictures business is a highly competitive business, as companies compete with each other as well as with other forms of entertainment and leisure-time activities, including video games, the Internet and other computer-related activities for viewers' attention. In the Motion Pictures business, major motion picture studios and independent film production companies are aggressively competing in the production and distribution of films all over the world. In this environment, higher expenses are generally required for production, talent, and distribution of films. Although Sony is working to hold down production costs for certain films by collaborating with and purchasing product from other studios, sales of such product may not adequately provide for such costs due to factors such as a lack of acceptance by customers or varying customer preferences.

The Pictures business may be directly or indirectly dependent upon union members, and work stoppages or strikes organized by such unions could materially adversely impact Sony's business or financial results and condition. The collective bargaining agreement with the Screen Actors Guild ("SAG") expires on June 30, 2001. Negotiations to renew that agreement are underway, but many significant issues remain unresolved. If a new agreement cannot be reached, a strike may result which, depending on the length of time involved, could slow down film and television production, impact future planned product releases and increase idle capacity in Sony's production facilities.

In addition, due to the new film accounting standard which Sony adopted in April 2000, certain expenses such as marketing and distribution, which were previously deferred and amortized over the life of the film or television product, are now expensed as incurred. The impact of this new standard is that losses are generally recorded for films, even those that are successful, during the initial theatrical release period, deferring the recognition of profits until later periods.

In the Television production and distribution business, available network broadcast time is limited and the audience is increasingly fragmented among the major broadcast networks, cable, and independent television stations. Competition to obtain customers between major networks and other production and distribution companies is becoming more intense. Furthermore, broadcast networks are increasingly producing their own shows internally. This competitive environment has resulted in a quicker turnover of shows. As a result, Sony, as well as other participants in the industry, has seen an increase in the

number of new programs being distributed, which are generally less profitable, and a decrease in the number of programs that are able to achieve syndication, which are generally more profitable. In addition, Sony and other members of the industry have seen significant increases in talent spending. Such developments may adversely affect Sony's consolidated financial results and condition. Furthermore, expenses to develop new services which combine digital network technologies and movies/ television programs and other strategic investments may adversely affect Sony's consolidated financial results and condition.

Insurance Business

In the Insurance business, with deregulation of the industry in Japan, the number of new market entrants from outside Japan and from other industries is increasing. Also, customers are becoming more exacting in regards to product selection and prices. In this environment, if Sony's life insurance business cannot provide products and services that fit customers' needs and achieve stable investment returns from its stock, bond, and real estate assets, Sony's consolidated financial results and condition may be adversely affected. Moreover, increases in insurance claims that Sony cannot accurately predict and shifts in customers' demand from such profitable products as life guarantees to such less profitable products as annuities may adversely affect Sony's consolidated financial results and condition. Moreover, due to competitors' successive bankruptcies, increases in the amount of mandatorily contributed reserves for the Life Insurance Policyholders Protection Corporation of Japan may adversely affect Sony's consolidated financial results and condition. In the non-life insurance business, revenues have not yet been sufficient to cover such expenses as advertising expenses necessary for business expansion, and increases in insurance claims that Sony cannot accurately predict may adversely affect Sony's consolidated financial results and condition.

Other Business

In the leasing and credit financing business, increases in funds required for purchasing goods to be leased and in leasehold assets, increases in non-performing receivables due to default in payment by customers, and decreases in profitability attributable to intensifying competition may adversely affect Sony's consolidated financial results and condition. In the location-based entertainment businesses, decreases in the number of visitors or in customers' expenditures may adversely affect Sony's consolidated financial results and condition. In the parts trading services business, reductions in the amount of exports and imports due to sluggish operations in the Electronics business may adversely affect Sony's consolidated financial results and condition.

Internet Related Businesses and Other New Businesses

Sony is actively expanding Internet related businesses and other new businesses. Such businesses include Sony Communication Network Corporation, whose main business is as an Internet service provider; bitwallet, Inc., which is developing a prepaid electronic money service; and Sony Bank Inc., which obtained a banking license in April 2001 from the Financial Services Agency in Japan and started operation in June 2001. These businesses operate in competitive markets characterized by rapid advancements in technology and competition with existing large companies/new market entrants. In this environment, Sony's consolidated financial results and condition may be adversely affected as a result of the substantial expenditures that are required to compete and that may exceed revenues. In addition, if these businesses fail to attract customers due to delays in expansion of Internet subscribers or customers' anxieties in terms of security, these businesses may be forced to change their business models.

Equity Affiliates

In recent years, Sony has recorded substantial losses and writedowns in some of its equity affiliates. These losses and writedowns have included those at Loews Cineplex Entertainment Corporation ("Loews"), including a total writedown due to Loews' bankruptcy, and at The Columbia House Company ("CHC"). Similar losses and writedowns may occur in the future. In addition, equity affiliates include newly established businesses in which expenses may exceed revenues.

Sony Is Subject to Increasing Financial and Reputational Risks Due to Product Quality/ Liability Issues.

Corresponding to rapid advancements in technologies and increases in demand for digital equipment, such technologies as software and electronic devices including semiconductors, that are utilized in products and services Sony introduces in the market, are becoming increasingly sophisticated and complicated. At the same time, since the technological life cycle is becoming shorter, Sony is required to introduce products and services in a shorter period of time. These factors apply particularly to Sony because of the importance to it of technological and product leadership as a feature of its competitive success. Accordingly, product quality/liability issues present greater risks. Sony endeavors to prevent the occurrence of such issues in advance by incorporating such measures as the Six Sigma method for improving management quality. Further, in order to minimize damages generated from any product quality/liability issues, Sony is seeking to develop a risk management structure designed to allow Sony group headquarters and each business unit to closely cooperate and to enable prompt awareness of the situation and appropriate execution of countermeasures. However, there is no assurance that Sony will be able to completely eliminate or mitigate occurrences of the aforementioned issues and consequent damages. If such factors adversely affect Sony's operating activities, generate expenses such as those for product recalls, service, and compensation, or hurt Sony's brand image, Sony's consolidated financial results and condition or reputation for quality products may be adversely affected.

Sony Is Subject to the Risks of International Operations.

A substantial portion of Sony's activity is conducted outside Japan, including in developing and emerging markets in Latin American and Asia. There are a number of risks inherent in doing business in those markets, including the following:

- less developed technological infrastructure, which can affect our production or other activities or result in lower customer acceptance of our services;
- unfavorable political or economic factors;
- unexpected legal or regulatory changes;
- difficulties in recruiting and retaining personnel, and managing international operations;
- fluctuations in currency exchange rates;
- reduced protection for intellectual property rights; and
- potentially adverse tax consequences.

Our inability to manage successfully the risks inherent in our international activities could adversely affect our business, financial condition and operating results.

Sony's Physical Facilities and Information Systems and Securities Are Subject to Damage as a Result of Disasters, Outages or Similar Events.

Sony's group headquarters functions, part of Sony's major data centers, and many of Sony's most advanced device manufacturing facilities, including those for semiconductors, are located in Japan, where the possibility of disaster or damage from earthquake is generally higher than in other parts of the world. In addition, Sony's facilities or offices, including those for research and development, material procurement, manufacturing, logistics, sales, and services are located throughout the world and subject to the possibility of disaster or outage or similar disruption as a result of any of a number of events. Sony periodically carries out disaster prevention checks, facility maintenance, and safety measures to minimize possible negative effects caused by such disasters as earthquakes, water, fire, electricity failure, or accidents to its operating activities, major facilities, and employees'/ customers' health. Furthermore, as the role of information systems is becoming ever more important in Sony's operating activities, such issues as shutdowns of information systems due to the aforementioned disasters, software/ hardware defects, and computer viruses, as well as leakage, falsifications, and disappearances of internal databases, including information of customers or vendors, pose increasing risks. Although Sony is working to establish appropriate backup structures for information systems and databases, advanced levels of security, and employee education, there is no assurance that Sony will be able to completely prevent or mitigate the effect of such issues as the aforementioned disasters, outflows of harmful substances, shutdowns of information systems, and leakage, falsifications, and disappearances of internal databases. If such factors adversely affect Sony's operating activities, generate expenses relating to physical or personal damage, or hurt Sony's brand image, Sony's consolidated financial results and condition may be adversely affected.

Sony Is Subject to Government Regulation That Can Limit Its Activities or Increase Costs of Operations.

Various regulations by governments in countries in which Sony does businesses, such as required business/ investment approvals, export regulations based on national-security or other reasons and other export/ import regulations such as tariffs, as well as commercial, antitrust, patent, consumer and business taxation, exchange control, and environment/ recycling laws and regulations, apply to Sony. If Sony is unable to comply with these regulations, they can serve to limit Sony's activities. In addition, even if Sony is able to comply, these regulations can result in increased costs. In either event, Sony's consolidated financial results and financial condition may be adversely affected.

In the case of environmental issues, Sony aggressively endeavors to carry out decreases in the amount of waste materials, reductions in the use of harmful substances, and comprehensive risk management in manufacturing activities, as well as in final products, the use of lead-free soldering, decreases in the level of standby power, and the recycling of products and packaging materials. Nonetheless, there can be no assurance that Sony can comply in all cases with environmental regulations, and environmental regulation and the effects on Sony can adversely affect its consolidated financial results and condition.

Sony Can Be Adversely Affected by Its Employee Benefit Obligations.

Regarding benefit obligations and plan assets, Sony funds and accrues the cost of benefits to the sufficient level based on conservative accounting policies. However, if returns from investment assets decrease due to conditions in, for example, stock or bond markets, additional funding and accruals may be required, and such funding and accruals may adversely affect Sony's consolidated financial results and condition.

Compliance with Changes in Accounting Requirements Can Adversely Affect Sony's Reported Results and Condition.

Compliance by Sony effective April 1, 2000 with the new motion picture accounting standard had a very significant one-time non-cash impact on net income for the fiscal year ended March 31, 2001, of approximately 101.7 billion yen. Compliance with this standard also had an approximately 28.7 billion yen non-cash impact on operating income, income before income taxes and net income for the same fiscal year. Compliance with this standard will also impact reported operating results in future years.

On April 1, 2001, Sony adopted new accounting standards establishing accounting and reporting standards for derivative instruments. The standards require an entity to recognize all derivatives as either assets or liabilities in the balance sheet and to measure those instruments at fair value. Additionally, the fair value adjustments will affect either stockholders' equity or net income depending on whether the derivative instrument qualifies as a hedge for accounting purposes and, if so, the nature of the hedging activity. On April 1, 2001, upon the adoption of the new standard, Sony recorded an unrealized gain of approximately 1.1 billion yen in accumulated other comprehensive income in the consolidated balance sheet and an after-tax gain of approximately 6.0 billion yen as the cumulative effect of an accounting change in the consolidated statements of income for the fiscal year ending March 31, 2002.

Changes in accounting standards that may be promulgated in the future cannot be predicted and may have a material adverse effect on Sony's reported consolidated financial results and condition.

Item 4. Information on the Company

History and Development of the Company