Risk Information

ITOCHU is exposed to various risks such as market risks, credit risks and investment risks, due to the nature of a wide range of their business. These risks include unpredictable uncertainty and may have significant effects on their future business and financial performance. ITOCHU has enhanced their risk management policy and risk management methodology to monitor and manage these risks, but it is impossible to completely avoid all these risks.

With respect to descriptions about future event, ITOCHU appropriately determines its assumption and estimates based on information at the end of fiscal year 2005.

(1) Corporate Result Risks Due to Macroeconomic Factors

ITOCHU involves a wide variety of business ranging from supply of raw materials to manufacturing and sale in each of their business areas. ITOCHU conducts diverse types of commercial transactions such as purchase and sale of products in the domestic market as well as import/export trade between overseas affiliates. Changes in the domestic economy and fluctuations in world economic environments can seriously affect ITOCHU's results of operations.

To give an overview of ITOCHU's main areas of business, the domestic economy has a relatively strong influence on a consumer and retail-related segment such as textiles and food. Trade in machinery such as plants, autos and industrial machinery, trade in mineral resources, energy and chemical products and investments in development are all largely dependent on economic trends in the U.S. and Asia countries, which take the lead in the world economy. Furthermore, with the steady expansion of demand in China, one of ITOCHU's priority markets, ITOCHU has conducted business and trade in China at a rapid pace for many areas of business. Consequently, Chinese economic trends have a possibility to seriously affect the financial position and results of operations of ITOCHU.

(2) Market Risks

ITOCHU is exposed to market risks such as foreign exchange rate risks, interest rate risks, commodity price risks and stock price risks. ITOCHU attempts to minimize risks related to market fluctuations such as changes in foreign exchange rates and interest rates by establishing risk management policy such as setting and controlling a limit and by utilizing a variety of derivative instruments for hedging purposes. Reference should be made to the accounting policy for derivative instruments in note 2, "Basis of Financial Statements and Summary of Significant Accounting Policies" and note 18, "Financial Instruments" to the consolidated financial statements.

Foreign Exchange Rate Risk

The Company and certain Group companies are exposed to foreign exchange rate risk related to transactions denominated in foreign currencies due to its significant involvement in import/export trading. ITOCHU is working to manage ITOCHU's foreign currency balance by contract amount, debt and liabilities, the amount of ITOCHU's own/other's risk, and short/long-term and set limits on foreign exchange rate risks (limit of balance and that of loss). ITOCHU is also working to minimize foreign exchange rate risks using derivative transactions such as forward exchange contracts and currency swap contracts. However, ITOCHU cannot guarantee a complete avoidance of such foreign exchange rate risks by utilizing derivative instruments.

Since the Company is engaged in businesses involving foreign currencies with a number of overseas trading subsidiaries and other overseas group companies, the figures denominated in Japanese yen on its consolidated balance sheets are also exposed to so-called foreign currency translation risk. This translation risk has no impact on the performance of the business conducted in foreign currencies. In addition, a long period is generally needed to recover the amount of investments. Accordingly, the Company does not hedge the translation risk, as the term of effectiveness provided by hedging is limited.

Interest Rate Risk

ITOCHU is exposed to interest rate risk in both fund raising and in its lending, investing, and operating activities. Interest rate risk refers to the risk of earnings fluctuation caused by changes to interest rates, when mismatches in interest rate sensitivity to assets/liabilities and durations occur. Interest rate risk, on the whole, consists of balance, magnitude of interest rate change, and duration. ITOCHU is working to quantify interest rate risks to control such risks in a concrete and objective manner. To be specific, using the management method Earnings at Risk (EaR), ITOCHU has set a certain limit (Loss Cut Limit) as the highest acceptable interest payment and has executed hedging transactions primarily in the form of interest rate swaps to minimize interest risk. However, ITOCHU still cannot guarantee a complete avoidance of interest rate risk, even having adopted these management methods.

Commodity Price Risk

As a trading company handling a diverse array of commodities, ITOCHU is exposed to commodity price risks due to such factors as market fluctuations. ITOCHU has established a fundamental risk management policy on an individual Division Company basis, assessing purchase contracts, inventories, and sales contracts, etc. and setting and managing a balance limit and loss cut limit for each individual product and conducting periodic reviews. In addition, ITOCHU works to minimize commodity price risk by utilizing derivatives such as futures or forward contracts as means of hedging. Despite these measures, ITOCHU cannot guarantee a complete avoidance of commodity price risks.

ITOCHU as well as certain Group Companies also participate in resource development businesses such as the energy sector and other manufacturing businesses. Production in these businesses is also exposed to the same commodity price risks noted above, and it is possible for the value of the businesses to deteriorate. If this were to occur, it could seriously affect the financial position and results of operations of ITOCHU.

Stock Price Risk

ITOCHU holds available-for-sale securities which are vulnerable to price fluctuation. ITOCHU strives to maintain appropriate levels of investment and to minimize stock price risk by applying exit rules for inefficient investments that ITOCHU has little reason to hold. The fair value of the available-for-sale securities held by the Company and its subsidiaries was ¥190.5 billion ($1,774 million) as of March 31, 2005. However, assuming that the price of these investments fluctuated and the fair value of these available-for-sale marketable securities decreased, it could seriously affect the financial position and results of operations of ITOCHU.