

Corporate Governance

Basic Policies

1. We shall respect the rights of shareholders, and ensure the equal and fair treatment of all shareholders.
2. We shall take the interests of shareholders and other stakeholders into consideration and endeavor to appropriately cooperate with those stakeholders.
3. We shall disclose not only information in compliance with the relevant laws and regulations, but also actively provide important and/or useful information to stakeholders to enable well-informed decision-making.
4. The Board of Directors shall be cognizant of its fiduciary responsibility and accountability to shareholders, and shall appropriately fulfill its roles and responsibilities in order to promote sustainable and stable corporate growth and increase corporate value, profitability and capital efficiency.
5. We shall engage in constructive dialogue with shareholders, and make efforts to obtain their support regarding the Company's Business Policies and also reflect their opinions and concerns in efforts to improve management.

Basic Approach for Regaining Trust

We have established the Corporate Guiding Principles to demonstrate our values regarding appropriate cooperation with stakeholders, respect for their interests, and sound business ethics. We have inculcated these principles and make efforts to ensure that compliance extends to the front lines of business activities in Japan and overseas. For example, we hold briefings on the Corporate Guiding Principles, conduct various types of compliance education, set compliance education as a requirement for promotions, conduct in-person reviews of relevant employees, and ensure that everyone in the Company is aware of the whistle-blowing system. Through these and other venues we have endeavored to broadly instill a sense of urgency among employees by making them keenly aware that the products and services that we supply through our businesses are connected to people's safety, physical wellbeing and financial position, and that they are involved in quality management both directly and indirectly, and that laxity in any aspect of their work could impact society at large. In addition, we have widely communicated our Bad News First reporting system for identifying and resolving issues when they are still minor. It calls for reporting any workplace

abnormalities whether favorable or unfavorable. However, improper acts occurred. As announced on October 16, 2018, performance inspection data records were falsified for some of the seismic isolation/mitigation oil dampers shipped by KYB and a subsidiary. Products that did not conform to performance evaluation standards approved by the Minister of Land, Infrastructure, Transport and Tourism nor met the standards of our customers were installed in buildings. In addition, there were improper claims in connection with a contract with the Ministry of Defense for defense equipment.

To prevent recurrence of the improper acts and demonstrate our commitment to regaining trust, we revised our Corporate Spirit by adding the item "Follow all rules and face all issues with honesty," and, based on the revised Corporate Spirit and basic policy, we will work to strengthen and enhance corporate governance. Having clearly codified the prevention of quality-related misconduct in our Corporate Guiding Principles, we will deeply inculcate these principles in all of our people at the front line of business operations in Japan and overseas, and will resolutely ensure compliance.

Overview of the Corporate Governance System

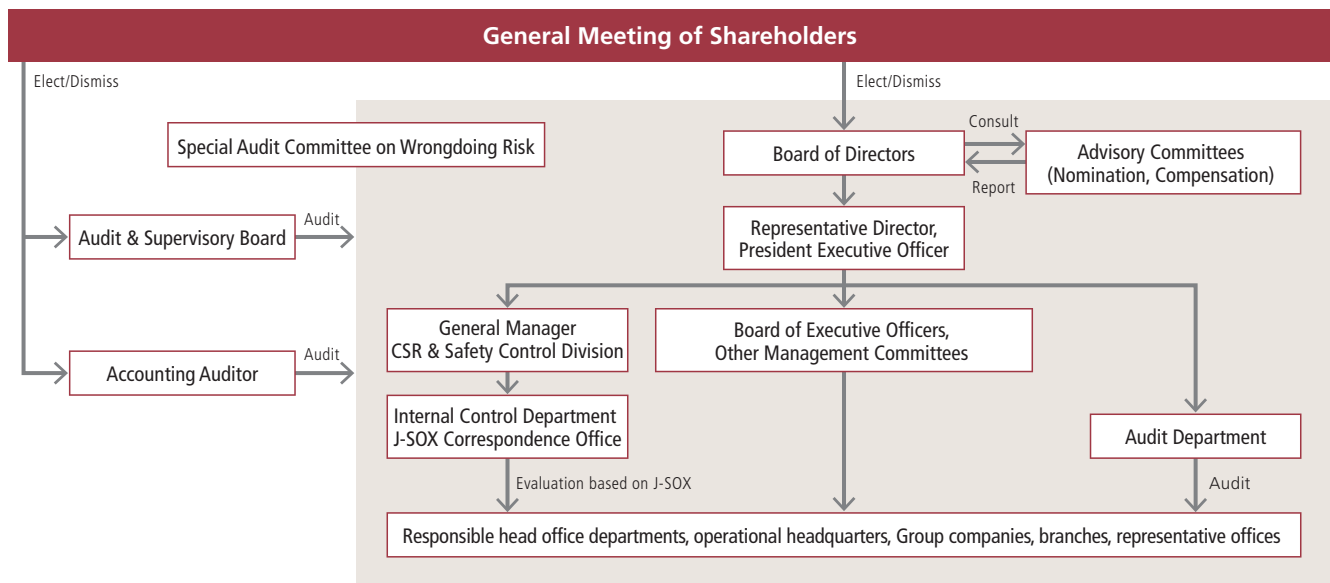
KYB is structured as a company with an Audit & Supervisory Board in accordance with the Companies Act, and corporate governance centers on the Board of Directors and the Audit & Supervisory Board and its individual members. In addition, KYB has instituted an executive officer system to expedite decision-making and streamline business execution.

Two of the six members of the Board of Directors are independent outside directors, and two of the four members of the Audit & Supervisory Board are outside Audit & Supervisory Board members (including one independent outside Audit & Supervisory Board member). KYB believes it has strengthened independent and objective management supervision by the Board of Directors because one-third of the board consists of independent outside

directors. KYB determines whether outside directors and outside Audit & Supervisory Board members are independent based on KYB's independence standards, and selects individuals who can be independent of other members of management.

Furthermore, the Internal Control Department is the organization responsible for overall planning and coordination of global governance and compliance, and the J-SOX Correspondence Office within the Internal Control Department conducts evaluations based on Japan's Financial Instruments and Exchange Law (J-SOX). We have also established the Special Audit Committee on Wrongdoing Risk, which is chaired by an outside director and has broad responsibility for detecting signs of misconduct and situations that give rise to it.

Corporate Governance Structure



Independence Standards for Outside Directors and Outside Audit & Supervisory Board Members

KYB Corporation (the Company) has established the following independence standards for outside directors and outside Audit & Supervisory Board members based on the requirements for independent officers established by financial instrument exchanges. Officers are deemed to lack independence if any of the following apply.

- Persons who have work experience at the Company or its subsidiaries (KYB Group)
- Persons who have work experience at principal lenders¹ to the KYB Group
- Major shareholders² of the Company, or their members or executives
- Major customers³ for the KYB Group's products and services, or their members or executives
- Major suppliers⁴ of products and services to the KYB Group, or their members or executives
- Consultants, accounting professionals, legal professionals and the like who receive annual payments or other goods in kind exceeding ¥10 million from the KYB Group, excluding officer compensation (if a corporation or other organization is the recipient and the amount received exceeds 2% of the organization's annual income, any member or executive of the organization).
- Persons who receive donations of more than ¥10 million annually from the KYB Group (if the recipient is a corporation or other organization, any member or executive of the organization).
- Members or executives of corporations or other organizations that engage in the mutual dispatch of directors or executive officers with the KYB Group.
- Persons who have work experience at an audit firm that is an accounting auditor of the KYB Group
- Persons to whom any of 3 to 9 above are applicable over the past 10 years
- A spouse or relative within the second degree of kinship of a person to whom any of 1 to 10 above are applicable
- Other persons who have special reasons that may cause a conflict of interest with the Company

Notes: 1. The KYB Group's principal lenders are financial institutions and other large creditors that the KYB Group relies on for funding and could not readily replace.
 2. Major shareholders of the Company are those that hold 10% or more of voting rights at the end of the Company's fiscal year, whether directly or indirectly (including rights held indirectly through a trust bank or other vehicle).
 3. Major customers for the KYB Group's products and services are those with an annual transaction amount exceeding 2% of the KYB Group's consolidated sales.
 4. Major suppliers of products and services to the KYB Group are those with annual transaction volume exceeding 2% of the consolidated sales of the supplier group.

Evaluation of the Effectiveness of the Board of Directors

In each of the past three fiscal years, KYB evaluated the effectiveness of the Board of Directors and disclosed a summary of issues and initiatives in the Corporate Governance Report. For example, we reviewed the standards for matters to be submitted for discussion at meetings of the Board of Directors, established a Nomination Committee and a Compensation Committee, and conducted factory tours for individual shareholders.

Takeover Defense Measures

Countermeasures to Large-Scale Purchase of the Company's Shares (Takeover Defense Measures) is a KYB initiative to increase corporate value and thus ensure the common interest of shareholders for the medium and long term. The 97th Ordinary General Meeting of Shareholders on June 25, 2019 approved a resolution to renew this initiative until the end of the 100th Ordinary General Meeting of Shareholders scheduled for June 2022.

Strengthening the KYB Group's Governance

| Initiatives | |
|-------------|--|
| FY2014 | Initiated in-person interviews with relevant employees |
| FY2015 | Appointed one independent outside director |
| FY2016 | Appointed two independent outside directors and established a discretionary Nomination Committee |
| FY2017 | Established a discretionary Compensation Committee |
| FY2018 | Established independence standards for outside directors and outside Audit & Supervisory Board members |
| FY2019 | Established the Special Audit Committee on Wrongdoing Risk and the Internal Control Department Raised the ratio of independent outside directors on the Board of Directors to one-third |

Non-Financial Corporate Governance Achievements

1. Corporate Guiding Principles now available in 14 languages (Japanese, English, Chinese (simplified and traditional script versions), Portuguese, Vietnamese, French, German, Czech, Thai, Indonesian, Spanish (European and Latin American versions), and Tagalog)
2. Ratio of independent outside directors on the Board of Directors now one-third
3. Independence standards for outside directors and outside Audit & Supervisory Board members formulated

Officer Compensation

Compensation Structure

Officer compensation consists of fixed monthly compensation (basic compensation) according to position and responsibilities, and performance-linked compensation (bonus) that varies depending on the Company's business results. Outside directors

and Audit & Supervisory Board members only receive fixed compensation according to their respective roles, and in view of their independence do not receive performance-linked compensation.

| Type of Compensation | Eligible Officers | Maximum Total Compensation | Date of Resolution of the General Meeting of Shareholders | Calculation Process |
|---------------------------------|---|--|---|--|
| Fixed compensation | Directors | ¥30 million per month (¥360 million per year) | June 27, 1997 75th Ordinary General Meeting of Shareholders | Consultation with Compensation Committee |
| | Audit & Supervisory Board members | ¥8 million per month (¥96 million per year) | June 24, 2011 89th Ordinary General Meeting of Shareholders | — |
| Performance-linked compensation | Directors (Excluding outside directors) | 40% or less of total compensation (Fixed compensation + Performance-linked compensation) | Approval annually by resolution at the Ordinary General Meeting of Shareholders | Consultation with Compensation Committee |

Note: The limit on total fixed remuneration for directors does not include salary for employees concurrently serving as directors.

Compensation Decisions

For director compensation, the discretionary Compensation Committee composed of representative directors and outside directors verifies the propriety of the criteria for calculating fixed and performance-linked compensation and reports the propriety of criteria to the Board of Directors.

Fixed compensation for directors is determined by resolution of the Board of Directors upon receiving the report from the Compensation Committee, within the limit on total compensation

decided at the Ordinary General Meeting of Shareholders.

Payment of performance-linked compensation for directors (excluding outside directors) is approved annually by resolution at the Ordinary General Meeting of Shareholders.

Fixed remuneration for Audit & Supervisory Board members is determined in consultation with Audit & Supervisory Board members, within the limit on total compensation decided at the General Meeting of Shareholders.

Calculation and Determination of Performance-Linked Compensation to Be Paid

1. Criteria and Business Results That Serve as the Basis for Calculation

Performance-linked compensation is calculated according to the degree of achievement in the preceding fiscal year (the “base fiscal year”) of the consolidated performance forecast according to the following calculation criteria (four items).

| Calculation Criteria | Target | Result |
|--|--------|----------|
| Segment profit (Millions of yen) | 22,000 | 22,010 |
| Segment profit margin (%) | 5.30 | 5.34 |
| Profit (loss) attributable to owners of the parent (Millions of yen) | 16,600 | (24,757) |
| Profit (loss) margin attributable to owners of the parent (%) | 4.00 | (6.01) |

Note: The targets are the consolidated financial results forecast for the base fiscal year (FY2018, or the fiscal year ended March 2019) described in the financial statements at the end of the fiscal year prior to the base fiscal year (FY2017, or the fiscal year ended March 2018).

2. Calculation of Amount to Be Paid

Total performance-linked compensation is limited to 1.0% of profit attributable to owners of the parent. Moreover, the ratio of performance-linked compensation to total compensation (fixed compensation + performance-linked compensation) of directors (excluding outside directors) shall not exceed 40%.

The total amount to be paid is calculated by multiplying the maximum amount payable by a payout ratio derived from the number of calculation criteria targets in 1. that were achieved. Performance-linked compensation is not paid in the case of a loss attributable to owners of the parent.

| Calculation criteria targets achieved | 4 | 3 | 2 | 1 | 0 | Loss attributable to owners of the parent |
|---------------------------------------|------|-----|-----|-----|-----|---|
| Payout ratio | 100% | 80% | 60% | 40% | 20% | 0% |

3. Determination of Amount to Be Paid according to Position

The amount of performance-linked compensation to be paid to individual directors (excluding outside directors) is calculated based on proportional distribution of the total amount to be paid in 2. to each director according to the following payment points for each position. Amounts are rounded down to the nearest ¥100,000.

| Position | Chairman | Vice Chairman | President | Vice President | Senior Managing Executive Officer |
|----------------|----------|---------------|-----------|----------------|-----------------------------------|
| Payment points | 8 | 7 | 10 | 6 | 5 |

Total Compensation for Each Officer Category, Total Compensation by Type, and Number of Eligible Officers

| Category | Total Compensation (Millions of yen) | Compensation by Category (Millions of yen) | | Number of Eligible Officers |
|---|--------------------------------------|--|---------------------------------|-----------------------------|
| | | Fixed compensation | Performance-linked compensation | |
| Directors (Excluding outside directors) | 225 | 225 | — | 7 |
| Outside directors | 17 | 17 | — | 2 |
| Audit & Supervisory Board members (Excluding outside members) | 46 | 46 | — | 2 |
| Outside Audit & Supervisory Board members | 47 | 47 | — | 3 |

Notes: 1. Total compensation for directors (excluding outside directors) does not include salary for employees concurrently serving as directors.

2. The above data includes one director and one outside Audit & Supervisory Board member who retired at the conclusion of the 96th Ordinary General Meeting of Shareholders on June 22, 2018.

3. KYB abolished the retirement benefits system for directors at the conclusion of the 89th Ordinary General Meeting of Shareholders on June 24, 2011, but the payment of retirement benefits according to tenure as of the close of that meeting was also approved. Based on this approval, in addition to total compensation shown above, the following retirement benefits for directors (excluding outside directors) were paid for FY2018. ¥14 million (one director)

Note: This amount includes the payment of ¥12.1 million to one director, which was disclosed in previous years as allowance for retirement benefits. Retirement benefits are paid to one director who retired during FY2018.

4. FY2018 retirement benefits for directors will not increase because the retirement benefit system for directors was abolished as described above.

Internal Control and Compliance

Internal Control System

Basic Policy

The Board of Directors of the Company ensures effective corporate governance by instituting the Basic Policy for Internal Control System¹ in accordance with the Companies Act, and by implementing various measures including a risk management system, a Group management system and an internal compliance system. The KYB Group also maintains and assesses the implementation of internal control over financial reporting using the procedures stipulated by the Financial Instruments and Exchange Act. In this way, the KYB Group ensures reliable financial reporting and appropriate information disclosure through internal control reports.

Key Points for Internal Control

1. Internal Control Department

The Internal Control Department is responsible for overall planning and coordination of global governance and compliance. The J-SOX Correspondence Office in the Internal Control Department maintains and assesses the implementation of internal control over financial reporting.

2. Basic Policy for Internal Control System

The Company's Board of Directors has instituted the Basic Policy for Internal Control System and monitors the status of related activities. Summaries of its findings are disclosed in business reports.

3. Strengthening Systems for Sharing Information and Collaborating among Group Companies

We are enhancing meetings between the Company and Group company management. We are increasing the frequency of meetings, and mainly at top management meetings, Domestic Affiliated Companies Management Meetings and at global division meetings, we are intensifying discussions about identifying and preventing misconduct.

4. Upgrading the Business Organization

We enhance mandatory checklists used in planning new product

and business development at product development assessment meetings and executive officer meetings in order to upgrade our system for verifying the adequacy of technologies, product performance, quality inspection systems and manufacturing capabilities.

5. Ensuring Personnel Rotation

We are developing effective lines of succession in ways such as ensuring transparent operations through sharing knowledge and expertise internally. In this way, we will conduct appropriate personnel rotation.

6. Rigorous Application of Internal Regulations during Emergencies

We remind all employees of the Company and Group companies of their reporting obligations to ensure rigorous reporting under internal reporting rules that include the Rule of Prompt Report² and Bad News First system, which calls for employees of the Company or Group companies to immediately report to the Company should they become aware of a potential serious problem.

7. Review to Improve the Effectiveness of the Whistleblowing System

We conduct education concerning the whistleblowing system using e-learning for indirectly related departments, through briefing sessions for frontline personnel, as well as by comprehension tests and in-person interviews.³ In addition, we are considering measures including mandatory reporting to improve the effectiveness of whistleblowing for improper acts related to product quality and safety.

Notes: 1. Please refer to the Company website for additional details.
<https://www.kyb.co.jp/english/company/governance.html>

2. A core component of the KYB Group's crisis management system, in which department heads and production base managers promptly and accurately report important information to the president of the Company.

3. We proactively gather frontline information in ways such as conducting in-person interviews to announce, explain and confirm compliance with internal regulations while collecting information about issues that interviewees are experiencing in their workplaces.

Compliance

Basic Policy

We regard compliance as adherence to the laws, orders and rules of society at large, as well as to the Company's articles of incorporation, rules and agreements associated with business activities, in addition to corporate ethics that promote sound business activities.

1. We have developed the Corporate Guiding Principles as rules for the execution of business activities by officers and employees, and are focusing on initiatives including establishing legal compliance and corporate ethics.

2. We are implementing compliance education through training sessions by job title and section.

3. We have established communication channels to management by using the Rule of Prompt Report and Suggestion Box as a system for the Company and all Group companies to identify company risks in a prompt manner. We have also established and are operating contact points for whistleblowers.

Key Points for Compliance

1. Fostering Compliance Awareness in the KYB Group

We will reconfirm employee responsibilities after reflecting on issues concerning improper acts. Based on this, we will use training and education to change the mindset of all executives and employees.

2. Education and Training to Raise Awareness of Social Responsibility

We will systematize repeated top-down education on corporate ethics. We will also proactively review the content of teaching materials to incorporate multiple case studies that lead to change in the awareness of all executives and employees.

3. Emphasize the Importance of Compliance Regularly

Top management of the Company will consistently emphasize the importance of compliance within the Group. In addition, top management will visit Company production bases and other locations, and Group companies in Japan and overseas, to provide guidance on fostering compliance awareness.

4. Personnel Evaluations and Related Measures

Personnel evaluations will include a system for evaluating attitudes toward compliance initiatives, such as compliance with laws and internal rules. In addition, we will conduct small group activities with the theme of preventing misconduct and commend useful activities and conduct other initiatives to support the development of executives and employees who think independently and make improvements themselves.

5. Organizational Upgrades

We will establish committees as necessary. For example, we have established the Personal Information Protection Management Committee to encourage the proper acquisition, use, management and storage of personal information and prevent its leakage. We have also established the Export Control Management Committee to ensure full compliance with export-related laws and regulations and to prevent illegal export of our products and technologies (including services), either directly or indirectly.

6. Initiatives to Prevent Recurrence of Antitrust Violations

We are working on the following measures to prevent violations of antitrust laws based on lessons learned from violations in the United States.

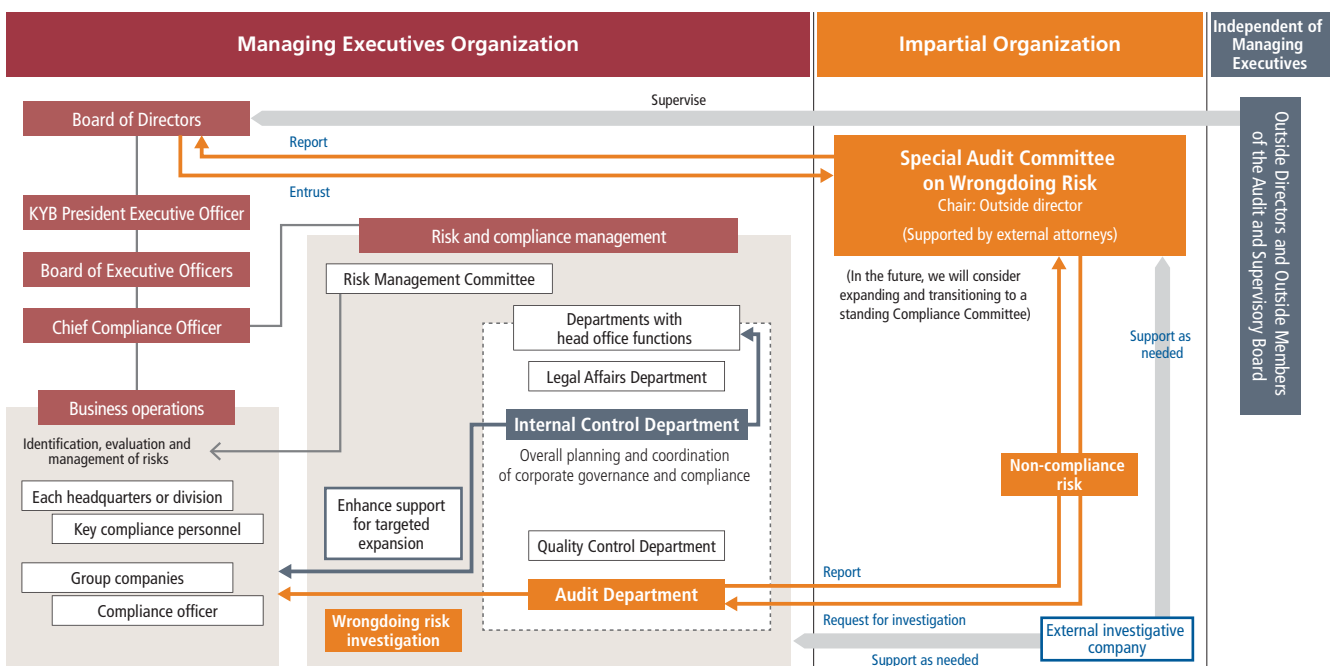
- 1) Establishing an anti-monopoly compliance policy
- 2) Securing written pledges from sales personnel that they will not violate antitrust laws
- 3) Formulating rules for contact with competitors
- 4) Conducting educational activities related to antitrust laws
- 5) Conducting in-person interviews with sales personnel

7. Initiatives to Prevent Bribery-related Violations

We are working on the following measures to prevent violations of bribery-related laws and regulations.

- 1) Establishing an anti-bribery policy
- 2) Establishing internal regulations
- 3) Conducting educational activities related to bribery-related laws
- 4) Conducting in-person interviews with sales personnel

Current Internal Control System (From April 2019)



Initiatives to Prevent the Recurrence of Nonconforming Acts Associated with Seismic Isolation/Mitigation Oil Dampers

Establishing Compliance Management

The KYB Group will use all of its capabilities to change the Group mindset to one that places the highest value on compliance.

Measures to Emphasize in Preventing Recurrence

We will implement the following initiatives as effective measures to encourage all executives and employees to autonomously promote compliance.

- ① We will promote awareness among executives and employees through education and training based on case studies and analysis of examples at other companies to bring attention to the adverse effects of compliance violations on society as a whole.
- ② We will measure how well corporate ethics have been inculcated among executives and employees.
- ③ We will add compliance issues to themes for improvement in each department.

The progress of measures to prevent recurrence is reported to the Company's Board of Directors and on its website every three months.

<https://www.kyb.co.jp/english/company/progress/index.html>

Tighten the Subsidiary Management System

We will work to review and strengthen our management system in order to conduct integrated management with Group companies.

Strengthen System for Sharing Information with Group Companies

- Enhance meetings between the Company and Group company management. Increase the frequency of meetings, and mainly at senior management meetings, management meetings at Group companies in Japan, and international meetings, intensify discussions about identifying and preventing misconduct.

Review Management Systems for Group Companies

- Make the Internal Control Department responsible for comprehensive planning and coordination of Group governance, and strengthen systems that provide deeper understanding of Group companies.
- Confirm the effectiveness of the Regulations on the Promotion of Group Compliance to strengthen the required systems, and strengthen external risk audits of business execution.
- We have established the Special Audit Committee on Wrongdoing Risk, which is chaired by an outside director. It has broad responsibility for uncovering signs of wrongdoing and conditions that give rise to it. Its purview includes quality misconduct, as well as accounting fraud and bribery. We will consider expanding and transitioning to a standing Compliance Committee (tentative name).
- The Audit Department investigates misconduct and reports monthly to the Board of Directors and other bodies. We will use external companies if more specialized investigation is required.

Analyze and Monitor Business Risks at Group Companies

- We will identify specific laws and regulations that apply to each subsidiary's business and conduct risk analysis and required education.

Reorganize Group Companies

- We will consider reorganizing the Group in light of compliance management.

Initiatives with Suppliers

Basic Policy for Procurement

KYB works to fulfill its corporate social responsibility (CSR) and continues to be a company that society can rely upon. Suppliers are important partners for us in continuously developing our business through *monozukuri* (Japanese manufacturing expertise) and contributing to realization of an affluent society.

Our basic policy for procurement is described below.

Basic Approach to Procurement

- ① Procurement activities aimed at the coexistence and mutual prosperity of KYB and its suppliers
- ② Legal compliance
- ③ Quality first
- ④ Safety and health, human rights and labor
- ⑤ Continuous cost reduction activities
- ⑥ On-time delivery
- ⑦ Protection of the natural environment
- ⑧ Construction of global procurement system
- ⑨ Risk management
- ⑩ Classified information management
- ⑪ Prevention of corruption

▶ For details, please see the corporate website.
<https://www.kyb.co.jp/english/company/csr.html>

FY2018 Procurement Policy Briefing

In April 2018, we invited 231 suppliers that have been involved in KYB manufacturing to the KYB Procurement Policy Briefing at the Palace Hotel in Chiyoda-ku, Tokyo to strengthen cooperation



with our suppliers. KYB senior management explained our corporate policy, procurement policy and quality policy to representatives of our suppliers, commended excellent suppliers who contributed greatly to QCD,* and presented mementos. After the briefing, we held a social event that facilitated and deepened discussion with suppliers.

* Quality, cost and delivery

Final Report Meeting of Theme Study Groups

In April 2018, six study groups composed of members from 42 suppliers began improvement activities for FY2018 under the themes of quality, delivery, productivity and business continuity plans



(BCP). In March 2019, we held the FY2018 Final Report Meeting of Theme Study Groups at Wink Aichi (Aichi Industrial Labor Center, Aichi Prefecture) for these groups to present their final reports on the year's achievements. The comprehensive activities of these groups have resulted in safety

improvements, fewer quality defects, faster delivery times and greater productivity among suppliers, and have led to the creation of a BCP crisis management system. New teams are continuing these activities in FY2019.

Survey of Status of BCP

In preparation for the three anticipated interlocked earthquakes (Tokai-Tonankai-Nankai) in Japan, we provided an explanation of BCP at the Procurement Policy Briefing and at meetings regarding production trends at each plant.

As in FY2017, in light of the importance of understanding the BCP status of suppliers we conducted a questionnaire for self-assessment consisting of 100 items in seven categories (actions for anticipated risks; securing personal safety and emergency evacuation; emergency measures taskforce; confirmation of employee safety; confirmation of property damage; instructions for returning home and measures for people who have difficulty returning home; and restoration taskforce). Moreover, we surveyed the status of readiness of first-, second- and subsequent level suppliers with regard to a major earthquake. In this way, we have all suppliers review the status of their BCPs and encourage them to study issues requiring improvement and systematically implement BCP activities.

Initiatives to Prevent Human Rights Violations in the Supply Chain

Companies today are expected to prevent human rights violations globally, including in their supply chains.

For example, under the Dodd-Frank Wall Street Reform and Consumer Protection Act, companies are required to perform due diligence and identify whether their products contain tantalum, tungsten, tin or gold purchased from mines in the Democratic Republic of Congo (DRC) and nine neighboring countries, where the extraction of such mineral resources may be used to finance or benefit armed groups that are causing human rights violations and environmental destruction. The aim of the Dodd-Frank Act is to indirectly cut off financial sources from these "conflict minerals" to prevent such human rights violations. The EU has taken a broader approach to restricting conflict minerals by requiring all companies importing mineral resources into the EU to take similar actions.

In light of the Dodd-Frank Act, the KYB Group annually checks its products with the cooperation of its suppliers, summarizes the results and reports to customers that request such information.

In addition, according to the U.K. Modern Slavery Act 2015 we annually release a statement on KYB Group business activities and initiatives to prevent slave labor and human trafficking in our supply chain, including the above-mentioned conflict mineral measures. We will carry on with our awareness-raising activities on prohibiting human rights violations and slavery labor.

▶ The details are available in our Modern Slavery Act Transparency Statement for Fiscal Year 2018 released on September 27, 2019.
https://www.kyb.co.jp/english/media/ir_20190927_02.pdf

Risk Information

This section explains the major risk factors relevant to the KYB Group's operating results and financial condition that may have a significant effect on decisions by investors. Forward-looking statements in this section represent the judgments of the KYB Group (KYB and its consolidated subsidiaries) as of March 31, 2019.

Economic Risks

Economic Conditions

The KYB Group's consolidated net sales primarily derive from the supply of components to automobile manufacturers, construction machinery manufacturers, commercial vehicle manufacturers and other customers. Component manufacturers have accelerated overseas operations to address the increase in the overseas production bases of customers. The Group also has production bases in the Americas, Europe and Asia, and supplies products to customers in each of these regions. Overseas production bases have a significant impact on the Group's operating results and financial condition, and are subject to the influence of changes in customer production volume resulting from factors including changes in regional economic conditions.

Fluctuations in Exchange Rates and Interest Rate Increases

With an overseas sales ratio of 55.2%, the KYB Group relies heavily on markets outside of Japan. As a result, fluctuations in foreign exchange rates have a significant impact on the Group's exports from Japan and the performance of Group companies in other countries. An increase in interest rates in Japan or other countries could have a significant impact on the KYB Group's operating results.

Risks in Business Operations

Demand Trends

Sales of the KYB Group's Automotive Components and Hydraulic Components Operations segments depend greatly on the global production volume of automobiles and construction machinery. A decline in demand for these products caused by a global economic downturn could have a significant impact on operating results. The KYB Group sells most of its system products, aircraft components, special-purpose vehicles and electronics components in Japan. In particular, demand for the KYB Group's special-purpose vehicles, which are primarily concrete mixer trucks, can fluctuate significantly due to changes in the amount of construction activity, which is closely correlated with the economic outlook.

Prices and Quality

The KYB Group's products are subject to intense price-based competition in both domestic and international markets. Customers regularly request cost cuts and lower prices. Quality is also critical. The Group supplies vital automotive components, such as shock absorbers that maintain vehicle stability and power steering systems. For construction machinery and commercial vehicles, the Group supplies key functional components such as motors and hydraulic cylinders that drive the main unit. Consequently, the Group may incur substantial expenses, including the payment of damages demanded by customers, if it supplies defective products. Furthermore, sales volume and prices for aftermarket automotive shock absorbers are subject to the impact of regional economic conditions and competition.

Procurement of Materials and Components

The KYB Group purchases materials and components from a large number of suppliers. Prices of these items are closely linked to prices on international commodity markets. The KYB Group may not be able to fully reflect an increase in the cost of materials or components in its selling prices, or to reduce prices of materials and components sufficiently to reflect a reduction in selling prices, which could have a significant impact on operating results.

Funding

The KYB Group obtains loans mainly from financial institutions in Japan and other countries to fund capital expenditures and to secure working capital. The Group obtains these loans while carefully monitoring financial markets. However, it may be unable to procure funds when needed at favorable terms due to events including a broad decline in the prices of the Group's products, an economic recession, a credit crunch, or a decline in the Group's credit rating, which could affect the Group's financial condition and operating results.

Business Downturn

Bankruptcy at KYB Group overseas production or sales bases caused by factors including a decline in orders or profitability could significantly impact the Group's operating results.

Counterparty Credit Risk

The KYB Group sells its products to automobile and construction machinery manufacturers and many other customers. An unexpected problem involving customer credit risk could affect the Group's operating results.

Nonconforming Acts in the Inspection Process for Seismic Isolation/Mitigation Oil Dampers

The Company and its subsidiary Kayaba System Machinery Co., Ltd. manufacture and sell seismic isolation/mitigation oil dampers for buildings. We recently determined that some of the seismic isolation/mitigation oil dampers ("Nonconforming Products") shipped and installed in buildings ("Target Properties") did not conform to performance evaluation standards certified by the Minister of Land, Infrastructure, Transport and Tourism (the "Minister"),* or to the standards of customers, because of falsification of performance inspection record data (the "Incident"). We reported the Incident to the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) and announced the status of our response on October 16, 2018.

On November 15, 2018, we uncovered additional matters that we should confirm. On December 19, 2018, we announced that in addition to the falsification of performance record data, the inspection measurement results submitted for damping force had been changed by moving the median damping force on extension and compression in the direction of the origin. At the same time, we presented the results of our investigation. In addition, as a result of ongoing analysis of data remaining in the inspection machines, on March 15, 2019 we revised the number of Target Properties and products that we had announced on December 19, 2018.

The Company's basic policy is to promptly ensure conformity of products that do not conform to the Minister's certified standards and products for which conformity is uncertain. For items that conform to the Minister's certified standards but not to customer standards, we will take appropriate measures according to the

wishes of property owners, residents and other stakeholders. Our management priority is to eliminate worries and concerns, so we will carefully explain matters to owners and other stakeholders. Considering the gravity of the Incident, we established an independent external investigative committee chaired by Koichi Namba, a lawyer from Mori Hamada & Matsumoto legal office and former Chief Judge at the Tokyo High Court, to review the facts of the Incident, analyze its causes, and recommend measures to prevent recurrence. On February 4, 2019, we received the committee's report on the results of the investigation, and accepted its findings and proposed preventive measures. Based on these recommendations, we will take appropriate steps, further strengthen corporate governance and the internal control system, thoroughly implement measures to prevent recurrence, and take action to restore trust.

The Company provides for product warranties for seismic isolation/mitigation oil dampers using information and facts currently available and considered reliable. Provisions have been recorded in our accounts for costs to produce seismic isolation/mitigation oil dampers, to replace seismic isolation oil dampers, to make structural modifications, and to cover expenses incurred by relevant headquarters and divisions. Therefore, future expenses associated with the Incident, including compensatory damages, could significantly impact the Group's operating results.

*There is no Minister's certification system for seismic mitigation oil dampers.

Impact of Improper Claims to the Ministry of Defense

The Company has recorded a provision in its accounts for loss related to repayment and other expenses associated with improper claims regarding working hours that were found to have been made to the Ministry of Defense in connection with a defense equipment contract. The Ministry of Defense has been conducting a special investigation since March 14, 2019, and we are cooperating fully. This provision is a reasonable estimate of expenses at this time, and may change depending on the progress of the special investigation.

Risks Associated with Significant Lawsuits or Other Legal Action

If the KYB Group is the defendant in a lawsuit and the outcome is unfavorable, the resulting payment and other demands may

have a significant impact on the Group's operating results.

Risks Associated with Fires, Accidents and Natural Disasters

Many plants of the KYB Group produce hydraulic products that utilize the properties of oil. In addition, some plants have coating equipment that uses organic solvents, and storage tanks for hydraulic oil, chemicals and other substances. A fire or hazardous substance leak could temporarily shut down manufacturing activity. In Japan, many plants of the KYB Group and many of its suppliers are located in the Chubu area. A major earthquake or

other event in this area that prevents these plants from operating could cause a substantial decline in the Group's production capacity. In addition, an earthquake, fire, conflict, act of terrorism or other event in an area outside of Japan where the KYB Group has a plant could cause a substantial decline in the Group's production capacity.