Management's Discussion and Analysis of Financial Position and Operating Results

Dentsu Inc. and Consolidated Subsidiaries
As of March 30, 2017

Any forward-looking statements in the following discussion and analysis are based on the judgment of management as of the date that Dentsu Inc. (hereinafter "Dentsu" or "the Company") filed its securities report for the fiscal year ended March 30, 2017 with regulatory authorities.

Significant Accounting Policies and Estimates

The Company's consolidated financial statements are prepared on the basis of International Financial Reporting Standards (IFRS), published by the International Accounting Standards Board.

In the preparation of these consolidated financial statements, management discloses the amounts of the reported asset and liability figures as well as those of off-balance sheet transactions such as contingent liabilities, as of the date the accounts are closed. Management also estimates the impact of these figures on the Company's financial position and operating results during the reporting period. Management continuously evaluates forecasts and assumptions regarding such items as investments, retirement benefits and corporate taxes, as well as contingencies and litigation. Management bases its estimates and assumptions on the consideration of several factors, given past performance and conditions. These results underpin asset and liability book values and reported revenue and expense figures. However, uncertainties are inherent in such results and estimates may vary from actual results.

The critical accounting policies described below are those that management considers to have specific potential to affect the financial position and operating results of the Group. Such policies may also include important assumptions and estimates used in creating the Company's consolidated financial statements and therefore have a material impact on these statements.

Revenue Recognition

Revenue consists primarily of commissions received for the placement of advertising into different media and consideration received from advertisers and others for providing services, such as assistance in the production of advertising, including creative, and various content-related services.

Revenue from the production of advertising and other advertising-related services is recorded based on the consideration paid as compensation for such services to the Group by advertisers and others less costs incurred. In some cases, revenue is also recorded based on a fixed fee or other compensation.

Revenue from commissions received from advertisers for the placement of advertising is generally recognized when the media is placed. Other revenue is generally recorded when the service is completed, an estimate of the amount of compensation can be reasonably determined and it is probable that the future economic benefit will flow to the Group.

Revenue and costs arising from transactions relating to services other than advertising services are presented as a gross amount.

Turnover represents the total amount billed and billable to clients by the Group, net of discounts, VAT and other sales-related taxes. Disclosure of turnover information is not required under IFRS.

Impairment Loss on Property, Plant and Equipment, Goodwill, Intangible Assets and Investment Property

The Group determines whether there is any indication of potential impairment loss on non-financial assets excluding inventories and deferred tax assets on the closing date. If any such indication exists, an impairment test shall be conducted based on the recoverable amount of relevant assets. Goodwill and intangible assets with indefinite useful lives are not subject to amortization, and are instead tested for impairment loss annually regardless of whether there is any indication of impairment, or every time when there is an indication of impairment loss. The recoverable amount of assets shall be either the fair value of assets or cash-generating units after deducting costs of disposal of the assets, or value in use, whichever is higher. If the carrying amount of an asset or cash-generating unit exceeds its recoverable amount, the carrying amount of the asset is reduced to its recoverable amount and impairment loss is recognized. In the calculation of its value in use, certain assumptions regarding useful life, future cash flow, growth rate, discount rate, etc., of the asset are used.

These assumptions are determined based on past performance, best estimates, and judgments based on business plans approved by the management of the Company. The assumptions, however, may be affected by modifications in business strategies and changes in market environment. If any change to these assumptions is required, the amount of impairment loss to be recognized may be significantly affected.

Valuation of Financial Instruments

The Group holds financial assets such as securities and derivatives, and uses certain assumptions in the valuation thereof. Fair values are determined in accordance with calculation procedures such as the market approach, as well as referencing market prices. In particular, the fair value of stocks that are actively traded in the market, among other securities and financial assets, is determined based on the market price. The fair value of stocks that are not actively traded in the market is evaluated at the amount calculated by using observable market data, or at the amount calculated primarily by the market approach using unobservable inputs.

Management evaluates whether the valuation of fair value of financial instruments is conducted in a reasonable manner. However, fair value to be recognized may be significantly affected if any revision to the estimate is required due to unforeseeable changes in assumptions that underlie the value.

Valuation of Defined Benefit Obligation

Defined benefit obligation and retirement benefit costs are recorded on the basis of pension actuarial calculations. These calculations are dependent upon such factors as the discount rate, future compensation levels, employee turnover, and mortality rates, among others.

Management evaluates whether those assumptions that underlie the above values are reasonable. However, if the actual values of these factors vary from the forecast values, or if the assumptions that underlie these values change, the Company may be significantly impacted by the recognition of such costs or by the recording of such liabilities, on a consolidated basis.

Provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the obligation will be required to be settled, and a reliable estimate can be made of the amount of the obligation. Where the effect of the time value of money is material, provisions are measured based on the present value using a discount rate reflecting the risks specific to the liability.

Such provisions are calculated based on the best estimate, taking uncertainties on the closing date into consideration. However, the amount may be impacted in case of any unforeseeable event s or changes in circumstances. If the actual result varies from the estimate, the amount of obligations to be recorded may be significantly affected.

Collectability of Differed Tax Assets

Deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which carryforwards of unused tax losses, tax credit carryforwards and deductible temporary differences can be utilized. Deferred tax assets are reassessed at the end of the fiscal year and reduced by the amount of any tax benefits that are not expected to be realized.

The Group records deferred tax assets based on future taxable income and ongoing tax planning that emphasizes cautious and highly implementable approaches. Thus, we determine that the collectability is evaluated based on reasonable estimates. However, such estimates may be impacted in case of any unforeseeable events or changes in circumstances. If the actual result varies from the estimate, costs to be recognized and assets to be recorded may be significantly affected.

Change in Fiscal Period

In the previous consolidated fiscal year, the Company changed its fiscal year end from March 31 to December 31. Subsidiaries with fiscal year-ends other than December 31 have also changed their fiscal year-ends to December 31. As a result of this change, for the Company and its main subsidiaries conducting business in Japan, the previous consolidated fiscal year is the nine-month period from April 1, 2015, to December 31, 2015. The fiscal year for subsidiaries conducting business overseas is the twelve-month period from January 1, 2015, to December 31, 2015.

Analysis of Operating Results for the Fiscal Year under Review

Revenue and Gross Profit

Consolidated revenue for the fiscal year under review reached 838.3 billion yen and gross profit totaled 789.0 billion yen.

Within gross profit, 363.2 billion yen (up 4.3%) was generated by the Japan business due to gross profit margin improvement on a non-consolidated basis and contributions from domestic Group companies.

In the Group's international business operations, gross profit was 426.0 billion yen (up 2.9%). The organic gross profit growth rate in the international business rose 5.7% year on year. By region, growth was higher than in the previous fiscal year, with EMEA up 6.9%; the Americas, 3.1%; and APAC, 7.9%.

Selling, General and Administrative Expenses, Other Income, Other Expenses and Operating Profit

Consolidated selling, general and administrative (SG&A) expenses for the consolidated fiscal year under review came to 659.8 billion yen.

Other income was 16.5 billion yen, and other expenses came to 8.0 billion yen.

As a result, operating profit for the consolidated fiscal year under review reached 137.6 billion yen.

Share of Results of Associates, Finance Income or Costs, and Profit for the Year

Share of results of associates for the consolidated fiscal year under review was 3.3 billion yen, and the net difference between finance income and finance costs came to 8.1 billion yen in costs. As a result, profit before tax came to 132.9 billion yen.

Of the profit for the year, derived by deducting income tax expense from profit before tax, profit attributable to owners of the parent reached 83.5 billion yen.

Management Issues

With the March 2013 acquisition of the Aegis Group plc, (currently the Dentsu Aegis Network Ltd.), the Dentsu Group was transformed into a full-fledged global network.

In recent years, amid the advance of technological innovations and significant changes in consumer behavior patterns, the organic combination of various measures within marketing activities has enabled companies to provide customers with rich corporate brand experiences like never before, while at the same time substantially heightening the precision and efficacy of marketing activities. Within this environment, we formulated the "Dentsu 2017 and Beyond" medium-term management plan to contribute to enhancing the corporate value of all our clients and becoming the world's most advanced global network. Four numerical targets for fiscal 2017 were established under this plan:

- Gross profit organic gross rate of 3%–5% (average annual growth rate)
- Gross profit international business ratio of 55% or higher
- Gross profit digital domain ratio of 35% or higher
- Underlying operating profit operating margin of 20% or higher

Note: Underlying operating profit operating margin: Underlying operating profit ÷ Gross profit × 100

Specific issues and initiatives for achieving the medium-term management plan are as follows.

(1) Diversifying the portfolio on a global basis

The gross profit organic growth rate in the Group's international business operations for the fiscal year under review was 5.7%, once again achieving a rate higher than those of its competitors in consecutive years. As a result, the gross profit international business ratio reached 54%, remaining flat on a 2016 calendar year basis. However, if the impact from exchange rate fluctuations is excluded, the gross profit organic growth rate in the Group's international business operations becomes 18.1%, demonstrating a steady increase over the same period in the previous fiscal year.

The Group believes the reasons for this robust growth is because each Group company provides one-stop solutions to meet client needs by cooperating and coordinating, leveraging their unique strengths, and creating expanded business from existing clients, in addition to the solid acquisition of new accounts through the Group's unique "One P&L" business model for its international business operations, and because business in the digital network domain is growing steadily. Furthermore, in the previous fiscal year we conducted a variety of M&As that contributed to the acquisition of necessary resources and enhanced competitiveness as a foundation for future growth, beginning with the acquisition of Merkle Group Inc., in the U.S.

Going forward, we will engage in global developments to strengthen our digital domain and content businesses, while at the same time making efforts to establish and enhance a competitive global network through the utilization of M&As.

(2) Evolving and expanding in the digital domain

Gross profit in the Japanese digital domain on a 2016 calendar year basis increased 8.6% year on year, continuing to achieve growth.

Outside of Japan, the Group acquired resources contributing to growth in various digital domain sectors in the fiscal year under review, including some large M&As. Due to M&As and internal growth, the gross profit of the international business operation in the digital domain increased 15.7% on a 2016 calendar year basis

As a result, the digital domain ratio across the entire Group reached 35% on a 2016 calendar year basis, achieving the goal of 35% or higher targeted in the fiscal year ending December 31, 2017.

Under the accelerated digital shift in client marketing activities, needs in the digital domain are becoming increasingly diversified and advanced in the advertising industry. These needs include the following:

- Programmatic buying systems in the media buying domain,
- Digital solutions including creative materials and contents, and
- Data analysis that contributes to business decision-making and consumer engagement strategies

As a result, the role played by the advertisement agency continues to expand. Given these circumstances, the Group will continue to proactively engage in M&As and work to improve its capabilities and quality of service.

Moreover, last year, with regard to confirming the appropriateness of questionable projects within digital advertising services provided in Japan, Dentsu and some of its domestic Group companies solicited the advice of outside experts (certified fraud investigators and certified public accountants) to assist Dentsu's in-house investigation committee that included outside experts (lawyers) to ascertain and verify the status of unsuitable business practice, investigate the cause of these occurrences and formulate measures to prevent future occurrences. One of these prevention measures involved the introduction of a mechanism for the independent verification of orders, implementation and billing pertaining to digital advertising at the beginning of September 2016 with the aim of thoroughly preventing human errors and unsuitable business practice within digital advertising work. Also, in light of issues revealed during subsequent investigations, we launched various measures to prevent recurrence, such as business process improvements and staff increases in relevant departments in an attempt to eradicate the causes of unsuitable business practice. Although this issue is not expected to have a material impact on business results, we will continue to proactively engage in efforts, such as improved operational accuracy within domestic digital advertising services, to realize higher quality, higher added value digital advertising services.

(3) Re-engineering business processes and improving profitability

Despite an increase in expenses related to technology investments in international business operations, the effect of ongoing cost control measures resulted in a consolidated underlying operating margin of 21.1% on a 2016 calendar year basis.

While aiming for top line growth in the Japan and international businesses, the Group achieved the goal of an "Underlying operating profit margin of 20% or higher" in fiscal 2016, one of the fiscal 2017 objectives targeted in the medium-term management plan. However, in the Group's Japan business, due to the aforementioned digital domain issues, we recognize the necessity of conducting ongoing business process improvements and are currently creating and implementing a roadmap in light of these efforts aimed at realizing sustainable growth in this business.

(4) Further reinforcing the business platform in the core Japanese market

The Group's greatest strength, its solid business platform in Japan, remains unchanged. To enhance competitiveness, we are deepening specialization focused on the priority digital and promotion domains while working diligently to improve profitability. As a result, in the fiscal year 2016, the Japan business achieved growth in gross profit and underlying operating profit.

In Japan, where consumer behavior patterns are undergoing rapid changes, online and offline consumer behavior data are becoming increasingly useful as companies continue further incorporate this information into their marketing activities. In light of these environmental changes, the entire Group continues to work on strengthening digital solutions capabilities, including those in the marketing intelligence domain, while further enhancing systems.

In addition, the Group is strengthening its competitiveness in the mass media business through collaborations with leaders in the media content domain and efforts to establish new revenue models and enhance value in a diverse range of media. Furthermore, the Company will work to increase its problem-solving capabilities and profitability in a greater number of domains, in an effort to evolve into a "partner" able to support the success of clients from a variety of angles.

Additionally, the Company will continue to provide support for the formulation of marketing plans and sponsorship sales at a variety of sporting events.

As mentioned above, the Group has engaged in a variety of measures to achieve the medium-term management plan. As a result, taking a comprehensive view that includes exchange rate fluctuations last year, in fiscal 2016 we believe we achieved the target levels established for fiscal 2017 overall.

At the same time, from last year, there is increasing uncertainty and fluidity in global conditions that has made the structural reform of our Japan business an urgent matter. To this end, the Group recognizes the urgency and appropriateness of formulating and presenting a new management plan based on a medium-term perspective under a new management structure instead of the current medium-term management plan. The Group is promoting the rapid formulation of this plan and will present the new medium-term management plan to stakeholders as soon as possible.

Dentsu was investigated by the relevant authorities regarding labor management-related issues, and on December 28, 2016, the Company as a corporate entity and one of our employees was referred to prosecutors by the Tokyo labor bureau on suspicion of violating the Labor Standards Act. We take these charges very seriously.

Going forward, the Company will position employees as the top management priority, making the protection of each and every employee more important than anything else. We now recognize that an environment enabling all employees to work with healthy minds and bodies, as well as an environment facilitating personal growth through various workstyles in response to diverse values, to be the most important factors enabling Dentsu to achieve sustainable growth. To realize this kind of labor environment, we are promoting labor environment reforms in recognition of the role and responsibilities the Company should fulfill in society.

In light of urgent issues focused on appropriate workloads, ideal organizational management, a review of all systems, and a redefining of corporate culture, at present we are making every effort to effectively promote thorough legal compliance and measures under the supervision of a full-time executive officer aimed at labor environment improvements and the eradication of long working hours to prevent similar occurrences in the future. These efforts are primarily driven by the Working Environment Reforms Commission established in November 2016. In terms of progress and efficacy, an outside expert has been appointed to the Supervisory Board to conduct ongoing verifications, the results of which will be disclosed as appropriate.

Finally, we will continue to engage in CSR activities globally.

Based on the "Dentsu Group Medium-term CSR strategy 2020" formulated in 2015, the Group is promoting activities in pursuit of targets to be achieved by 2020 in four key domains including environmental conservation. In recognition of these efforts, this fiscal year we were selected for the first time for inclusion in the Dow Jones Sustainability Asia Pacific Index (DJSI Asia/Pacific), a global socially responsible investment index.

In June 2016, in response to a call from the United Nations Secretary General, Dentsu announced Sustainable Development Goal (SDG) initiatives in collaboration with the five largest advertising agencies in the world. This campaign, called Common Ground, is a groundbreaking initiative that approaches global social issues through cooperation overriding competitive business relationships.

Moving forward, we plan to continue efforts to enhance corporate value by augmenting desirable CSR activities as a leading global group in the communication domain.

Analysis of Capital Resources and Cash Liquidity

Assets, Liabilities and Equity

As of December 31, 2016, total assets increased by 89,155 million yen, liabilities increased by 209,937 million yen, and total equity decreased by 120,782 million yen compared to the previous consolidated fiscal year due to the impact of business combinations and other factors.

Cash Flows

As of December 31, 2016, cash and cash equivalents (hereinafter "cash") amounted to 242,410 million yen (263,322 million yen was posted at the end of the previous consolidated fiscal year). As net cash provided by operating activities exceeded net cash used in investing activities and net cash provided by financing activities, cash at the end of the consolidated fiscal year under review decreased 20,911 million yen from the end of the previous consolidated fiscal year.

Cash flows from operating activities

Net cash provided by operating activities amounted to 143,585 million yen (provided 69,554 million yen in the previous consolidated fiscal year), primarily due to recording of profit before tax.

Cash flows from investing activities

Net cash used in investing activities amounted to 156,161 million yen (used 61,203 million yen in the previous consolidated fiscal year), primarily due to purchase of investments in subsidiaries.

Cash flows from financing activities

Net cash provided by financing activities amounted to 2,539 million yen (used 95,666 million yen in the previous consolidated fiscal year), primarily due to a net increase in short-term borrowings.

Capital Requirements

The Group's principal working capital requirements are payments for the purchase of advertising time and/or space and the production of advertisements, as well as personnel costs and other SG&A expenses.

In recent years, capital requirements have increased for investments in the digital and global domains in the course of exploring different from existing advertising opportunities.

Financial Policy

The Group's primary source of funds is cash generated from internal reserves, short-term borrowings and the issuance of commercial paper. The Group has generally had positive working capital (current assets minus current liabilities) on a consolidated basis. In the previous fiscal year and the fiscal year under review, the Group's working capital recorded positive amounts of 129.4 billion yen and 18.8 billion yen, respectively.

To ensure short-term liquidity, Dentsu established a bank credit line of up to 50.0 billion yen via a syndication arrangement. Also, Dentsu Aegis Network established a bank credit line of 500 million pounds (approximately 71.5 billion yen) as a contingency fund. In addition, to improve cash efficiency within the Group, a cash management system (CMS) was introduced so that Dentsu could borrow cash from domestic consolidated subsidiaries. A Groupwide finance system is now in place that enables nearly all domestic consolidated subsidiaries that require funding to borrow funds acquired for this purpose from other domestic consolidated subsidiaries with excess cash. Also, a global CMS has been introduced at Dentsu Aegis Network, through which overseas cash is consolidated in London.

The Japanese rating agency Rating and Investment Information, Inc., or R&I, has assigned a rating of AA- to Dentsu's long-term debt and a rating of a-1+ to its short-term debt.

Operating and Other Risks

The operating results, share price and financial position of Dentsu and, by extension, the Dentsu Group are subject to various risks, as described below.

Any forward-looking statements in the following discussion are based on the judgment of management as of the date of filing the securities report.

Overall Industry-related Risk

Risk related to fluctuations in the economic and business environments

The financial results of the Dentsu Group and other companies in the advertising industry are highly susceptible to changes in the market and business conditions because many advertisers adjust their spending in response to changes in these conditions.

Management has taken steps, such as diversifying the types of services the Group provides and geographic regions in which the Group operates, to reduce exposure to the impact of fluctuations in economic and business environments. Nonetheless, the Group's financial results may be influenced by macroeconomic trends in Japan and fluctuations in the operating environment of key domestic industry sectors that have significant advertising expenditures. In addition, changes in business conditions outside Japan, such as an economic slowdown or exchange rate fluctuations, could also adversely affect business conditions in Japan, and therefore adversely affect the results of operations of the Group's business in Japan.

The Great East Japan Earthquake that occurred in March 2011 adversely affected the Japanese economy due to supply chain disruptions, electricity shortages and other factors. While economic and business conditions in Japan have improved since then, there is no assurance that conditions may not deteriorate again in the future, including as a result of future earthquakes or other natural disasters.

With the acquisition of the major British advertising agency Aegis in March 2013, the proportion of the Group's gross profit accounted for by its operations outside of Japan increased significantly, to 54%, in fiscal 2015. With this development, downturns in the economies and business environments of the principal markets in which the Group operates outside of Japan could have an increased adverse impact on its overall results of operations.

Risk related to technological innovation and structural changes in the media

Developments in technology and structural changes in the media are having an increasing impact on the Dentsu Group's business. According to 2016 Advertising Expenditures in Japan (issued by Dentsu), Internet advertising expenditures have continued to grow since the first survey in 1996 and have reached a level surpassing the amounts allocated to newspaper, magazine or radio advertising, which are three of the four traditional mass media (newspapers, magazines, radio and television).

Management believes that the development of Internet-based and other new media advertising should contribute to expanding the overall advertising market by generating synergies between advertising in the four traditional mass media and such new advertising. The Dentsu Group also believes that it has already secured a leading position in Japan not only in advertising in the four traditional mass media but also in Internet advertising, and the Group continues to seek to explore and exploit further business opportunities.

Nevertheless, if the Group cannot cope appropriately with changes in the media structure associated with the rapid pace of technological innovation, its results of operations could be adversely affected.

Risk related to shortfalls in financial targets and other goals

Pursuant to the Dentsu Group's new medium-term management plan—Dentsu 2017 and Beyond—the Group has set financial targets and other goals to be achieved by the fiscal year ending December 31, 2017. For example, the Group intends to continue to increase the proportion of its revenue from business outside of Japan by enhancing and extending its new global network formed with the acquisition of Aegis. However, the Group's ability to achieve its financial targets and other goals is based on a number of underlying assumptions, including assumptions regarding factors beyond its control such as growth in advertising expenditures globally, foreign currency exchange rates and interest rates, as well as general economic growth rates of countries in which the Group operates. If any of these assumptions proves to be inaccurate, the Group may be unable to achieve its financial targets and other goals. In addition, there is no assurance that management will be able to successfully implement the medium-term management plan.

Risk related to common business practices

In Japan, Dentsu Group companies are liable for payment to media companies regardless of whether they receive payment from their clients. This practice exposes the Group to the risk of payment default by advertiser clients, including as the result of the bankruptcy of clients. An increase in payment defaults by clients could adversely affect the Group's results of operations. The nature of the advertising business is such that sudden changes in advertising proposals and actual advertisements are frequent. The Group strives to preclude problems related to work for clients through measures such as encouraging the conclusion of basic written contracts with them, but unforeseen events or disputes with clients may arise.

Overseas, especially in Europe and the Americas, relationships between advertisers and advertising agencies are usually exclusive within a particular industry In Japan, however, these relationships are typically less exclusive. Accordingly, the Dentsu Group, like other advertising agencies in Japan, handles multiple clients in a single industry. If the practice in Japan were to change in favor of exclusive relationships, and if the Group's efforts to respond to such a change were ineffective, its results of operations could be adversely affected.

Competition-related Risk

Risk related to competition among advertising agencies

The Dentsu Group faces increasing competition from advertising agencies in Japan and overseas.

In Japan, mergers among domestic advertising companies or other reorganizations of the domestic industry, or further entry into the market by large global advertising companies, could alter the structure of Japan's advertising industry and increase the competitive pressure that the Group faces. Going forward, the Group's results of operations could be adversely affected by increased competition to secure clients if the Group is unable to respond effectively to changes in the structure of the industry or standard business practices prompted by such developments.

Outside of Japan, the Group competes with large global advertising companies, some of which have greater geographic scope and greater financial, human and other resources than the Group, as well as with smaller agencies that specialize in one or more countries or local markets. To the extent that the Group is not able to remain competitive and obtain and retain key clients, its results of operations may be adversely affected.

Risk related to competition from new market entries and from adjacent industries

The rapid expansion and diversification of the advertising field is giving rise to competition from an increasing number of companies in adjacent industries, including general trading and consulting companies. Fields related to Internet advertising and social networking services are also seeing a sharp increase in the number of new market entrants, and the Dentsu Group competes with these companies in the development and expansion of new businesses. If the Group is unable to respond effectively to client needs in such business domains from either a service or a cost perspective, or if the entrance of new companies into these new markets suddenly causes rapid changes in customary advertising business practices, the Group's results of operations could be adversely affected.

Risk Related to Advertisers and Media Companies

The Dentsu Group has formed business ties with major advertisers in Japan and has maintained stable, long-term relationships with a large majority of its current clients.

The Group has also established strong relationships with Japan's mass media companies, which enhances its ability to coordinate operations and sales activities between advertisers and media companies, and thereby facilitate transactions.

However, if the Group is unable to provide services that match the needs of existing or new advertisers and media companies, the Group may be adversely affected, including by the termination of business relationships, the reduction of accounts or unfavorable changes in the terms of business.

In recent years, advertisers have sought to consolidate their media service activities with one advertising agency to boost advertising efficiency and reduce costs. For this and other reasons, the Group and other advertising companies have experienced a decrease in the profitability of mass media advertising services. If this trend persists, the Group's results of operations could be further adversely affected.

Risk Related to Efforts to Reinforce Domestic Service Capabilities

Risk related to the development of information technology processes and databases

The Dentsu Group is currently involved in research and development on information technology processes and databases that verify the effectiveness of clients' advertising activities and marketing budgets. Through these efforts, management seeks to bring latent demand to the surface and expand its share of the Japanese advertising market. However, it is unclear if or when the results of these efforts will be marketable and put to practical use. Moreover, even if the Group is able to develop marketable services from its R&D activities, these services may not produce the results the Group expects, especially if the needs of clients have changed significantly or technological challenges preclude widespread use of the services.

Risk related to investments in media and Internet advertising businesses

To reinforce the Dentsu Group's position in the media markets and otherwise expand its business, the Group has made investments in the four traditional mass media, OOH media (out-of-home media such as transit and billboard) and satellite media (broadcast and communication satellites), as well as in related research and business development programs. However, if demand for media advertising becomes stagnant or competition in the media advertising market intensifies, profits and other business results may not be sufficient to generate the return the Group expects from these investments in R&D and commercialization.

In the Internet advertising domain, as advertising methods diversify and demands from clients expand, the Dentsu Group has been actively establishing alliances with leading, specialized agencies as well as investing in other specialized companies and technologies. These moves support the Group's efforts to further promote and propose cross-media campaigns that are aimed at creating effective synergies among multiple media and creative outlets that are effective in light of target consumers' behavior patterns. The Group is also focusing on performance-based advertising, a method of ad delivery which utilizes platforms that employ ad technologies processing vast amounts of data to provide automatic or instantaneous optimization of advertising. However, if the Group's efforts fail to adequately address the rapid progress in technologies and services associated with the Internet advertising domain, the Group may be unable to realize its initially expected return on these investments.

Risk related to expansion of the promotion business
The importance of promotional activities has been rising for advertisers, and the market is expanding. Taking advantage of this opportunity, the Dentsu Group has established several specialized companies in promotion-related fields such as point-of-purchase marketing, flyer production, direct business and client access in order to expand its future promotion business. However, if demand for these services falls short of expectations, or if the Group is unable to maintain competitiveness with other solutions providers, the Group may not realize the return on investments that it expects.

Risk Related to Content Business

The Dentsu Group actively invests in the acquisition of rights to, and in the production of, films, television programs, sports events and music, and seeks to generate profits from the production, distribution, sale and licensing of films and other content as well as from the sale of sponsorships, broadcasting rights and content-related advertising. However, these projects may extend over several fiscal years and require significant acquisition costs and financial commitments. In addition, media that provide content have been diversifying in recent years. Moreover, the success of the Group's content business depends primarily upon acceptance by the general public, which can be difficult to predict. Therefore, if these investments in content or events do not develop as planned or do not realize the benefits expected, the Group's results of operations may be adversely affected.

Risk Related to International Businesses

Risks related to international business development
With the acquisition of Aegis, the Dentsu Group's global operations have expanded to over 140 countries and regions. The Group's global operations are subject to a number of risks, including but not limited to the following:

- Difficulties in monitoring and coordinating operations in such a large number and wide range of jurisdictions;
- Heightened exposure to any downturn affecting the global economy;
- Risks related to foreign laws, regulations and policies, including capital and exchange controls;
- Differences in, or conflicts among, the taxation regimes in the different jurisdictions in which the Group operates;
- Changes with respect to taxation, including impositions or increases of withholding and other taxes on remittances and other payments by the Group's overseas subsidiaries;
- Fluctuations in foreign currency exchange rates;
- Varying standards and practices in the legal, regulatory and business cultures in which the Group operates, including potential inability to enforce contracts or intellectual property rights and restrictions on employment matters;
- Trade restrictions and changes in tariff;
- Risks related to political instability and uncertain business environments;
- Changes in the political or economic relationship between Japan and the other countries and regions in which the Group operates;
- Acts of terrorism, war, epidemics and other sources of social disruption; and
- Difficulties associated with managing local personnel and preventing misconduct by local third-party alliance partners.

Any one or more of these or other factors could increase the Group's costs, reduce its revenues or disrupt its operations, with possible material adverse effects on its business, financial condition and results of operations.

Risk related to impairment losses on goodwill and other intangible assets
The Dentsu Group carries significant amounts of goodwill and other intangible assets on its balance sheet, particularly as a result of the acquisition of Aegis. The Group is to recognize impermanent losses when the carrying amount of an asset is not recoverable. The recognition of such impairment charges may adversely affect the Group's business, financial condition and results of operations.

Risk Related to Maintaining and Developing Human Resources

The growth potential and competitiveness of the Dentsu Group are highly dependent upon attracting, retaining and developing excellent human resources. Therefore, Group companies strive to attract the necessary talent by hiring a stable number of new graduates and by recruiting mid-career professionals with expertise and experience that will make an immediate contribution. At the same time, the Group endeavors to promote personnel development by offering training opportunities according to the position and ability of each individual. However, these efforts could be sidetracked for all sorts of reasons, making it difficult to attract exceptional people or keep them within the Group. If this were to occur, the Group's growth potential and its competitive edge could be adversely affected.

Moreover, the Group is continuing to address issues inherent in the management of a greater number of employees in diverse cultural and geographic areas, particularly with the integration of a large number of new overseas employees in connection with the acquisition of Aegis. There can be no assurance that the Group will be able to attract or retain key employees and successfully manage them. The Group's inability to do so could disrupt its business and have a material adverse effect on its financial condition, results of operations and competitive position.

Risk Related to Reliance on Information Technology Systems

The Dentsu Group relies on information technology systems and infrastructure to process transactions, summarize results and manage its business, including maintaining client marketing and advertising information. The Group's information technology systems are potentially vulnerable to system failures and network disruptions, malicious intrusion and random attack. Likewise, data security incidents and breaches by employees and others with or without permitted access to its systems may pose a risk that sensitive data may be exposed to unauthorized persons or to the public. Additionally, the Group utilizes third parties to store, transfer or process data. While the Group has taken prudent measures to protect its data and information technology systems, there can be no assurance that its efforts will prevent system failures or network disruptions or breaches in its systems, or in systems of third parties the Group uses, which could adversely affect its results of operations.

Risk Related to Legal or Regulatory Changes

Advertising companies in Japan, including those under the Dentsu Group umbrella, are subject to a number of laws and regulations, including the Act against Delay in Payment of Subcontract Proceeds, Etc. to Subcontractors and the Act on the Protection of Personal Information. At the current time, management does not anticipate that these laws and regulations will have any material impact on the Group's business. However, the financial results of the Dentsu Group and other advertising companies could be adversely affected if existing laws or regulations governing the advertising activities of advertisers or the format or content of advertisements are strengthened, if new laws or regulations are introduced, or if existing laws and regulations are reinterpreted.

Members of the Group handle personal and other advertiser information in the course of doing business. The Dentsu Group's information security system is certified to international standards, and the utmost care is given to safeguarding information entrusted to the Group. However, in the unlikely event of an information leak or other such incident occurring, the Group's credibility could be severely compromised. This could adversely affect its financial results.

Risk of Litigation

The Dentsu Group could become involved in litigation brought against it directly or indirectly in association with the execution of business by members of the Group, including claims by clients, organizations, consumers or owners of intellectual property.