Management's Discussion and Analysis

Business Overview

Looking back at the state of the economy during the period under review, emerging economies, particularly China, stayed strong on the back of increasing domestic demand, while developed economies followed a recovery trend as a whole, despite a slowdown due to fiscal concerns in the euro zone. In Japan, in spite of signs of moderate economic recovery, the yen's continued appreciation throughout the year, coupled with the massive damage from the Great East Japan Earthquake that occurred on March 11, 2011, has given rise to uncertainties about the future.

Under these circumstances, the Brother Group's consolidated net sales increased 12.7% over the previous year to ¥502,830 million primarily because of substantially higher sales of machine tools and industrial sewing machines following sharp market recovery, despite the negative effect of the stronger yen. Although there was the negative effect of exchange rates and cost increase of raw materials, substantially higher sales and improving sales composition pushed up operating income by 35.5% year-on-year to ¥36,092 million. Net income chalked up a year-on-year increase of 33.7% to ¥26,238 million.

Performance by Business Segment

For details about performance by business segment, please see "Review of Operations," Pages 10-11.

Fund Procurement, Liquidity and Cash Flows

The Brother Group's financial policies ensure flexible and efficient funding and maintain an appropriate level of liquidity for current and future operating activities. In accordance with these policies, we have created a cash management system to optimize the group-wide use of cash held by individual companies. We also maintain open lines of credit with several banking institutions to complement existing liquidity on hand. Through these measures, we have established a system to correct the uneven distribution of funds and minimize the overall borrowing needs of the Group.

Liquidity Management

The Group's liquidity on hand consists of cash and cash equivalents and the unused portion of open commitment lines of credit. As of March 31, 2011, cash and cash equivalents totaled ¥65,101 million. We maintain commitment lines of credit with several financial institutions for a combined amount of ¥30,000 million, and the entire amount in open lines of credit was unused as of March 31, 2011. This total plus cash and cash equivalents was ¥95,101 million at fiscal year-end. Taking into consideration seasonal funding requirements, debt payable within one year and business environment risks, we believe that we have sufficient liquidity on hand to support our operations through a whole year.

Fund Procurement

As a basic rule, we procure working capital and other short-term funding in debt payable within one year that is funded with local currency. The basic policy on long-term funding for manufacturing facilities is that funds should come from internal reserves, long-term fixed-rate borrowings and corporate bonds. As of March 31, 2011, short-term borrowings stood at ¥8,637 million, primarily denominated in yen. The balance of long-term debt (including current portion of long-term debt within one year) was ¥21,728 million, all procured in fixed-rate debt procured in yen. Outstanding corporate bonds stood at ¥15,500 million.

We have obtained credit ratings from Rating and Investment Information, Inc. (R&I). As of March 31, 2011, R&I assigned the Group's long-term bonds and issuer credit "A" ratings and its commercial paper an "a-1" rating. We consider consistent ratings important in maintaining our access to credit and capital markets.

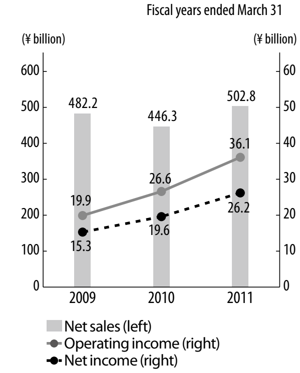
The Brother Group believes that its liquidity on hand, including open commitment lines of credit, and sound corporate finance structure, on top of its ability to generate cash flows from operating activities, make it possible to secure working capital as well as funds for capital investment and R&D investment to maintain the Group's growth.

Cash Flows

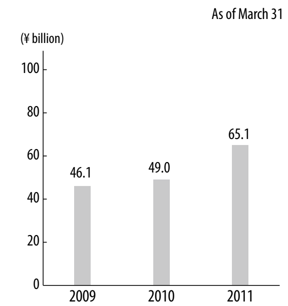
Cash flows from operating activities

Cash flows from operating activities provided net cash and cash equivalents amounting to ¥49,489 million, ¥859 million less than ¥50,348 million in the previous year. This was primarily because of increases in inventories and income taxes-paid despite an increase in income before income taxes and minority interests.

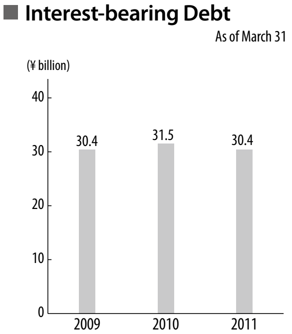
Operating Results



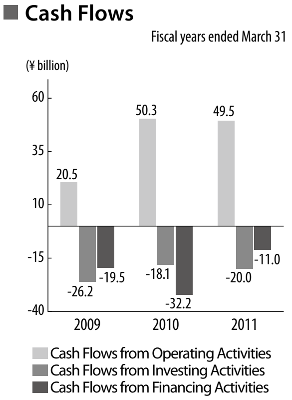
Cash and Cash Equivalents, End of Year



Interest-bearing Debt



Cash Flows



Cash flows from investment activities
Net cash used in investing activities amounted to ¥20,043 million, ¥1,982 million more than ¥18,061 million used in the previous year, reflecting an increase in disbursement for purchases of property, plant and equipment.

Cash flows from financing activities
Net cash used in financing activities totaled ¥10,950 million, ¥21,223 million less than ¥32,173 million used in the previous year. Interest-bearing debt resulted in ¥2,536 million in disbursements, ¥24,429 million less than in the previous year. Cash dividends paid used ¥5,912 million, ¥537 million more than in the previous year.

As a result of these activities, as well as the exchange rate fluctuations affecting the yen conversion value of cash and cash equivalents of overseas consolidated subsidiaries, cash and cash equivalents as of March 31, 2011, amounted to ¥65,101 million, an increase of ¥16,070 million over a year earlier.

■ Outlook for Fiscal 2011

We expect the business environment in fiscal 2011 to stay uncertain due to the anticipated lingering impact of the Great East Japan Earthquake despite gradual growth expectations of developed economies on top of the robust growth of emerging economies.

Despite these conditions, the Brother Group will aim for growth in fiscal 2011, the first year of the new mid-term business strategy "CS B2015." We expect net sales to increase over the previous year given strong demand for our products, but we are likely to see lower profits than the previous year. Although the earthquake caused no direct damage to the Group, we expect to feel the impact on the production of some of our products associated with difficulty in procuring parts and components and also the effect on the online karaoke business in Japan of shorter operating hours at stores owing to power-saving requirements. Though the business outlook going forward still involves opaque factors, the Brother Group as a whole will exert efforts to keep the impact of these factors to a minimum.

■ Business and Other Risk

The following items may impact Group businesses, operating performance and financial conditions. Forward-looking statements reflect the Group's judgment as of March 31, 2011.

(1) Market Competition
In printing and other operations, the Brother Group cultivates business in many markets where it faces stiff competition. Competitors could allocate more management resources to their business than the Group does, new competitors could enter the market and competition could intensify as a result of alliances or collaboration among competitors. As a result, the Group may be unable to maintain its current market share, adversely affecting Group performance.

(2) Acquisition of Human Resources
The Brother Group places a special emphasis on research and development, aiming to differentiate its products from its competitors' through the accumulation of technology and expertise. However, competition for human resources is rising. In the event that ongoing recruitment and employment of skilled human resources becomes more difficult, the Group may become unable to deploy sufficient human resources in research and development, which could lower the competitiveness of its products, adversely affecting Group performance.

(3) Intellectual Property Rights
We conduct business operations by concluding license agreements with other companies on patents and other intellectual property rights as necessary. The balance of royalty revenues and payments based on such license agreements could cause fluctuations in the Group's operating performance and also become constraints on business operations depending on the terms of such agreements. Furthermore, there are limits to the degree to which proprietary technology acquired through research and development can be protected, and the potential exists for third parties to infringe upon our intellectual property rights and manufacture and sell counterfeit products. Other companies may file lawsuits against the Group with regard to intellectual property rights, which could affect the Group's performance. The Group provides appropriate rewards to in-house inventors based on the Invention Incentive Scheme. Despite this, there is the possibility of litigation with inventors over compensation.

(4) Product Quality Control
To provide high-quality, attractive products, the Group has established a production management system with rigorous product quality control standards. However, not all products are free from defects, and there is no guarantee that no problems will arise as a result of product safety or quality issues. In the event that significant problems arise, substantial costs may be incurred, brand image and reputation may deteriorate, and customer willingness to purchase Group products may fall, adversely affecting Group's performance.

(5) Exchange and Interest Rates
The Brother Group conducts a high percentage of its manufacturing and sales overseas, and exchange rate fluctuations could affect foreign currency transactions. To reduce this risk and improve the link between foreign currency transaction receipts and payments, the Group utilizes forward exchange contracts and other instruments to reduce short-term risk. However, currency appreciation in China, Southeast Asia or other regions where the Group operates major manufacturing facilities could cause procurement and production costs to rise, and mid- to long-term exchange rate fluctuations could affect its financial condition.

To reduce interest rate fluctuation risk, the Group endeavors to raise funds at fixed interest rates, and employs interest rate swaps and other financial instruments. Nevertheless, higher market interest rates could raise fund procurement costs.

(6) Raw Materials Cost Increases

Higher prices on resins, steel plates and other raw materials push up the cost of manufacturing Group products. The Group may be unable to pass on such rises through higher product prices, or to fully absorb higher costs by reducing expenses or boosting efficiencies, all of which have the potential to impact future earnings.

(7) Statutory Regulations

The Group conducts its business according to the laws and regulations of each country in which it operates. In addition to strengthening the internal controls that ensure compliance throughout the Group, the Group has created a risk management system. If an event arises where the Group is unable to comply with regulations, Group business activities may be restricted, which may result in cost increases.

(8) Information Network

The Brother Group employs a network to manage information related to production and sales management, as well as financial matters. The Group expects its information storage and equipment maintenance systems to be fully effective. However, network disconnections and system stoppages may adversely affect business activities. Furthermore, although the Group takes ample precautions to prevent infections from computer viruses and hackers, in the event of infiltration or attacks from the outside, depending on the scale of the interruption, business activities may be adversely affected.

Reflecting its internal controls, while maintaining and enhancing the reliability of financial information, the Group is also involved in ongoing quality improvements in development, maintenance and operation from the perspective of overall IT controls. However, in the event that procedural guidelines are not followed, a situation may arise where the Group is unable to guarantee the reliability of its financial information.

(9) Information Security

The Brother Group, having established the Information Management Committee and defined regulations for the management of information, has created information security operation rules for ongoing information risk management activities. The Group makes a thorough effort to prevent the leakage of personal and confidential information through internal training based on these operational rules. It controls access to personal information and maintain an access log to avoid the mishandling of this information. However, if personal information is leaked nevertheless, the Group may lose the confidence of its customers and its brand image may suffer, which could adversely affect Group business activities and performance.

In addition, to provide comprehensive customer services, the Group established websites that provide customers with product information and support. It makes an effort to maintain an adequate level of security on this website, but in the event of an unforeseen attack from the outside, website content falsification or the addition of links to fraudulent websites may adversely affect its business activities.

(10) Future Business Developments and Forecasts

To expand its operations by growing existing businesses and developing new business, the Brother Group engages in research and development and strategic investment, including M&A.

The launch of new businesses may involve risk inherent to that particular business, which may adversely affect overall performance.

Also, M&A and other activity may entail unforeseen costs involved with the merging of operations that prevent the realization of initially forecasted returns on investment, which could adversely affect Group performance and financial conditions.

(11) Natural Disasters and Other Threats

The majority of the Brother Group's manufacturing and sales facilities is located overseas. Our main manufacturing facilities are in China, Malaysia and Vietnam, and the Group continues to establish sales bases in countries throughout the world. To mitigate damage from natural disasters at these facilities, the Group has formulated response procedures in the event of fire, earthquakes, typhoons and other disasters. However, unforeseen events (such as war, terrorism, outbreaks of infectious diseases, strikes or other labor disputes, and natural disasters of unforeseeable scale) may cause social unrest that can damage production and sales, including parts procurement systems, which could adversely affect the Group's operating performance. At the Group's headquarters in Japan, the Group has established a crisis management system in the event of a major earthquake in the Tokai region. However, there is a possibility that the damage resulting from an earthquake may exceed the anticipated severity.