Review of Operations

TIRE group

Sales in the Tire Group declined 8.1% in fiscal 2010, to ¥367.5 billion, and operating income rose 106.9%, to ¥20.5 billion. Sales were generally weak throughout the first half of the fiscal year but picked up in the fourth quarter. The improvement in profitability resulted from declines in raw material costs and from progress in paring costs. Note that overseas sales included in the Tire Group’s fiscal results are for the calendar year ended three months before the fiscal year-end.

We project a rebound in sales and a decline in operating income in the Tire Group in fiscal 2011. Our projections call for sales to rise 12.1%, to ¥412.0 billion, as demand recovers in principal markets. However, we project a decline of 34.0% in operating income, to ¥13.5 billion, on account of resurgent prices for raw materials.

J A P A N

Solid replacement demand for high-end and middle-market tires

Our Japanese business in replacement tires in fiscal 2010 was basically unchanged from the previous fiscal year in unit volume and in sales value. That performance mirrored overall demand, which was essentially unchanged despite signs of recovery in the fiscal second half.

We made the most of the lackluster business environment by optimizing our sales portfolio. That included product launches in high-end tires and a strategic emphasis on high-end and middle-market tires in marketing. The ADVAN dB, launched in July 2009, is our best-ever offering for providing a quiet ride. Sales benefited from the excellent market reception for that product and from continuing strong sales of our DNA GRAND map, for large minivans, and of our fuel-saving DNA Earth-1. Those products demonstrated the potential for winning business with distinctive offerings, even amid the general shift toward lower-priced tires.

Our unit sales of truck and bus tires declined in fiscal 2010. We improved our sales portfolio, however, by achieving sales growth with the fuel-saving, highly durable tires of the ZEN series. In addition, we augmented the ZEN series with a studless snow tire, the ZEN 902ZE.

We project little change in unit volume and sales value in fiscal 2011 in our Japanese replacement
tire business. That projection reflects our expectation that demand, too, will change little. Business opportunities will arise, however, following tire manufacturers’ adoption in January 2010 of unified labeling standards for rolling resistance and wet-surface grip. The new standards promise to stimulate demand for environmentally oriented tires. We will emphasize our environmental credentials in working to strengthen our brand image, to increase the weighting of high-end and middle-market tires in our sales portfolio, and to thereby fortify our profitability.

The BluEarth AE-01, launched in July 2010, is an important new middle-market tire developed to secure large sales volume. It has qualified for the AA ranking for rolling resistance under the new labeling guidelines, which indicates excellent fuel economy. And its cost performance is superb. We will offer the BluEarth AE-01 in an increasing number of sizes, and we plan for it to become a core product for us within three years.

In truck and bus tires, we will continue to cultivate demand for the ZEN series. And we will reinforce our tire business through other measures. We will promote our HiTES system, for example, for monitoring the air pressure and air temperature inside tires in real time. We will also develop business in marketing retreaded tires.

The BluEarth AE-01: a showcase of advances in reducing rolling resistance destined to anchor our product line in Japan and in other markets

Declining demand for original equipment tires amid slumping vehicle production

Our Japanese business in original equipment tires declined in unit volume and in sales value as automakers cut back production amid shrinking exports. Demand began recovering, however, in the fiscal second half. Leading the nascent recovery were strong domestic sales of small cars and hybrid vehicles, spurred by tax incentives for purchases of fuel-saving models. We stepped up our marketing aimed at winning supply contracts for environmentally oriented vehicles, and we succeeded in winning factory fitments on two high-profile hybrid models: the Toyota Prius and the Honda CR-Z.

In fiscal 2011, we expect growth in unit volume and in sales value in our Japanese business in original equipment tires. Vehicle production volume is recovering, and we are expanding our business in original equipment tires for environmentally oriented vehicles. At the same time, we are redoubling our emphasis on sound profit margins in pursuing supply contracts.
NORTH AMERICA

Sales decline despite growth in replacement tires as original equipment demand slumps

We posted declines in unit volume and in sales value in our U.S. tire business in fiscal 2010. Despite trade-in incentives from automakers, original equipment demand for passenger car tires weakened. We posted sales growth in the replacement sector, but the weakness in original equipment demand undermined our overall sales performance. Contributing to our sales growth in replacement tires was our Yokohama Advantage program, which provides tire retailers with sales incentives and marketing support. The number of participating retailers in that program increased during the fiscal year.

Our U.S. business in truck and bus tires focuses on the replacement market. In fiscal 2010, our sales of replacement tires for trucks and buses declined as demand sagged. We succeeded, however, in increasing our market share.

In fiscal 2011, we project growth in unit volume and in sales value in our U.S. tire business. Demand turned upward in the latter half of fiscal 2010, and we expect demand to increase overall in fiscal 2011.

Product launches are bolstering our sales momentum in passenger car tires and in truck and bus tires. Especially promising is the AVID ENVigor, a new kind of all-weather high-performance tire launched in spring 2010. The AVID ENVigor combines excellent handling with superior fuel economy.

In truck and bus tires, we are fortifying our brand image and promoting sales by emphasizing our advances in reducing environmental impact. We have earned accreditations for several products under the U.S. Environmental Protection Agency’s SmartWay program for recognizing products that reduce transport-related emissions. Our marketing highlights the excellence of our ZEN series with respect to fuel economy and to the tires’ resistance to camber wear and other kinds of wear.

Sales gains in Canada led by snow tires

We registered growth in unit volume and in sales value in the Canadian market despite flat demand. Leading that growth were sales gains in snow tires, where we were successful with purchasing incentives for early orders. Another contributor to sales growth was our newly launched AVID Touring-S all-season tire.

Canadian demand appears likely to remain steady in fiscal 2011. We are strengthening our sales organization and are recruiting new members for our sales channels. In working to increase sales, we will make the most of the sales momentum of the AVID Touring-S and the new AVID ENVigor, launched in spring 2010.
ASIAN NATIONS
BESIDES JAPAN

Unit sales growth of more than 15% in China

Our Asian tire business outside Japan grew in fiscal 2010, led by growth in passenger car tires. Underlying that growth was recovering demand in emerging economies. Our unit sales in China, our largest Asian market outside Japan, increased more than 15%. Aiming to share fully in the upturn in demand, we cultivated new business with large wholesalers and expanded business with established partners. And we recruited new members for our retailer network.

Also showing double-digit growth were our unit tire sales in India, the Philippines, the Republic of Korea, and Thailand. The sales growth in India reflected the sweeping expansion of our network of affiliated retailers. In the Republic of Korea, our sales growth occurred mainly through expanded business with retail chains of large tire outlets. A marketing company that we established in Thailand in May 2008 cultivated new sales channels and otherwise coordinated our sales growth there. The growth in the Philippines reflected a continuing combination of marketing measures.

New Thai factory for processing natural rubber begins operation

We began processing natural rubber in May 2010 at a newly built factory in the southern Thai province of Surat Thani. Demand for natural rubber, an alternative to petroleum-based synthetic rubber, is growing annually. Our new plant, with a monthly processing capacity of 3,000 tons, improves our access to reliable supplies of high-quality natural rubber. It incorporates our accumulated expertise in producing rubber of highly consistent specifications. We are counting on the plant to support advances in applications development for natural rubber, such as high-performance tires that contain an increased percentage of natural rubber.
Outlook for further growth in fiscal 2011 led by vigor in emerging economies

We project further sales growth in emerging economies in fiscal 2011, supported by expected growth in demand. The Yokohama Club network of affiliated retailers is a crucial plank in our strategy for increasing sales. And we will work in fiscal 2011 to raise the pace of growth in that network.

Our product launches will center on high-performance tires as we undertake marketing aimed at fortifying our brand image. In fiscal 2010, we launched the ADVAN NEOVA AD08, which we characterize as a “street sports tire,” and the DNA Earth-1, which offers excellent fuel economy. Upcoming product launches include the ADVAN dB, a premier offering in riding comfort.

We will continue to reinforce our marketing with supplementary activities. That will include public relations and advertising for highlighting our position as the official tire supplier to the Macau Grand Prix. It will also include participating actively in motor shows and other events in each nation.

Expanding production capacity in Thailand and China

Plant expansion projects are increasing our supply capacity in China and in Thailand. China passed the United States in 2009 to become the world’s largest automobile market, and vehicle demand there is poised to continue growing. That will mean parallel growth in demand for tires, so we are expanding our Hangzhou Plant, which produces passenger car tires. The expansion will increase the plant’s annual production capacity to 5.1 million tires by the end of fiscal 2012, from 3.0 million presently.

Our tire plant in Thailand produces tires for passenger cars and for light trucks. We will increase its annual production capacity to 4.0 million tires by the end of fiscal 2012, from 2.6 million presently. Our Thai plant exports tires to other Asian nations and to North America and Europe, as well as serving local demand. The expansion is mainly for increasing the plant’s capacity to serve growing demand in export markets.
EUROPE

Russian-led sales growth amid weakening demand
Our unit sales in Europe increased in fiscal 2010 despite adverse market trends. Demand for replacement tires weakened in Europe amid deteriorating economic conditions. Weighing notably on overall demand were downturns in the formerly robust markets of eastern Europe and Russia. Our sales increase reflected growth of more than 20% in Russia, which offset sales declines elsewhere in Europe.

Outlook for further growth in fiscal 2011 stimulated by product launches
Uncertainty clouds the economic outlook for Europe, but our sales are improving gradually throughout the region, and we expect European demand to firm in fiscal 2011. We are aiming for further sales growth in Europe and are promoting new products aggressively to achieve that aim.

The drive series is our main product line in passenger car tires in Europe, and we fortified that line in fiscal 2010 with the C.drive2. That tire, the successor to the comfort-oriented C.drive, features improved wet-surface performance. We are offering the C.drive2 in an increased number of sizes in fiscal 2011 and are promoting it in the mass-market price range.

In Russia, we are expanding our presence in snow tires, the main product category in the tire market there. We will make the most of product launches in snow tires in a bid to increase sales greatly.

Tires for minimizing environmental impact are a strategic emphasis in measures for strengthening our brand image in Europe. We fortified our European product line in fiscal 2010 with the launch of the dB super E-spec, which provides superior fuel-saving performance. And we will launch another important tire product oriented toward fuel economy in fiscal 2011.

Promoting environmentally oriented products is a European emphasis for us in truck and bus tires. We underlined that emphasis with the fiscal 2010 launch of the ZEN series, which features important advances in fuel savings and wear resistance. The ZEN series will highlight our marketing in truck and bus tires in fiscal 2011.

We have broadened our European marketing reach through a newly concluded alliance with the Italian company Marangoni Spa. Our partner is a leading supplier of retreading technologies and retreading services, and it also has solid positions in tire manufacturing and marketing. The alliance will greatly fortify our European marketing position in truck and bus tires.

Also fortifying our European presence is our new European Distribution Center, opened in Germany in April 2010. We are counting on that center to contribute to sales growth by shortening lead times in product delivery and to lower costs by consolidating our European inventories.
MIDDLE EAST
Our Middle Eastern unit sales declined in the wake of the sales surge that accompanied the previous fiscal year’s oil price spike. Tire demand turned upward in the fiscal second half, and our sales rebounded as we allocated ample product volume to the region.

We project rising demand and sales growth in the Middle East in fiscal 2011. Highlighting our marketing strategy is the scheduled launch in the gulf states of A.drive tires specially configured to withstand high temperatures.

OCEANIA
In Oceania, our unit sales declined in fiscal 2010. That decline resulted primarily from decreased shipments to automakers in Australia, who experienced production declines. We posted strong sales in replacement passenger car tires, led by our GEOLANDAR tires for sport-utility vehicles. Our sales declined in the region, however, in truck and bus tires.

Vehicle production in Australia is turning upward in fiscal 2011, and we project growth in original equipment sales. We are eyeing sales growth in passenger car tires, especially through our company-owned Tyres & More network of retail outlets. And we are readying product launches in truck and bus tires to support sales growth in that sector.

LATIN AMERICA
We posted a decline in unit sales in Latin America in fiscal 2010. A big reason for that decline was the Argentine government’s imposition of import restrictions, which diminished our Argentine business greatly. Our sales increased in Brazil, however, as the Brazilian currency appreciated and as demand expanded.

Fiscal 2011 promises to occasion resurgent sales for the Tire Group in Latin America. We will allocate ample supply capacity to serve the growing demand in Brazil, where economic expansion continues. In Argentina, we are aggressively promoting a line of studless snow tires that we launched in fiscal 2010. Our distributors throughout Latin America have bolstered their marketing capabilities impressively, and we will support their efforts by augmenting our product line in each nation. We have fortified our marketing staff for off-the-road tires in Latin America, for instance, with an eye to increasing sales.

AFRICA
Our African business centers on South Africa, and our unit sales there declined in fiscal 2010, undermined by the sharp weakening of the rand. We asserted a renewed presence in Egypt, where the government lifted an antidumping import tariff in 2009, and our Egyptian sales gained strong momentum. Our activity in Africa includes developing business in nations where we formerly lacked a market presence, and we recently began serving customers in Madagascar and in Senegal.

We are tentatively optimistic of improvement in our African sales performance in fiscal 2011. South Africa’s hosting of the soccer World Cup tournament has stimulated demand in that nation, and the rand appears to be stabilizing. In addition, we expect continuing sales growth in Egypt, which is becoming a second important market for us in Africa.