## Item 7A. Market Rate Risks

**Interest Rate Risk**

Our exposure to interest rate risk relates primarily to our investment portfolio. (See Note 5 of Notes to Consolidated Financial Statements.) Our primary aim with our investment portfolio is to invest available cash while preserving principal and meeting liquidity needs. The portfolio includes tax-advantaged municipal bonds, tax-advantaged auction rate preferred municipal bonds, commercial paper, and U.S. Treasury securities. In accordance with our investment policy, we place investments with high credit quality issuers and limit the amount of credit exposure to any one issuer. These securities are subject to interest rate risk and will decrease in value if market interest rates increase. A hypothetical 10% increase in interest rates would result in a $2.8 million and $1.5 million (less than 0.3% for both years) decrease in the fair value of our available-for-sale securities as of the end of fiscal 2000 and 1999, respectively. In addition, we have historically had the ability and have the intent to hold our securities until maturity and therefore, do not expect to recognize an adverse impact on income or cash flows, although there can be no assurance of this.

**Foreign Currency Risk**

We use forward currency exchange contracts to reduce financial market risks. Our sales to Japanese customers are denominated in yen while our purchases of processed silicon wafers from Japanese foundries are primarily denominated in U.S. dollars. Gains and losses on foreign currency forward contracts that are designated and effective as hedges of anticipated transactions, for which a firm commitment has been attained, are deferred and included in the basis of the transaction in the same period that the underlying transactions are settled. Gains and losses on any instruments not meeting the above criteria would be recognized in income in the current period. A 15% adverse change in yen exchange rates, based on historical average rate fluctuations, would have had approximately a 1.0% adverse impact on revenue for fiscal years 2000, 1999 and 1998. In fiscal 2000, we have also begun to share the yen exchange rate risk with some of our Japanese customers through risk sharing agreements. As we will continue to have a net yen exposure in the near future, we will continue to mitigate the exposure through yen hedging contracts. However, no currency forward contracts were outstanding as of March 31, 2000.

Our investments in several subsidiaries and in the UMC securities are recorded in currencies other than the U.S. dollar. As these foreign currency denominated investments are translated at each month end during consolidation, fluctuations of exchange rates between the foreign currency and the U.S. dollar increase or decrease the value of those investments. If permanent changes occur in exchange rates after an investment is made, the investment's value will increase or decrease accordingly. These fluctuations are recorded within stockholders' equity as a component of accumulated other comprehensive income. Also, as our subsidiaries maintain investments denominated in other than local currencies, exchange rate fluctuations will occur.