

## Consolidated Financial Results

### for the Fiscal Year Ended March 31, 2004

Company name: ELMIC SYSTEMS, INC.  
 Stock code: 4770  
 Stock market listing: TSE Mothers Market  
 Company domicile: Kanagawa prefecture  
 Head office: 4-59 Benten-Dori, Naka-ku, Yokohama 231-0007 Japan  
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 Date of board meeting for approving financial results: May 21, 2004  
 Accounting principle: Japanese GAAP

#### 1. Consolidated Financial Results (From April 1, 2003 to March 31, 2004)

##### (1) Financial Results

(Amounts rounded down to million yen)

	Net sales		Operating income		Ordinary income	
	¥ millions	%	¥ millions	%	¥ millions	%
Fiscal year ended March 2004	1,733	(8.2)	(77)	-	(78)	-
Fiscal year ended March 2003	1,888	(1.0)	(26)	-	(27)	-

	Net income		Net income per share (basic)	Net income per share (diluted)
	¥ millions	%	¥	¥
Fiscal year ended March 2004	142	-	29.51	-
Fiscal year ended March 2003	(392)	-	(78.81)	-

	Return on equity	Ratio of ordinary income to total assets	Ratio of ordinary income to net sales
	%	%	%
Fiscal year ended March 2004	5.2	(2.4)	(4.5)
Fiscal year ended March 2003	(14.6)	(0.8)	(1.4)

Notes: 1. Equity in earnings of unconsolidated subsidiaries:

Fiscal year ended March 2004: ¥ 11 million

Fiscal year ended March 2003: ¥ 9 million

2. Average number of shares outstanding:

Fiscal year ended March 2004: 4,816,230 shares

Fiscal year ended March 2003: 4,979,746 shares

3. Changes in accounting principles applied: None

4. The percentages shown for net sales, operating income, ordinary income, and net income represent changes from the corresponding of the same period of the previous year.

## (2) Financial Position

(Amounts rounded down to million yen)

	Total assets	Shareholders' equity	Shareholders' equity ratio	Shareholders' equity per share
	¥ millions	¥ millions	%	¥
As of March 31, 2004	3,221	2,773	86.1	576.20
As of March 31, 2003	3,210	2,690	83.8	558.55

Note: 1. Number of shares outstanding:

As of March 31, 2004:	4,815,730 shares
As of March 31, 2003:	4,816,720 shares

## (3) Cash Flows Position

(Amounts rounded down to million yen)

	Net cash provided by operating activities	Net cash used in investing activities	Net cash used in financing activities	Cash and cash equivalents at end of year
	¥ millions	¥ millions	¥ millions	¥ millions
Fiscal year ended March 2004	35	(60)	(4)	1,254
Fiscal year ended March 2003	40	(207)	(227)	1,278

## (4) Scope of Consolidation and the Application of Equity Method

Consolidated subsidiaries: 1

Unconsolidated subsidiaries accounted for under the equity method: None

Affiliates accounted for under the equity method: 1

## (5) Changes in the Scope of Consolidation and Affiliates Accounted for Under the Equity Method

Consolidated subsidiaries:

New: None

Excluded: 1

Affiliates accounted for under the equity method:

New: None

Excluded: None

## 2. Forecast for the Fiscal Year Ending March 2005 (From April 1, 2004 to March 31, 2005)

	Net sales	Ordinary income	Net income
	¥ millions	¥ millions	¥ millions
Full year	1,660	110	71

Reference: Estimated net income per share for the fiscal year ending March 2005: ¥14.80

Note: Forecast for the fiscal year ending March 2005 was made by management based on currently available data and information. Please be aware that actual results may turn out different from those forecast as our company's business is affected by many factors. Please reference page 12 for details on the above forecasts.

## 1. Corporate Group

The Elmic Systems Group is made up of three companies: Elmic Systems, Inc. (the Company), Airfolc Corporation, (a 78%-owned subsidiary based in Kyoto, Japan) and Wescom Inc. (a 25%-owned affiliate based in Osaka, Japan).

Airfolc specializes in the development of technology, such as programs (H.323 and others) related to software for Internet-linked embedded systems for processing voice and imaging data (VoIP).

Wescom is a software house established in 1982 by Kazuya Murashima, who has served as deputy chairman of the Japan System House Association. This company is responsible for part of the Company's systems development activities, performing a broad range of software development ranging from applications for microprocessors to multi-purpose computers, stand-alone units and large-scale systems.

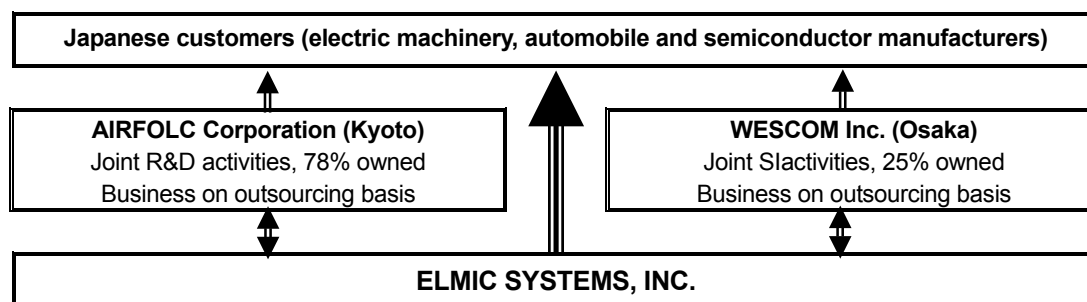
Elmic Systems USA Inc. (Elmic USA), a wholly owned subsidiary based in San Francisco, California, was established through the fall 2000 acquisition of a U.S. company. Elmic USA sells TCP/IP in Europe and North America. Additionally, anticipating the connection of embedded systems to high-speed Internet links, this company's R&D section has been assigned the task of developing a next-generation TCP/IP (IPv6) and related software. However, on December 25, 2003, Elmic USA was sold to Ardro Engineering, Inc., which is based in Cincinnati, Ohio, and subsequently renamed Treck Inc.

Major products are as follows.

Major products		Description	Elmic Systems Group		
			ELMIC SYSTEMS	AIRFORC	WESCOM
Manufactured products	Communications	Software and hardware for wire line and wireless communications	○		
	Internet protocol	Embedded TCP/IP modules, products for KASAGO application modules	○	○	○
	Real-time OS	The ELX exclusive RTOS, ITRON and other existing OS-related products, Windows CE resale and related products	○		
	System Integration (customization)	Products and system development using exclusive Elmic Systems key technologies, consigned products	○		○
Purchased products	Others	Products for Windows, Linux and TCP/IP and semiconductor-related products	○		

- Notes: 1. "Communications" is a new category this fiscal year that was formed by combining the "multi-purpose communications boards" and "ISDN board" categories of the previous fiscal year.  
 2. "Real-time OS" is a new category this fiscal year that was formed by combining the "Windows" and "Real-time OS" categories of the previous fiscal year.  
 3. Both the "communications" and "Real-time OS" categories cover exactly the same business activities in the current and prior fiscal years.

[Business Flowchart]



This chart shows only consolidated subsidiaries and equity-method affiliates.

## **2. Management Policies**

### **(1) Fundamental Management Policy**

The Elmic Systems Group is guided by the management philosophy of "Justice and Logic." The basic code of behavior is "Speedy, Compact, Perfect." In accordance with these precepts, the Group aims to be an organization capable of meeting the expectations of customers.

The Group is mainly involved in the provision of real-time OS (RTOS) products for embedded systems, the commercialization of software, and system integration (SI or customization) services that meet specific customer needs. Consequently, the Group depends heavily on expertise in the field of software. As the experience and skills of employees are critical to the Group's ability to serve customers, management places priority on realizing the full potential of all employees and retaining personnel.

### **(2) Fundamental Policy Regarding Distribution of Earnings**

In the production of software, securing the funds required to implement medium- and long-term business plans as well as to conduct an aggressive R&D program is essential to the success.

The Company's fundamental policy is to return earnings to shareholders by paying a stable dividend while maintaining a sound operating base and financial position.

### **(3) Policy Regarding Reduction in Investment Unit**

The Company regards a reduction in the investment unit as an effective means of increasing the number of individual shareholders and increasing trading volume of its shares on the stock market.

In consideration of current operating results, the share price, investor distribution and share liquidity, the Company will continue to consider taking concrete actions in accordance with changes in various factors.

### **(4) Targeted Performance Indicators**

The Elmic Systems Group is seeking to use its collective strengths, including those of consolidated subsidiaries, to maximize earnings, thereby returning to consolidated profitability at the operating level as soon as possible.

### **(5) Medium- and Long-Term Management Strategy**

By 2005, many home electronics appliance other than the PC will be linked to the Internet along with all other types of electric products (devices built into other products). To capitalize on the resulting opportunities, the Group is placing priority on the research and development targeting the necessary software. Particular emphasis is being placed on IPv6, the next-generation of the TCP/IP software that is essential for all Internet links. Development work is taking place primarily at the U.S. subsidiary. In addition, the Group is determined to begin selling Internet-related products at precisely the right times. For this purpose, the Group is accumulating the necessary funds (to establish affiliated companies and invest in partners) and hiring new product development engineers to bolster its technical capabilities. The Group is also enhancing its financial position by amortizing R&D expenditures in a suitable manner.

### **Sales**

The Elmic Systems Group is an independent organization having no affiliations with other companies. As such, the Group sells its products to numerous major producers of electrical products as well as to companies in many other industries. To serve this diverse customer base, the Group is upgrading its ability to conduct sales that seamlessly link expertise in marketing and the development of new technology. Sales target strategic customers and the introduction of new products that reflect market needs.

## Development

The Group's core products are RTOS, communications software and other items that are distinguished by their technology and broad market coverage. From this base, the Group is developing new products and building systems (system integration or customization) using those products to meet customers' demands. The pace of technological progress in embedded systems is extremely rapid. It is imperative that Elmic Systems be prepared to offer the embedded products and services for next-generation equipment as well as products for the subsequent generation. For this purpose, the Group is focusing on acquiring new technology, fostering its engineers and many other necessary measures.

### 1) Communications Software

In the IT arena, the Group is working together with large manufacturers of electronics products in the development of Bluetooth, IEEE802.11 and other next-generation wireless communication protocols. The Group is also forming business alliances in its drive to acquire knowledge involving new technologies.

With regard to communications boards supplied to producers of semiconductor manufacturing equipment, a major customer segment for Elmic Systems, the Company developed and began sales of SoftCOM, a package system that completely replaces these boards with software. SoftCOM fully complies with the SEMI standard, making it both easy to use for customers as well as a product with a high gross profit margin.

### 2) Internet Software

There are widespread concerns about the dwindling number of available Internet IP addresses. In response, the Company worked with Elmic Systems USA (now Treck Inc.) to develop the IPv6 protocol, a next-generation standard for embedded systems. Sales of this protocol began under the KASAGO IPv6 brand. This new protocol is sold as a single package (dual stack system) with the currently used KASAGO TCP/IP (IPv4) protocol, a technology with a proven record of reliability.

At present, this dual system is being distributed to large companies at no charge so that this technology can be evaluated. Some IPv6 software has begun contributing to sales. The final version of IPv6 will employ exclusive Company engineering to be compatible with equipment of all types, ranging from high-end data terminals to household products. Sales of this TCP/IP have started by loading it with the T-Engine (successor to ITRON), a next-generation OS.

In addition, the Company has developed a number of exclusive products as successors to existing software. Examples are an SIP that, as its predecessor H.323 protocol, makes possible VoIP (Voice over IP); IPSec, which facilitates secure communications; and a router protocol for connecting many terminals.

### 3) Real-Time OS (RTOS)

In the RTOS market, open source is becoming increasingly common, as is the case with TRON and Linux for embedded systems. Elmic Systems is focusing on system integration services based on these kinds of RTOS. Another successful RTOS is Accel-Linux, which offers the advantages both systems: the unrestricted development environment of Linux and the fast processing speed of ITRON.

Elmic has developed a new version of Hyper ITRON (Specifications independent of ITRON association), featuring enhanced security functions.

Furthermore, Elmic's technology is finding more applications in the automotive sector (car navigation systems).

### 4) System Integration

The Elmic Systems Group offers its consulting services, a particular Elmic Systems strength that links core

technology and products, and system development services to enhance the total performance of systems used in embedded systems (finished products or consumer goods).

With regard to embedded systems, the operation of software within a particular physical environment, such as the hardware, is critical. The experience of engineers is essential to delivering the needed performance. With expertise gained with expertise gained over its many years of operations, Elmic Systems can offer customers a valuable advantage in this regard.

#### 5) Others

Elmic Systems developed and began sales of an exclusive product called the PC iNHERITOR, which targets needs generated by the imminent termination of production of the NEC FC98 system, a PC for industrial use. The iNHERITOR will enable users of this PC to continue using the large volume of software developed for use with the ELX286, an RTOS developed by the Company that is widely employed by the NEC FC98.

The Group intends to develop more new products to further solidify its prominent position in its industry. This drive will be backed by the core technologies, products, highly experienced team of engineers and resources of Group companies, as has been outlined above.

##### a. Internet Software

The Company will continue to develop various functions and optional software, mainly tied to the KASAGO IPv6, to further enlarge its product lineup. Although Elmic SystemesUSA, which was primarily engaged in software development, has been sold, the Company maintains a good relationship with this company, which is now named Treck. System development activities will continue to be outsourced to Treck, which will serve as a business partner for the Company.

##### b. Real-Time OS (RTOS)

Elmic Systems will make its ELX and ITRON RTOS compatible with many CPUs and develop Linux-based application systems. The goal is to become a solution provider of embedded systems for any platform.

The Elmic Systems Group's product strategy will continue in the same basic direction as that outlined above. The Group is placing particular emphasis on the upcoming post-PC era. Embedded systems, such as phones and other mobile terminals, automotive systems, IT home appliances, kitchen appliances and all other electrical products, will be controlled via the Internet and exchange information. The TCP/IP will be at the nucleus of these systems. IPv6 will open the way to a virtually unlimited number of addresses. Both image processing (H.323, SIP) and security (IPSec) will be needed. In addition, as broadband communications take hold, the importance will grow not only of wired networks, but also of wireless networks and routers that facilitate communications within a limited scope.

Along with the above measures, the Group plans to upgrade products for industrial applications, an existing market that includes systems for semiconductor manufacturing equipment.

#### **Management of Sales and Development Activities**

Management systems are being strengthened from the standpoint of corporate governance. The Group is building a more clearly defined structure for submitting reports and directives and performing other management-related tasks covering sales, gross profit, delivery times, cost of sales, quality assurance, support services and other operating items.

**(6) Key Issues**

- a. Bolstering alliances
- b. Maintaining stable relationships with reliable vendors
- c. Training personnel
- d. Upgrading risk management
- e. Refining Data management systems
- f. Improving marketing capabilities

With expansion foreseen in markets where the Elmic Systems Group is active, the Group must minimize risk and maximize earnings in order to grow.

To accomplish this, the Group is working on cutting fixed costs (reducing selling, general and administrative expenses) and direct costs (cost of sales). At the same time, the Group must upgrade marketing capabilities to develop and sell products that accurately target market demands of the future.

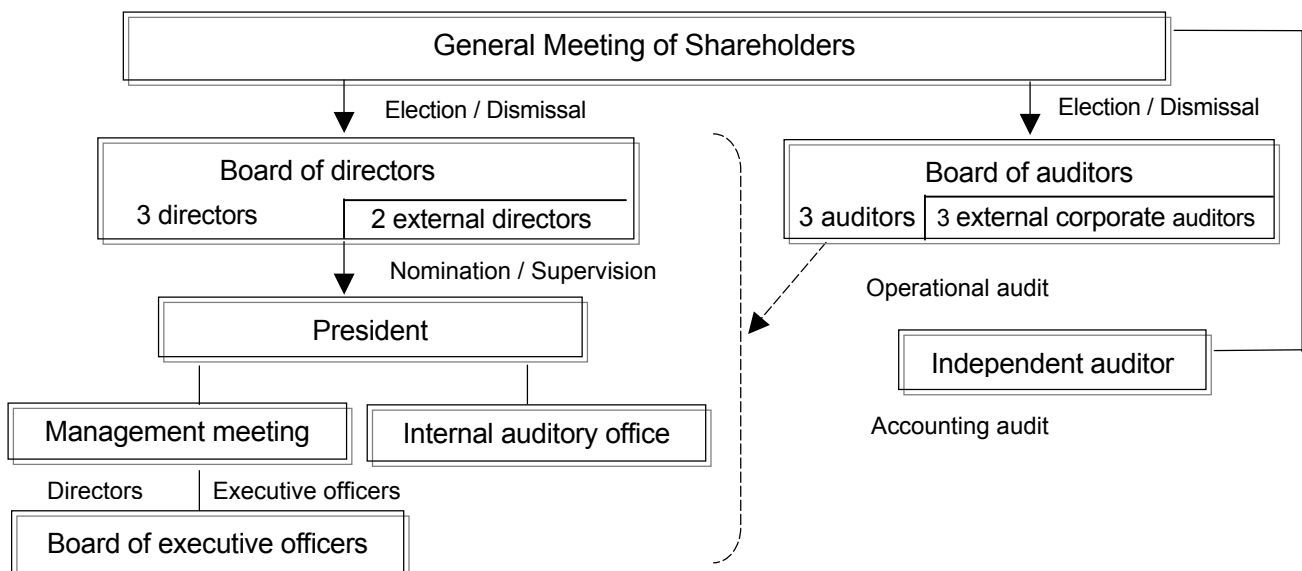
**(7) Fundamental Approach to and Actions Regarding Corporate Governance**

1) Fundamental approach to corporate governance

The most important goal of management is to sustain growth over the long term. This requires a decision-making system that is sound, efficient, speedy, and backed by managers who exercise strong leadership. The Company believes that such a system demands management that is transparent and devoted to the interests of shareholders. For this purpose, the Company quickly discloses financial information on its Internet site and through other channels.

2) Actions regarding corporate governance

- a. Status of management oversight organization and other corporate governance systems for management decision-making, the execution of business activities and the supervision of operations



As of March 31, 2004, the Company had a corporate auditor system in which all three corporate auditors were from outside the Company. Furthermore, two of the Company’s three directors were from outside the Company. None of these individuals have careers that involve the Company or any group companies. To ensure that management decisions can be reached quickly and executed with flexibility and speed, the Company adopted the executive officer system in October 2002, naming six executive officers.

b. Personnel, capital, business and other relationships between the Elmic Systems Group and external directors and external corporate auditors

The Company has an external director who is a representative director of IBT Corp. and a director of Toshiba LSI System Support Co., Ltd. One external corporate auditor is a tax accountant and representative director of Pacific Tsusho Co.

One external director is a director of a company that has a business relationship (a consulting contract) with the Company and a shareholder of the Company.

One external corporate auditor is also a shareholder of the Company.

There are no other related party interests among other external directors and external corporate auditors.

c. Corporate governance actions during the past year

An executive officer system with a clear mission has been adopted. This move has enabled the board of directors to reach decisions faster. To increase the transparency of management, the Company is upgrading IR activities, including the expansion of its Internet site (adding English-language IR information, etc.)

**(8) Other Significant Items**

Not applicable.

### 3. Results of Operations and Financial Position

#### (1) Results of Operations

##### 1) Summary of year ended March 31, 2004

In the current fiscal year, Japan's economy began showing signs of a recovery, particularly during the first half of the period, as the war in Iraq came to a swift end, the Japanese government supported financial institutions with public funds and stock prices rebounded. Furthermore, surveys revealed that sentiment among corporate managers is improving. However, the impact of a cool summer in Japan, soft consumer spending in Japan and overseas and political turmoil show that it is too soon to adopt an optimistic outlook.

Among the manufacturers that are the primary customers for Elmic Systems, there was a delay in the recovery of investments due to lingering effects of restructuring programs. As a result, there were dramatic differences in operating results among these manufacturers.

In this difficult operating environment, net sales at Elmic Systems were far below the level that was forecasted when the fiscal year began. However, cost-cutting measures and other actions minimized the impact on earnings of the drop in sales.

Over its entire 27-year history, the Company has concentrated on the development of software for embedded systems. In recent years, the Company has enlarged its business model to target the immense opportunities associated with Internet connections. As a result, a transition is under way in targeted markets and products. At the center of this transition is TCP/IP. This involves the development of IPv6, which will be a vital element of the devices that make possible a ubiquitous information society, as well as of IPv6 options. The strategic shift is beginning to produce results that include clear changes in sales by product category. Although manufacturers of finished products, which are the buyers of this software, are somewhat reducing the speed of investments in new product development, they are undoubtedly preparing for the advent of a ubiquitous information society. As a partner for these manufacturers, the Company plans to grow primarily by participating in the joint development of various systems and products.

##### 2) Results by product category

- In communications products, which the Company regards as a contracting business, there were strong first-quarter sales of ISDN boards for POS equipment and strong demand associated with capital expenditures for semiconductor and LCD manufacturing equipment. As a result, the decline in sales slowed somewhat as category sales were down 12.7% from the previous fiscal year.
- In Internet protocol products, the provision of KASAGO IPv6 at no cost to large companies to permit evaluations and research is producing results, leading to growth in licensing revenues from development kits and other products. Moreover, IPv4 is also generating royalties due to its adoption by several cell phone manufacturers. Elmic Systems believes that these manufacturers are selecting this protocol because it offers a higher processing (communication) speed than competing products, ease of migration, low memory requirements (compact size) and the outstanding support system. The large product lineup that includes many options is another major reason for the success of this protocol. Total Internet protocol sales in the first half were 4.4% lower than one year earlier.
- In real-time OS products, demands are growing among users of all types, particularly with regard to system integration needs, the focus of demand is shifting to open OS such as ITRON, T-Engine and Linux. As a result, OS sales have fallen sharply. In the current fiscal year, RTOS-related net sales were 68.3% less than one year earlier.
- In system integration (customization) products, the current fiscal year saw a continuation in the growth in orders and sales for SI services at liquid crystal factories that began in the previous fiscal year. There was also a large increase in sales for system integration services involving Internet protocols. The result was a 6.7%

increase in net sales in this category.

Due to these factors, consolidated net sales decreased 8.2% to ¥1,733 million, there was an ordinary loss of ¥78 million and a net loss of ¥142 million.

Results by geographic segment were as follows.

a. Japan

Sales in Japan decreased 1.8% to ¥1,571 million and there was an operating income of 13.5% increased of ¥94 million.

b. North America

Sales in North America decreased 49.8% to ¥141 million and there was an operating loss of ¥99 million.

c. Europe

Sales in Europe increased 223.0% to ¥20 million and operating loss was ¥31 million.

3) Research and development

Research and development expenses declined ¥119 million to ¥125 million. This was 7.3% of net sales. Major accomplishments were as follows.

a. Internet protocol

Work continued on the development of TCP/IP (KASAGO IPv6). A beta-version has already been shipped. The Company is now working on the next phase and upgraded options. Two examples are Mobile-IP for mobile communications applications and IPSec, which provides data security to address needs stemming from the growing variety of devices linked to the Internet. Another theme is peripheral software such as voice and image transmission software (H.323, embedded SIP). The Company is also working on a software development kit for the home router market, a field where much growth is foreseen. In addition, the Company developed a TCP/IP (KASAGO for T-Engine) for T-Engines, which are being promoted by the TRON Association as the new standard.

b. Communications

In research for CIM (Computer Integrated Manufacturing) for semiconductor production equipment, the Company completed development and began sales of the SoftCOM GEM300 communications protocol for 300mm wafer-compatible production equipment and the Cicadus host simulator for system tests.

c. Real Time OS

In addition to creating an upgraded version of its proprietary OS (ELX), research was conducted to make ITRON even easier to use. For this purpose, a group management function within the OS was newly developed and put on sale. Due to NEC's termination of the manufacture of industrial PCs, in which the Elmic Systems RTOS (ELX286) was used extensively, the Company developed and began selling a successor product called INHERITOR.

As a software manufacturer, Elmic Systems will continue to focus R&D activities on these areas while continuing to work on the development of a variety of products and upgraded versions of existing products.

## (2) Financial Position

### Cash Flows

Cash and cash equivalents decreased ¥23 million during the current fiscal year.

There was an income before income taxes and minority interest of ¥182 million, (compared with a ¥668 million loss one year earlier) ¥82 million increase in trade receivables (¥11 million more than one year earlier), ¥138 million in proceeds from the sale of investment securities (up 126.5% year on year), but there was a gain of ¥258 million on the sale of stock in a subsidiary, payments of ¥77 million for the purchase of intangible assets (down 12.3%) and ¥112 million in payments for investment securities (up 109.3%). Due to these and other factors, cash and cash equivalents totaled ¥1,254 million at the end of the fiscal year.

Cash flows by category in the current fiscal year were as follows.

### Operating activities

Net cash provided by operating activities was ¥35 million, 12.0% less than one year earlier. There was an income before income taxes and minority interest of ¥182 million, a gain of ¥258 million on the sale of stock in a subsidiary, a depreciation and amortization of ¥76 million (up 11.2%) and a ¥82 million decrease in trade receivables.

### Investing activities

Net cash used in investing activities was ¥60 million, 70.9% less than one year earlier. The major components were payments of ¥112 million (up 109.3%) for acquisition of investment securities, income of ¥138 million (up 126.5%) from gain on sales of investment securities and payments of ¥77 million (down 12.3%) for the purchase of intangible assets.

### Financing activities

Net cash used in financing activities was ¥4 million, 98.2% less than one year earlier. This was mainly due to payments of ¥3 million (up 3.7%) for the repayment of finance leases.

Trends in cash flow indicators were as follows.

	Year ended March 31, 2001	Year ended March 31, 2002	Year ended March 31, 2003	Year ended March 31, 2004
Shareholders' equity ratio (%)	84.1	87.5	83.8	86.1
Shareholders' equity ratio at market value (%)	114.5	54.5	28.5	88.5
Debt repayment multiple (years)	-	-	0.2	-
Interest coverage ratio	-	-	98.6	274.3

Notes: 1. The above figures are calculated as follows.

Shareholders' equity ratio: shareholders' equity divided by total assets

Shareholders' equity ratio at market value: market capitalization divided by total assets

Debt repayment multiple: interest-bearing debt divided by operating cash flows

Interest coverage ratio: operating cash flows divided by interest expenses

- All indicators are calculated based on consolidated financial figures.
- Market capitalization is calculated by multiplying the value of the Company's stock at the close of each period by the total number of shares issued at the end of the period.
- Operating cash flows are calculated using the figures for operating cash flows in the consolidated statements of cash flows. Net interest-bearing debt is the sum of all liabilities on the consolidated balance sheets for which interest payments are made. Interest expenses as shown in the consolidated statements of cash flows are used to calculate the interest coverage ratio.
- The fiscal 2002 and September 2003 interim debt repayment multiples and interest coverage ratios are not shown because operating cash flows were negative in these periods.
- The fiscal 2001 debt repayment multiple and interest coverage ratio are not shown because there was no interest-bearing debt or interest expenses in this year.

### **(3) Outlook for the Fiscal Year Ending March 2005**

TCP/IP (IPv6) next-generation Internet connection software for embedded systems has been very well received by customers, indicating that it will contribute to sales and earnings in the fiscal year ending in March 2005. Manufacturers have advanced to the planning stage for next-generation mobile phones, car navigation products and home appliances. It is quite possible that the Company's IPv6 will become the industry standard.

In addition, prospects are excellent for communication boards for semiconductor manufacturing equipment and particularly for equipment used to make LCD panels, a product sector where manufacturers are expanding output capacity. The iNHERITOR industrial PC is off to a strong start. The Company expects that sales will grow due to aggressive sales activities.

Furthermore, the development of a hybrid OS, ITRON with memory protection function, and other products is enabling Elmic Systems to play a leading role among suppliers of software for embedded systems. Despite these favorable trends, the Company is adopting a conservative view of market trends.

Due to the above factors, the Company is forecasting consolidated net sales of ¥1,660 million, ordinary income of ¥110 million and net income of ¥71 million in the fiscal year ending in March 2005. On a non-consolidated basis, the forecast is for net sales of ¥1,620 million, ordinary income of ¥110 million and net income of ¥61 million.

These forecasts are based on management's judgments in accordance with information that is currently available. Actual results may differ significantly due to a variety of factors.

Therefore, investors are cautioned not to make investment decisions based solely on these forecasts. Factors that can affect operating results include, but are not limited to, the economic environment in major markets, changes in demand and prices for products, rapid advances in technology, changes in exchange rates, and revisions in regulations and accounting standards in Japan and overseas.

Due to the seasonal nature of the Company's operating results, in which the majority of deliveries and sales occur during the second half of each fiscal year.

#### 4. Other Important Information

Presented below are a list of risk factors that can affect the Company's business operations and other aspects of its activities. This information is being supplied from the standpoint of conducting an aggressive disclosure program for investors by providing information on items that are believed to be important to reaching investment decisions. This list even includes items that may not necessarily correspond to obvious risk factors. The Company is aware of these risk factors and is taking measures to respond in the event that any of these problems occurs. However, investors should carefully read this list and all information in this document, as well as gather information from other sources so that all factors can be carefully considered before reaching an investment decision.

##### Risks concerning business operations

###### Communication Risk

The Company is acquiring new technology primarily through joint development programs and other forms of alliances. In the event that one or more alliances are terminated, the Company could have difficulty acquiring new technology, an event that could have a material impact on operating results.

###### Internet risk

KASAGO TCP/IP (IPv4) is employed by a large number of users and sales of KASAGO IPv6 have been started based on these existing users. At present, a number of Japanese companies, mostly large manufacturers of electrical equipment, are using KASAGO IPv6 at no charge to conduct evaluations and research. Elmic Systems is now in phase 2 of the development process, which mainly entails the development of IPv6 optional softwarepackages. Any delay in the market launch of thesepackages could have an impact on operating results.

###### System integration risk

By maintaining good relationships with vendors, the Company strives to maintain access to qualified personnel, sustain the profitability of system integration operations and maintain a stable level of orders. Any difficulties concerning these relationships could have a material impact on operating results.

##### Fables Policy

Elmic Systems designs hardware but has no manufacturing facilities of its own. The development and manufacturing companies listed below, and the new development and manufacturing outsourcing companies, are used to maintain a flexible design and manufacturing capability. This enables the Company to avoid the risk of holding excessive inventories of components and production facilities. External development and manufacturing outsourcing factories are utilized under outsourcing contracts, and every effort is made to prevent problems concerning quality. As products developed by Elmic Systems are assets of the Company, management is conducted to permit the continuous manufacture of these products at the factories of outsourcing partners.

##### Reliance on External Vendors (Orders Placed)

During the past fiscal year, the Company placed a total of ¥496 million of orders with external vendors.

Major companies and orders placed are shown below.

This table does not include Airfolc Corporation, Wescom Inc. and Elmic Systems USA, Inc.

Yen in thousands

Vendor	Product	Orders		Remarks
		Fiscal year ended Mar. 31, 2004		
			Share (%)	
Treck Inc. (Elmic Systems USA, Inc.)	Customized software	108,929	21.9	
Yamaki Electric Corporation	Communication boards	47,531	9.6	
MDK Corporation	Communication boards	41,859	8.4	
Towada Audio Co., Ltd.	Communication boards	29,898	6.0	
Raisey Systems	Customized software	28,630	5.8	
Other (39 companies)		256,848	51.7	
Total		496,384	100.0	

Note: The above amounts do not include consumption taxes.

Elmic Systems closely monitors the management, manufacturing supervision, quality assurance and other aspects of the operations of these companies. Furthermore, precautions are taken to diversify risk to avoid excessive reliance on any particular vendor. Nevertheless, a problem in the ability of a vendor to conduct operations could affect the Company's ability to ship products. Therefore, the inability to ship products at the required time due to a problem involving the design, manufacturing or quality assurance capabilities of a vendor could have a material impact on operating results.

### **Human resources**

Employees involved in marketing and development activities will play an important role in the expansion of new businesses. As Elmic Systems operates in a small industry and there are a limited number of talented individuals, there is a risk that the Company may not be able to hire the necessary personnel due to intense competition. The Company is currently reviewing its personnel system in order to attract skilled individuals and motivate employees. The Company will further upgrade its target management system and compensation structure to reflect the capabilities of each employee. Any difficulty in hiring or retaining the necessary personnel could hinder the Company's ability to reach its medium- and long-term strategic goals and have a material impact on operating results.

### **Investments**

Elmic Systems has consistently invested in its core business. At this time, management plans to aggressively conduct a broad spectrum of business activities that are based on existing products and services. As part of this drive, the Company will be establishing subsidiaries and forming alliances in Japan and overseas.

The investments required by these actions may be large compared to the size of the Company, creating greater risks involving the Company's financial position and business operations. However, it is impossible to accurately predict the impact on the Company's operations of conditions at companies in which it has invested. In some cases, the Company may not be able to recover its investments.

### **Significant alliances**

Significant contracts signed during the first half of the current fiscal year were as follows.

The Elmic Systems Group enters into a large number of business agreements and alliances to acquire new technologies. Most of these actions involve systems that will be commercialized in the future. Any leaks of such information could be harmful to these customers. Consequently, the Company enters into confidentiality contracts with all customers and external vendors in addition to contracts for the placement of orders. The following information is therefore provided only to the extent possible under these confidentiality contracts.

Alliances of the type described in (6) Key Issues are conducted under strict secrecy until the products of the alliance partners are shipped. Any leak of information concerning these activities may not only cause a termination of the alliance, but could also subject the Company to a lawsuit seeking payment of damages. Consequently, the following list of alliances contains information only to the extent possible under secrecy agreements with each company.

#### **a. NexWave Solutions Inc.**

Purpose: Agreement for the resale of component structure software for the embedded systems industry

Personnel: None

#### **b. Websoft International Inc.**

Purpose: Partnership contract for the development of the "Esprit" embedded system browser software

Personnel: None

## 5. Consolidated Financial Statements

### (1) Consolidated Balance Sheets

Account	Period	FY2002 As of March 31, 2003		FY2003 As of March 31, 2004		YoY change
		¥ thousands	%	¥ thousands	%	¥ thousands
<b>Assets</b>						
I Current assets						
1. Cash and deposits		171,219		154,251		(16,967)
2. Notes & accounts receivable - trade		801,048		686,551		(114,497)
3. Available for sale securities		1,106,818		1,100,636		(6,181)
4. Inventories		104,722		116,614		11,892
5. Deferred tax assets - current		63,201		51,832		(11,369)
6. Other current assets		53,607		80,067		26,459
7. Reserve for doubtful receivables		(2,266)		(264)		2,002
Total current assets		2,298,352	71.6	2,189,690	68.0	(108,661)
II Fixed assets						
1. Property, plant and equipment						
(1) Buildings		12,577		12,577		
Accumulated Depreciation		7,986	4,591	8,775	3,802	(788)
(2) Tools, furniture & fixtures		147,139		102,836		
Accumulated Depreciation		100,919	46,220	91,145	11,691	(34,529)
Total property, plant and equipment		50,811	1.6	15,493	0.5	(35,317)
2. Intangible assets						
(1) Goodwill		58,842		-		(58,842)
(2) Other intangible assets		144,478		160,971		16,493
Total intangible assets		203,320	6.3	160,971	5.0	(42,348)
3. Investments and other assets						
(1) Investment securities	*1	195,758		215,784		20,026
(2) Long-term loans receivable		-		147,680		147,680
(3) Deferred tax assets - non-current		320,924		294,773		(26,150)
(4) Others		142,734		198,297		55,563
(5) Reserve for doubtful receivables		(1,500)		(1,400)		100
Total investments and other assets		657,917	20.5	855,136	26.5	197,218
Total fixed assets		912,049	28.4	1,031,602	32.0	119,552
Total assets		3,210,401	100.0	3,221,292	100.0	10,890

Account	Period	FY2002 As of March 31, 2003		FY2003 As of March 31, 2004		YoY change
		¥ thousands	%	¥ thousands	%	¥ thousands
<b>Liabilities</b>						
I Current liabilities						
1. Accounts payable - trade		133,439		127,041		(6,397)
2. Income taxes payable		7,636		5,971		(1,665)
3. Reserve for accrued bonuses		50,200		45,691		(4,508)
4. Other current liabilities		101,096		48,030		(53,065)
Total current liabilities		292,372	9.1	226,735	7.1	(65,637)
II Long-term liabilities						
1. Reserve for employees' retirement benefits		19		-		(19)
2. Reserve for directors' retirement benefits		160,225		161,499		1,273
3. Other long-term liabilities		59,664		52,094		(7,570)
Total long-term liabilities		219,909	6.9	213,593	6.6	(6,315)
Total liabilities		512,281	16.0	440,329	13.7	(71,952)
<b>Minority interest</b>						
Minority interest		7,706	0.2	7,006	0.2	(699)
<b>Shareholders' equity</b>						
I Common stock	*2	1,160,041	36.1	1,160,041	36.0	-
II Capital surplus		1,459,152	45.5	1,459,152	45.3	-
III Retained earnings		192,041	6.0	334,189	10.4	142,148
IV Net unrealized gain (loss) on other securities		(16,740)	(0.5)	5,757	0.2	22,498
V Foreign currency translation adjustment		80,539	2.5	-		(80,539)
VI Treasury stock	*3	(184,619)	(5.8)	(185,184)	(5.8)	(564)
Total shareholders' equity		2,690,414	83.8	2,773,956	86.1	83,542
Total liabilities, minority interest and shareholders' equity		3,210,401	100.0	3,221,292	100.0	10,890

## (2) Consolidated Statements of Income

Account	Period	FY2002 From April 1, 2002 to March 31, 2003		FY2003 From April 1, 2003 to March 31, 2004		YoY change ¥ thousands		
		¥ thousands	%	¥ thousands	%			
I Net sales			1,888,436	100.0	1,733,403	100.0	(155,032)	
II Cost of sales	*2		853,308	45.2	815,492	47.0	(37,816)	
Gross profit			1,035,128	54.8	917,911	53.0	(117,216)	
III SG&A	*1,2		1,061,207	56.2	995,720	57.5	(65,486)	
Operating loss			26,079	(1.4)	77,809	(4.5)	(51,730)	
IV Non-operating income								
1. Interest income		2,935			1,476			
2. Dividends income		100			1,015			
3. Equity in earnings of affiliates		9,215			11,180			
4. Gain on anonymous partnerships		5,217			7,185			
5. Other non-operating income		2,173	19,641	1.0	2,331	23,188	1.4	3,546
V Non-operating expenses								
1. Interest expense		414			131			
2. Loss on options		6,700			-			
3. Foreign exchange loss		12,873			23,835			
4. Other non-operating expenses		785	20,774	1.1	-	23,966	1.4	3,192
Ordinary loss			27,211	(1.4)		78,587	(4.5)	(51,376)
VI Extraordinary income								
1. Gain on reversal from doubtful receivables		-			413			
2. Gain on sales of investment securities		10,150			22,904			
3. Gain on sale of subsidiary stock		-	10,150	0.5	258,801	282,119	16.3	271,968
VII Extraordinary loss								
1. Loss on removal of fixed assets	*3	-			232			
2. Loss on impairment of goodwill		604,785			-			
3. Loss on revaluation of investment securities		32,120			10,735			
4. Loss on revaluation of inventories		14,399			-			
5. Prior year consumption taxes, etc.		-	651,305	34.5	10,466	21,434	1.3	(629,870)
Net income (losses) before income taxes and minority interest			(668,366)	(35.4)		182,097	10.5	850,463
Income taxes - current		6,979			6,091			
Income taxes - deferred		(283,424)	(276,445)	(14.6)	34,555	40,647	2.3	317,092
Minority interest			550	0.0		(699)	0.0	(1,249)
Net income (losses)			(392,471)	(20.8)		142,148	8.2	534,619

### (3) Consolidated Statements of Retained Earnings

Account	Period	FY2002 From April 1, 2002 to March 31, 2003		FY2003 From April 1, 2003 to March 31, 2004		YoY change
		¥ thousands		¥ thousands		¥ thousands
<b>Capital surplus</b>						
I	Capital surplus at beginning of year				1,459,152	
	Additional paid-in capital	1,459,152	1,459,152			-
II	Capital surplus at end of year		1,459,152		1,459,152	-
<b>Retained earnings</b>						
I	Retained earnings at beginning of year				192,041	
	Retained earnings at beginning of year	624,316	624,316			(432,275)
II	Increase in retained earnings					
1.	Net income	-		142,148	142,148	142,148
III	Decline in retained earnings					
1.	Cash dividends	39,804		-		
2.	Net loss	392,471	432,275	-	-	(432,275)
IV	Retained earnings at end of year		192,041		334,189	142,148

#### (4) Consolidated Statements of Cash Flows

Account	Period	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004	YoY change
		¥ thousands	¥ thousands	¥ thousands
I Cash flows from operating activities				
Net income (losses) before income taxes and minority interest		(668,366)	182,097	850,463
Depreciation and amortization		68,848	76,587	7,738
Amortization of long-term prepaid expenses		-	247	247
Equity in earnings of affiliates		(9,215)	(11,180)	(1,964)
Increase (decrease) in reserve for doubtful receivables		2,266	(363)	(2,630)
Decrease in reserve for accrued bonuses		(2,462)	(4,508)	(2,045)
Increase (decrease) in reserve for employees' retirement benefits		19	(19)	(38)
Increase in reserve for directors' retirement benefits		2,818	1,273	(1,545)
Interest and dividends income		(3,035)	(2,491)	544
Interest expense		414	131	(283)
Gain on anonymous partnerships		(5,217)	(7,185)	(1,968)
Foreign exchange loss		6,827	667	(6,159)
Loss on options		6,700	-	(6,700)
Gain on sales of investment securities		(10,150)	(22,904)	(12,753)
Loss on impairment of goodwill		604,785	-	(604,785)
Loss on removal of fixed assets		-	232	232
Gain on sale of subsidiary stock		-	(258,801)	(258,801)
Loss on revaluation of investment securities		32,120	10,735	(21,384)
Loss on revaluation of inventories		14,399	-	(14,399)
Decrease (increase) in notes and accounts receivable-trade		(11,444)	82,267	93,711
Increase in inventories		(33,318)	(11,801)	21,516
Increase (decrease) in accounts payable-trade		25,067	(4,310)	(29,378)
Decrease (increase) in other assets		(11,673)	29,043	40,716
Decrease in other liabilities		(16)	(15,955)	(15,939)
Decrease in suspense receipt of consumption taxes		9,302	-	(9,302)
Increase (decrease) in suspense payment of consumption taxes		16,858	(4,988)	(21,847)
Subtotal		35,528	38,772	3,243
Interest and dividends received		10,560	4,991	(5,569)
Interest paid		(414)	(131)	283
Income taxes paid		(4,817)	(7,688)	(2,871)
Net cash provided by operating activities		40,857	35,943	(4,914)

Account	Period	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004	YoY change
		¥ thousands	¥ thousands	¥ thousands
II Cash flows from investing activities				
Payments for acquisition of available for sale securities		(202,154)	-	202,154
Proceeds from redemption of available for sale securities		100,654	-	(100,654)
Payments for acquisition of property, plant and equipment		(24,470)	(3,169)	21,300
Payments for acquisition of intangible assets		(88,767)	(77,819)	10,947
Payments for acquisition of investment securities		(53,656)	(112,280)	(58,623)
Gain on sales of investment securities		61,267	138,784	77,517
Decline in cash and cash equivalents due to sale of consolidated subsidiary		-	(4,514)	(4,514)
Payments for short-term loans receivable		(10,000)	-	10,000
Proceeds from collection of short-term loans receivable		10,000	-	(10,000)
Payments for long-term loans receivable		(500)	(700)	(200)
Proceeds from collection of long-term loans		1,640	1,010	(630)
Proceeds from return of leasehold and security deposits		373	4,645	4,272
Others		(2,230)	(6,386)	(4,155)
Net cash used in investing activities		(207,844)	(60,429)	147,415
III Cash flows from financing activities				
Payments for finance lease liabilities		(3,245)	(3,366)	(121)
Payments for acquisition of treasury stock		(184,264)	(564)	183,700
Cash dividends paid		(39,504)	(168)	39,336
Net cash used in financing activities		(227,013)	(4,098)	222,914
IV Effect of exchange rate changes on cash and cash equivalents		(10,370)	5,434	15,804
V Decrease in cash and cash equivalents		(404,370)	(23,149)	381,220
VI Cash and cash equivalents at beginning of year		1,682,407	1,278,037	(404,370)
VII Cash and cash equivalents at end of year	*1	1,278,037	1,254,887	(23,149)

## Significant Accounting Policies in the Preparation of Consolidated Financial Statements

Period Item	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
1. Scope of consolidation	(1) Consolidated subsidiaries: 2 Names of consolidated subsidiaries: Elmic Systems USA, Inc. AIRFOLC Corporation  (2) Unconsolidated subsidiaries: 0	(1) Consolidated subsidiaries: 1 Names of consolidated subsidiaries: AIRFOLC Corporation Effective March 31, 2004, Elmic Systems USA, Inc, a consolidated subsidiary in prior years, has been excluded from the consolidation since the Company sold its entire equity stake in the entity on December 25, 2003. The consolidated financial statements include Elmic Systems USA, Inc.'s statements of income and statements of cash flows for the period from Jan. 1, 2003 to Dec. 31, 2003.  (2) Unconsolidated subsidiaries: 0
2. Equity method accounting	(1) Affiliates accounted for by the equity method of accounting: 1 Affiliate name: WESCOM Inc.  (2) Affiliates not accounted for by the equity method RockHand Technology, an equity-method affiliate in prior periods, is excluded from the scope of affiliates accounted for by the equity method, given the fact that it has a very minor effect on consolidated net income/loss (equity in earnings) and consolidated retained earnings (equity in earnings) and is relatively insignificant in the context of consolidated financial statements.	(1) Affiliates accounted for by the equity method of accounting: 1 Affiliate name: WESCOM Inc.  (2) RockHand Technology, an equity-method affiliate in prior periods, is excluded from the scope of affiliates accounted for by the equity method, given the fact that it has a very minor effect on consolidated net income/loss (equity in earnings) and consolidated retained earnings (equity in earnings) and is relatively insignificant in the context of consolidated financial statements.
3. Balance sheet dates of subsidiaries	The consolidated financial statements include the accounts of the following consolidated subsidiaries, of which the fiscal year ends on a different day: Elmic Systems USA, Inc Fiscal year-end: Dec. 31 AIRFOLC Corporation Fiscal year-end: Feb. 28  In the preparation of consolidated financial statements for the fiscal year, the financial statements of the subsidiaries for their respective fiscal year have been used. With respect to significant transactions, which occurred after the balance sheet dates of the consolidated subsidiaries, necessary adjustments have been made in the consolidated financial statements.	The consolidated financial statements include the accounts of the following consolidated subsidiaries, of which the fiscal year ends on a different day: AIRFOLC Corporation Fiscal year-end: Feb. 28  In the preparation of consolidated financial statements for the fiscal year, the financial statements of the subsidiary for its respective fiscal year have been used. With respect to significant transactions, which occurred after the balance sheet date of the consolidated subsidiary, necessary adjustment has been made in the consolidated financial statements.
4. Accounting standards	A. Valuation criteria and methods for significant assets: (1) Securities Held-to-maturity securities Valued using the amortized cost method Affiliated company stock Stated at cost, cost using the moving average method	A. Valuation criteria and methods for significant assets: (1) Securities Held-to-maturity securities Same as on the left. Affiliated company stock Same as on the left.

Item \ Period	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
	<p>Other securities</p> <p>Securities with market quotations Stated at fair value based on market prices on the balance sheet date (Unrealized holding gains and losses are accounted for as a component of the shareholders' equity; cost of other securities sold is determined using the moving average method)</p> <p>Securities without market quotations: Stated at cost, cost using the moving average method</p> <p>(2) Inventories Merchandise: Stated at cost, cost being determined by the moving average method</p> <p>Products, work in process and raw materials: Stated at cost, cost being determined by the period average method</p> <p>B. Depreciation and amortization of significant depreciable assets</p> <p>(1) Property, plant and equipment The Company and its domestic subsidiaries compute depreciation using the declining balance method, in accordance with Corporation Tax laws. Overseas-consolidated subsidiaries compute depreciation using the straight-line method in accordance with the generally accepted accounting standards of the countries of their domicile.</p> <p>(2) Intangible assets The Company and its domestic subsidiaries amortize capitalized costs using two alternate methods, which is higher, depreciation based on estimated sales volume or the straight-line method based on remaining period to expiration. Software for internal use is amortized using the straight-line method over its estimated useful life of five years. Effective the current consolidated fiscal year, overseas subsidiaries adopted the SEC accounting standards on "Goodwill and Other Intangible Assets." The SEC accounting standards require that goodwill no longer be amortized but instead tested for impairment at least annually.</p> <p>The application of the new standards caused amortization expense, operating loss and ordinary loss to decline by ¥35,393 thousand compared to amounts that would have been reported if the previous method had been applied consistently. Net loss before income taxes and minority interest increased by ¥569,392 thousand since impairment evaluation for goodwill resulted in a ¥604,785 thousand extraordinary charge to income.</p>	<p>Other securities</p> <p>Securities with market quotations Same as on the left.</p> <p>Securities without market quotations: Same as on the left.</p> <p>(2) Inventories Merchandise: Same as on the left.</p> <p>Products, work in process and raw materials: Same as on the left.</p> <p>B. Depreciation and amortization of significant depreciable assets</p> <p>(1) Property, plant and equipment Same as on the left.</p> <p>(2) Intangible assets The Company and its domestic subsidiaries amortize capitalized costs using two alternate methods, which is higher, depreciation based on estimated sales volume or the straight-line method based on remaining period to expiration. Software for internal use is amortized using the straight-line method over its estimated useful life of five years.</p>

Item \ Period	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
	<p>C. Recognition of reserves</p> <p>(1) Reserve for doubtful receivables To prepare for credit losses on accounts receivable, the Company and its domestic subsidiaries provide an allowance equal to the estimated amount of uncollectible receivables for general receivables based on the historical write-off ratio, and bad receivables based on a case-by case determination of collectibility. Overseas-consolidated subsidiaries provide allowances for credit losses based on a case-by-case determination of collectibility.</p> <p>(2) Reserve for accrued bonuses As a means of providing for bonus obligations, the Company and its domestic subsidiaries designates in the reserve account an amount accrued for the current fiscal year among the estimated future obligations.</p> <p>(3) Reserve for employees' retirement benefits To provide for employee retirement benefits, an allowance for retirement benefits is provided in the amount deemed to have accrued, determined based on the estimated retirement benefit obligations and pension assets on the balance sheet date.</p> <p>(4) Reserve for directors' retirement benefits To provide for directors' retirement benefits, an allowance is provided pursuant to the Company's rules on directors' retirement benefits.</p> <p>D. Accounting for lease transactions The Company and its domestic subsidiaries account all finance lease contracts other than those that are deemed to transfer the ownership of the leased assets to lessees by the method similar to that applicable to ordinary operating leases. Overseas-consolidated subsidiaries account lease transactions by the method similar to that applicable to regular trading transactions.</p> <p>E. Accounting for significant hedge transactions</p> <p>(1) Hedge accounting method The deferred hedge accounting method is applied.</p> <p>(2) Hedging method and risks hedged Hedging method: Foreign currency forward contracts Risks hedged: Planned foreign currency denominated transactions</p>	<p>C. Recognition of reserves</p> <p>(1) Reserve for doubtful receivables Same as on the left.</p> <p>(2) Reserve for accrued bonuses Same as on the left.</p> <p>(3) Reserve for employees' retirement benefits To provide for employee retirement benefits, an allowance for retirement benefits is provided in the amount deemed to have accrued, determined based on the estimated retirement benefit obligations and pension assets on the balance sheet date. The Company accounted ¥109 thousand as pre-paid pension expenses in the current fiscal year. The amount represents pension fund assets at fair value in excess of the retirement benefit liability.</p> <p>(4) Reserve for directors' retirement benefits Same as on the left.</p> <p>D. Accounting for lease transactions Overseas consolidated subsidiaries account all finance lease contracts other than those that are deemed to transfer the ownership of the leased assets to lessees by the method similar to that applicable to regular trading transactions.</p> <p>E. —</p>

Item \ Period	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
	<p>(3) Hedging policy Currently the company uses foreign currency forward contracts only to hedge exchange rate risk on its planned future foreign currency denominated transactions.</p> <p>(4) Assessing hedge effectiveness No information is provided on the method of assessing the effectiveness of the hedge since the fair value of the cash flow from the hedged item is expected to almost fully offset the changes in the fair value of the cash flow from the hedging instrument.</p> <p>F. Other significant accounting policies in the preparation of consolidated financial statements for the fiscal year</p> <p>(1) Equity method of accounting based on the anonymous partnership agreement The Company in March 1995 entered a leveraged lease agreement (term of agreement: 12 years) with an anonymous partnership. The ¥50,000 thousands investment at the time of participation is recognized as a claim against the anonymous association. A share of the anonymous partnership's net assets (as recorded in the most recent settlement of accounts) proportional to the Company's investment in the anonymous partnership is recognized as a claim or liability against the anonymous partnership. A share of the anonymous partnership's net income (as recorded in the settlement of accounts for the fiscal year), applicable to the current consolidated fiscal year, proportional to the Company's investment in the anonymous partnership is recognized as a gain or loss on investment in the anonymous partnership.</p> <p>(2) Accounting treatment for consumption taxes Consumption taxes are accounted by the tax exclusion method.</p> <p>(3) Accounting standard for treasury stock and reduction of legal reserves Effective the current consolidated fiscal year, the Company has adopted the new accounting standards for treasury stock and reduction of legal reserves (Financial Accounting Standard No. 1, Accounting Standard for Treasury Stock and Reduction of Legal Reserves, Business Accounting Deliberation Council). The effect of this change on profit/loss is insignificant. Effective the current consolidated fiscal year, in accordance with the revised Regulations of Financial Statements, the "Shareholders' equity"</p>	<p>F. Other significant accounting policies in the preparation of consolidated financial statements for the fiscal year</p> <p>(1) Equity method of accounting based on the anonymous partnership agreement Same as on the left.</p> <p>(2) Accounting treatment for consumption taxes Same as on the left.</p> <p>(3) ———</p>

Item \ Period	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
	<p>section in the consolidated balance sheets and the "Consolidated Statements of Retained Earnings" conform with the revised Regulations of Financial Statements.</p> <p>(4) Per share data Corporate Accounting Standard No.2 "Accounting Standard on Net Income per Share" and Corporate Accounting Standard Procedure No.4 "Accounting Standard Procedure on Net Income per Share," which became effective in the fiscal year starting on April 1, 2002, are adopted to for the consolidation fiscal year under review. Regarding the impact arising from this change, see the note in "Amounts Per Share," p.34.</p>	(4) —
5. Evaluation of assets and liabilities of consolidated subsidiaries	The market value method is adopted fully for the evaluation of assets and liabilities of the consolidated subsidiaries.	Same as on the left.
6. Appropriation of earnings	The consolidated statement of retained earnings is prepared based on the appropriation of earnings as finalized at the relevant consolidated entities in the consolidation fiscal year under review.	Same as on the left.
7. Scope of cash and cash equivalents on consolidated statement of cash flows	For the purpose of consolidated statement of cash flows, cash and cash equivalents consists of vault cash, deposits that can be withdrawn on demand, and short-term investments, with original maturities of three months or less, that are readily convertible to known amounts of cash and present insignificant risk of change in value.	Same as on the left.

## Reclassifications

FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
—————	<p>Consolidated balance sheets</p> <p>Effective the current consolidated fiscal year, Long-term Loans Receivable, included in Others under Investments and Other Assets in prior periods, is reclassified and presented as a separate line item since Long-term Loans Receivable exceeded 1/100 of total assets in the current consolidated fiscal year.</p> <p>In the previous fiscal year, Long-term Loans Receivable totaled ¥7,275 thousand.</p>

## Notes to consolidated financial statements

### Notes to consolidated balance sheets

Yen in thousands

FY2002 As of March 31, 2003	FY2003 As of March 31, 2004
<p>*1. Affiliated company stock:</p> <p style="padding-left: 20px;">Investment securities 75,208 (equity securities)</p> <p>*2. Number of shares outstanding</p> <p style="padding-left: 20px;">Common stock 5,307,680 shares</p> <p>*3. Number of treasury stock held by the consolidated subsidiaries and affiliates accounted for under the equity method</p> <p style="padding-left: 20px;">Common stock 490,960 shares</p>	<p>*1. Affiliated company stock:</p> <p style="padding-left: 20px;">Investment securities 87,070 (equity securities)</p> <p>*2. Number of shares outstanding</p> <p style="padding-left: 20px;">Common stock 5,307,680 shares</p> <p>*3. Number of treasury stock held by the consolidated subsidiaries and affiliates accounted for under the equity method</p> <p style="padding-left: 20px;">Common stock 491,950 shares</p>

### Notes to consolidated statements of income

Yen in thousands

FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
<p>*1. Principal components and amounts of SG&amp;A expenses are as follows:</p> <p style="padding-left: 20px;">Wages &amp; allowances: 359,094</p> <p style="padding-left: 20px;">Provision of reserve for accrued bonuses: 21,302</p> <p style="padding-left: 20px;">Provision of reserve for directors' retirement allowance: 7,552</p> <p style="padding-left: 20px;">R&amp;D: 161,383</p> <p>*2. Research and development expenses included in SG&amp;A expenses 245,190</p> <p>*3. —————</p>	<p>*1. Principal components and amounts of SG&amp;A expenses are as follows:</p> <p style="padding-left: 20px;">Wages &amp; allowances: 382,320</p> <p style="padding-left: 20px;">Provision of reserve for accrued bonuses: 24,683</p> <p style="padding-left: 20px;">Provision of reserve for directors' retirement allowance: 6,965</p> <p style="padding-left: 20px;">R&amp;D: 79,078</p> <p>*2. Research and development expenses included in SG&amp;A expenses 125,899</p> <p>*3. Loss on removal of fixed assets represents the loss on removal of tools, furniture and fixtures.</p>

**Notes to consolidated statements of cash flows**

Yen in thousands

FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004																
<p>1. Reconciliation of cash and cash equivalents of the statements of cash flows and account balances of consolidated balance sheets for the fiscal year is made as follows:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;"></td> <td style="text-align: right;">As of March 31, 2003</td> </tr> <tr> <td>Cash and deposits:</td> <td style="text-align: right;">171,219</td> </tr> <tr> <td>Short-term investments with original maturities of less than 3 months:</td> <td style="text-align: right;">1,106,818</td> </tr> <tr> <td style="border-top: 1px solid black;">Cash and cash equivalents:</td> <td style="text-align: right; border-top: 1px solid black;">1,278,037</td> </tr> </table>		As of March 31, 2003	Cash and deposits:	171,219	Short-term investments with original maturities of less than 3 months:	1,106,818	Cash and cash equivalents:	1,278,037	<p>1. Reconciliation of cash and cash equivalents of the statements of cash flows and account balances of consolidated balance sheets for the fiscal year is made as follows:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;"></td> <td style="text-align: right;">As of March 31, 2004</td> </tr> <tr> <td>Cash and deposits:</td> <td style="text-align: right;">154,251</td> </tr> <tr> <td>Short-term investments with original maturities of less than 3 months:</td> <td style="text-align: right;">1,100,636</td> </tr> <tr> <td style="border-top: 1px solid black;">Cash and cash equivalents:</td> <td style="text-align: right; border-top: 1px solid black;">1,254,887</td> </tr> </table>		As of March 31, 2004	Cash and deposits:	154,251	Short-term investments with original maturities of less than 3 months:	1,100,636	Cash and cash equivalents:	1,254,887
	As of March 31, 2003																
Cash and deposits:	171,219																
Short-term investments with original maturities of less than 3 months:	1,106,818																
Cash and cash equivalents:	1,278,037																
	As of March 31, 2004																
Cash and deposits:	154,251																
Short-term investments with original maturities of less than 3 months:	1,100,636																
Cash and cash equivalents:	1,254,887																
<p>2. _____</p>	<p>2. Significant components of assets and liabilities of consolidated subsidiary excluded from the consolidation due to sale of equity stake:                      Significant components of assets and liabilities of Elmic Systems USA, Inc. excluded from the consolidation due to sale of equity stake in the entity:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">Current assets</td> <td style="text-align: right;">31,512</td> </tr> <tr> <td>Fixed assets</td> <td style="text-align: right;">77,557</td> </tr> <tr> <td style="border-top: 1px solid black;">Total assets</td> <td style="text-align: right; border-top: 1px solid black;">109,070</td> </tr> <tr> <td>Current liabilities</td> <td style="text-align: right;">184,108</td> </tr> <tr> <td style="border-top: 1px solid black;">Total liabilities</td> <td style="text-align: right; border-top: 1px solid black;">184,108</td> </tr> </table>	Current assets	31,512	Fixed assets	77,557	Total assets	109,070	Current liabilities	184,108	Total liabilities	184,108						
Current assets	31,512																
Fixed assets	77,557																
Total assets	109,070																
Current liabilities	184,108																
Total liabilities	184,108																

## Accounting for Leases

Yen in thousands

FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
Finance lease transactions not involving a transfer of title to the lessee	—————
(1) Acquisition cost, accumulated depreciation and fiscal year-end balance equivalents of the leased property.	
Tools, furniture and fixtures	
Acquisition equivalents	4,884
Depreciation equivalents	4,884
Year-end balance equivalents	-
Total	
Acquisition equivalents	4,884
Depreciation equivalents	4,884
Year-end balance equivalents	-
(2) Outstanding lease commitments and the fiscal year-end balance equivalents	
Within one year	-
Over one year	-
Total	-
(3) Lease payments, depreciation and interest equivalents	
Lease payments	532
Depreciation	474
Interest	6
(4) Calculation of accumulated depreciation equivalents	
Depreciation is based on the straight-line method, assuming the lease period to be the useful life and no residual value.	
(5) Calculation of interest equivalents	
The difference between total lease payments and acquisition cost equivalent is treated as interest equivalent. It is allocated to each period using the simple-interest method.	

## Securities

As of March 31, 2003

### Securities classified as other securities

#### 1. Securities with market quotations

Yen in thousands

Security	Acquisition cost	Carrying value	Unrealized gain or loss
Securities whose carrying value exceeds their acquisition cost			
(1) Equity securities	-	-	-
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	-	-	-
Subtotal	-	-	-
Securities whose carrying value does not exceed their acquisition cost			
(1) Equity securities	18,860	18,860	-
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	94,800	79,600	(15,200)
Subtotal	113,660	98,460	(15,200)
Total	113,660	98,460	(15,200)

Note: In this fiscal year ended March 31, 2003, the impairment loss on securities with market quotations classified as "Other securities" totaled ¥32,120 thousand. All securities whose market values are at least 50% (inclusive) below book value on the current fiscal year balance sheet date are tested for impairment. All securities whose market values are at least 30% (inclusive) to 50% below book value on the current fiscal year balance sheet date are reviewed for impairment based on materiality of the security and prospects of recovery in market price.

#### 2. Securities sold during the current fiscal year

Yen in thousands

Total amount sold	Gains on sales	Losses on sales
61,267	10,150	-

#### 3. Securities without market quotations

Yen in thousands

	Carrying value
(1) Other securities	
Money management funds	924,701
Free financial funds	100,015
Medium-term government bond funds	82,101
Unlisted stock	22,090
Total	1,128,908

As of March 31, 2004

**Securities classified as other securities**

**1. Securities with market quotations**

Yen in thousands

Security	Acquisition cost	Carrying value	Unrealized gain or loss
Securities whose carrying value exceeds their acquisition cost			
(1) Equity securities	8,060	11,800	3,740
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	102,000	105,560	3,560
Subtotal	110,060	117,360	7,300
Securities whose carrying value does not exceed their acquisition cost			
(1) Equity securities	-	-	-
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	-	-	-
Subtotal	-	-	-
Total	110,060	117,360	7,300

**2. Securities sold during the current fiscal year**

Yen in thousands

Total amount sold	Gains on sales	Losses on sales
134,784	22,904	-

**3. Securities without market quotations**

Yen in thousands

	Carrying value
(1) Other securities	
Money management funds	998,513
Free financial funds	100,019
Medium-term government bond funds	2,104
Unlisted stock	11,354
Total	1,111,990

## **Derivatives**

### **FY2002 (From April 1, 2002 to March 31, 2003)**

#### **1. Matter concerning derivatives**

##### (1) Description

The Company employs foreign exchange forward contracts (currency exchange related). The Company also acquired certain yen-denominated corporate bonds with warrants.

##### (2) Policy

Derivatives are employed to hedge foreign currency exposures, but the Company establishes certain limits on derivatives positions. The Company also holds derivative instruments for speculative purposes.

##### (3) Objective

The Company employs foreign currency forward contracts to hedge exposure of exchange rate fluctuations on scheduled foreign currency denominated transactions. The Company also holds derivative instruments for speculative purposes. These include financial products with options contracts.

The Company accounts derivatives by the hedge accounting method. For details, see Section 5: Significant Accounting Policies in the Preparation of Consolidated Financial Statements.

##### (4) Risks

Foreign exchange transactions are exposed to the risk of exchange rate fluctuations. Exchangeable bonds are exposed to the stock price fluctuation risk.

##### (5) Risk management

An authorized executive approves all new derivative transactions the Company enters into.

#### **2. Market value of contract amounts**

No information is presented since the Company did not employ derivatives during the consolidated fiscal year.

### **FY2003 (From April 1, 2003 to March 31, 2004)**

No reportable information. The Group did not have any outstanding derivative positions as of the end of the consolidated fiscal year ended March 31, 2003.

## Retirement benefit

### 1. Description of retirement benefit plans

(1) Retirement benefit plans of the Company and its consolidated subsidiaries

The Company and its consolidated subsidiaries offer defined benefit plans, i. e., a tax-qualified pension plan, and a certain mutual aid retirement benefit plan, i. e., a defined contribution pension plan, covering substantially all employees. Other affiliates do not offer retirement benefit plans.

(2) Supplementary information

A. Mutual aid retirement benefit plan: Established 1979

The Company participates in the Mutual Aid Retirement Benefit Plan established by the Yokohama Chamber of Commerce to offer retirement benefits to employees retiring voluntarily.

Pension fund assets: ¥112,200 thousands

B. Tax-qualified pension plan: Established: 1985

To provide for retirement benefits, in addition to the above, to employees with three or more years of service, the Company offers the tax-qualified pension plan.

### 2. Principal components of retirement benefit obligations

Yen in thousands

	FY2002 As of March 31, 2003	FY2003 As of March 31, 2004
(1) Retirement benefit obligation	(27,158)	(29,049)
(2) Plan assets at fair value	27,139	29,158
(3) Reserve for employees' retirement benefits	(19)	-
(4) Prepaid pension costs	-	109

Note: Retirement benefit obligations are calculated using the Simple method.

### 3. Principal components of retirement benefit expenses

Yen in thousands

	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
(1) Service cost	2,404	1,899
(2) Contribution to mutual aid pension plan	11,824	11,825
Total	14,228	13,724

Note: Service cost is computed using the Simple method.

### 4. Matters concerning the accounting standards for retirement benefit obligations

FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
In the calculation of retirement benefit liabilities, in recent years, the Company has been using the fair value of pension assets as of the end of the term to estimate pension assets.	Same as on the left.

## Deferred tax accounting

Yen in thousand

FY2002 From April 1, 2002 to March 31, 2003		FY2003 From April 1, 2003 to March 31, 2004			
1. The significant components of deferred tax assets and liabilities		1. The significant components of deferred tax assets and liabilities			
Deferred tax assets		Deferred tax assets			
Enterprise tax payable	132	Reserve for directors' retirement benefits	65,568		
Reserve for directors' retirement allowance	64,820	Provision of depreciation and amortization in excess of maximum	10,222		
Inventories	16,566	Inventories	16,015		
Membership	8,504	Investment securities	4,358		
Provision of reserves for accrued bonuses in excess of maximum	17,127	Membership	8,546		
Organization expenses	6,835	Reserve for accrued bonuses	17,978		
Deficit carried forward	421,355	Deficit carried forward	289,931		
Retained earnings carried forward	5,977	Others	4,031		
Others	7,304	Subtotal deferred tax assets	416,653		
Subtotal deferred tax assets	548,623	Valuation allowance	(42,258)		
Valuation allowance	(129,660)	Total deferred tax assets	374,395		
Total deferred tax assets	418,963				
Deferred tax liabilities		Deferred tax liabilities			
Special depreciation reserve	(2,849)	Special depreciation reserve	(2,021)		
Program reserve	(30,100)	Program reserve	(22,573)		
Others	(1,887)	Other unrealized losses on other securities	(2,963)		
Total deferred tax liabilities	(34,837)	Others	(230)		
Net deferred tax assets (liabilities)	384,125	Total deferred tax liabilities	(27,789)		
		Net deferred tax assets (liabilities)	346,605		
Net deferred tax assets (liabilities) are included in the following consolidated balance sheet accounts		Net deferred tax assets (liabilities) are included in the following consolidated balance sheet accounts			
Current assets	Deferred tax assets	63,201	Current assets	Deferred tax assets	51,832
Fixed assets	Deferred tax assets	320,924	Fixed assets	Deferred tax assets	294,773
Current assets	Deferred tax liabilities	-	Current assets	Deferred tax liabilities	-
Long-term liabilities	Deferred tax liabilities	-	Long-term liabilities	Deferred tax liabilities	-
2. Significant sources of the difference in corporate and other tax liabilities as calculated according to the effective tax rate and tax-effect accounting		2. Significant sources of the difference in corporate and other tax liabilities as calculated according to the effective tax rate and tax-effect accounting			
Significant sources of difference are not presented since the Company reported net loss before income taxes in the consolidated fiscal year under review.		Statutory tax rate		42.0	
Regarding statutory tax rates applicable to timing differences as of the end of the year, 42.0% is applied to those differences which will have extinguish by the end of March 2004, and 40.4% thereafter.		Adjustments			
		Entertainment and other expenses in excess of tax allowable maximum		1.5	
		Dividends receivable and other items not to be included in income indefinitely.		(0.8)	
		Per capita Inhabitant Tax		3.3	
		Valuation reserve		31.9	
		Differences in tax rates		6.2	
		Equity in earnings/loss of non-consolidated subsidiaries		(2.0)	
		Gain on sale of subsidiary stock		(59.7)	
		Other		(0.1)	
		Effective tax rate		22.3	

FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
<p>3. Change of statutory tax rate</p> <p>Regarding statutory tax rates used in calculation of deferred tax assets and deferred tax liabilities, 42.0% are applied to those differences, which will have extinguish by the end of March 2004, and 40.4% thereafter. This is made in accordance with Law No.9 in Fiscal 2003 "Law regarding Amendment on Local Tax Law and Related enforcements" issued on March 31, 2003, by which external standard taxation was introduced to corporate income taxes in the fiscal year starting on April 1, 2004. Due to this change of tax rate, net deferred tax assets after deduction of deferred tax liabilities has decreased 12,558 thousand yen, which amount is booked as an increase under "income taxes – deferred."</p>	—————

## Segment Information

### 1. Segment information by operating segment

#### FY2002 (April 1, 2002 - March 31, 2003)

No reportable items. The Company and its major consolidated subsidiaries operate in a single industry commonly classified as electronics component manufacturing. These activities include manufacturing and marketing of components products related to communications and real-time operating systems.

#### FY2003 (April 1, 2003 - March 31, 2004)

No reportable items. The Company and its major consolidated subsidiaries operate in a single industry commonly classified as electronics component manufacturing. These activities include manufacturing and marketing of components products related to communications and real-time operating systems.

### 2. Geographical segment information

#### FY2002 (April 1, 2002 - March 31, 2003)

Yen in thousands

	Japan	N. America	Europe	Total	Elimination or Corporate	Consolidated
I. Net sales and operating income/ loss						
Net sales						
(1) Sales to external customers	1,599,767	282,352	6,316	1,888,436	-	1,888,436
(2) Inter-segment sales and transfers	308	63,094	-	63,402	[63,402]	-
Total	1,600,075	345,447	6,316	1,951,839	[63,402]	1,888,436
Operating expenses	1,517,151	388,977	21,793	1,927,922	[13,406]	1,914,515
Operating income (loss)	82,923	(43,529)	(15,476)	23,917	[49,996]	(26,079)
II. Assets	1,894,106	286,412	6,896	2,817,415	1,022,986	3,210,401

Notes: 1. Countries and regions are grouped together according to the proximity of their geographical locations.

2. The principal countries or areas included in each region, outside Japan, are as follows:

North America: U. S. A.                      Europe: France

3. Amount of unallocatable operating expenses included in eliminations or corporate is ¥42,393 thousand, and its significant components are representing expenses related to the administration division

4. Unallocatable assets included in eliminations or corporate total ¥1,288,004 thousands the principal components of which are idle funds under management (cash and securities available for sale) and assets of the administration division.

5. Supplementary information

(Amortization of goodwill)

Effective the current consolidated fiscal year ended March 31, 2003; overseas subsidiaries adopted SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 requires that goodwill no longer be amortized but instead tested for impairment at least annually. (See Significant Accounting Policies in the Preparation of Consolidated Financial Statements for the current consolidated fiscal year ended March 2003, Section 4. Accounting Standards, Subsection: B Depreciation and amortization of significant depreciable assets). The application of the new standards caused full year operating expenses in the North American operations to decline by ¥35,393 thousand and total assets to decrease by ¥569,392 thousand.

### FY2003 (April 1, 2003 - March 31, 2004)

Yen in thousands

	Japan	N. America	Europe	Total	Elimination or Corporate	Consolidated
I. Net sales and operating income/ loss						
Net sales						
(1) Sales to external customers	1,571,284	141,715	20,404	1,733,403	-	1,733,403
(2) Inter-segment sales and transfers	-	111,537	-	111,537	[111,537]	-
Total	1,571,284	253,252	20,404	1,844,940	[111,537]	1,733,403
Operating expenses	1,477,167	352,354	52,331	1,881,853	[70,639]	1,811,213
Operating income (loss)	94,117	(99,101)	(31,927)	(36,912)	[40,897]	(77,809)
II. Assets	-	-	-	-	-	-

Notes: 1. Countries and regions are grouped together according to the proximity of their geographical locations.

2. The principal countries or areas included in each region, outside Japan, are as follows:

North America: U. S. A. Europe: France

3. Amount of unallocatable operating expenses included in eliminations or corporate is ¥42,564 thousand, and its significant components are representing expenses related to the administration division

4. Asset allocation is not presented since the Company does not have consolidated subsidiaries or major branch offices in regions and countries other than Japan after the exclusion of the overseas subsidiary at the end of the current consolidated fiscal year.

### 3. Overseas sales

#### FY2002 (April 1, 2002 - March 31, 2003)

Yen in thousands

	North America	Other	Total
I. Overseas sales	262,860	42,077	304,937
II. Consolidated net sales	-	-	1,888,436
III. Weight of overseas sales in total consolidated net sales	13.92%	2.23%	16.15%

Notes: 1. Countries and regions are grouped together according to the proximity of their geographical locations.

2. The principal countries or areas included in each region, outside Japan, are as follows:

(1) North America: U.S.A., Canada (2) Other regions: Germany, Britain, Hong Kong and India, etc.

3. Overseas sales of the Company and its consolidated subsidiaries represent sales in countries and regions other than Japan.

#### FY2003 (April 1, 2003 - March 31, 2004)

Yen in thousands

	North America	Other	Total
I. Overseas sales	95,023	86,747	181,770
II. Consolidated net sales	-	-	1,733,403
III. Weight of overseas sales in total consolidated net sales	5.48%	5.01%	10.49%

Notes: 1. Countries and regions are grouped together according to the proximity of their geographical locations.

2. The principal countries or areas included in each region, outside Japan, are as follows:

(1) North America: U.S.A., Canada (2) Other regions: Germany, Britain, Hong Kong and India, etc.

3. Overseas sales of the Company and its consolidated subsidiaries represent sales in countries and regions other than Japan.

## Related Party Transactions

### FY2002 (April 1, 2002 - March 31, 2003)

Directors, principal individual shareholder and others

Yen in thousands

Type	Company etc. name	Address	Capital or investment	Activities or occupation	Voting rights (held)	Business relationship Joint director Transactions	Transaction description	Transaction amount	Item	Account balance
Directors and relatives	Seiichi Nobehara	/	/	Company director CEO IBT Co., Ltd.	None	/	Consultation and language services related to domestic business and overseas expansion Notes2	3,600	Accounts payable -other	315

- Notes: 1. Transaction amounts are exclusive of consumption taxes. Fiscal year-end account balances are inclusive of consumption taxes.  
2. Transactions are arms length.

### FY2003 (April 1, 2003 - March 31, 2004)

Directors, principal individual shareholder and others

Yen in thousands

Type	Company etc. name	Address	Capital or investment	Activities or occupation	Voting rights (held)	Business relationship Joint director Transactions	Transaction description	Transaction amount	Item	Account balance
Directors and relatives	Seiichi Nobehara	/	/	Company director CEO IBT Co., Ltd.	None	/	Consultation and language services related to domestic business and overseas expansion Notes2	3,600	Accounts payable -other	315

- Notes: 1. Transaction amounts are exclusive of consumption taxes. Fiscal year-end account balances are inclusive of consumption taxes.  
2. Transactions are arms length.

## Amounts Per Share

Yen

FY 2002 From April 1, 2002 to March 31, 2003		FY 2003 From April 1, 2003 to March 31, 2004	
Net assets per share	558.56	Net assets per share	576.02
Net loss per share	78.81	Net income per share	29.51
Net income per share (diluted) is not presented since the company reported net loss per share for the fiscal year.		Diluted net income per share is not reported since the Company has no outstanding securities with dilutive effect.	
Corporate Accounting Standard No.2 "Accounting Standard on Net Income per Share" and Corporate Accounting Standard Procedure No.4 "Accounting Standard Procedure on Net Income per Share, have been adopted from the current fiscal year under review. There is no impact caused by the change.			

Note: The basis of calculation of net income / net loss per share and the diluted net income / net loss per share for the period is as follows.

Yen in thousands

	FY2002 From April 1, 2002 to March 31, 2003	FY2003 From April 1, 2003 to March 31, 2004
Net income (loss) for the period	(392,471)	142,148
Equity in net loss not account of common shareholders	-	-
Common stock in net income (loss)	(392,471)	142,148
Average number of shares outstanding for the period (1,000 shares)	4,979	4,816
Details on potential stock not included in the calculation of diluted net earnings per share since there is no dilution.	Pursuant to Article 280-19 of the Commercial Code of Japan, the Company has only one type of share acquisition right by way of stock options outstanding (Shares to be issued upon execution of share acquisition rights: Common shares, Number of shares to be issued upon execution of share acquisition rights: 179,000 shares)	Pursuant to Article 280-19 of the Commercial Code of Japan, the Company has only one type of share acquisition right by way of stock options outstanding (Shares to be issued upon execution of share acquisition rights: Common shares, Number of shares to be issued upon execution of share acquisition rights: 160,000 shares)

## Subsequent events

Not applicable.

## 6. Production, Orders Received and Net sales

### (1) Production

Yen in thousands

Product category	FY 2002		FY 2003		YoY change (%)
	From April 1, 2002 to March 31, 2003		From April 1, 2003 to March 31, 2004		
Manufactured products					
Communications		328,547		667,510	203.2
Internet protocol		880,368		461,916	52.5
Real-time OS		278,424		60,748	21.8
SI (customized)		574,423		641,281	111.6
<b>Total</b>		<b>2,061,764</b>		<b>1,831,456</b>	<b>88.8</b>

- Notes: 1. Amounts are calculated based on sales prices.  
2. The above amounts do not include consumption taxes.

### (2) Procurement

Yen in thousands

Product category	FY 2002		FY 2003		YoY change (%)
	From April 1, 2002 to March 31, 2003		From April 1, 2003 to March 31, 2004		
Others		100,219		152,935	152.6
<b>Total</b>		<b>100,219</b>		<b>152,935</b>	<b>152.6</b>

- Notes: 1. Amounts are calculated based on sales prices.  
2. The above amounts do not include consumption taxes.

### (3) Orders received

Yen in thousands

Product category	FY 2002		FY 2003		
	From April 1, 2002 to March 31, 2003		From April 1, 2003 to March 31, 2004		
	Orders received	Order backlog	Orders received	Order backlog	YoY change (%)
Manufactured products					
Communications	410,162	115,956	386,988	119,231	102.8
Internet protocol	562,357	21,433	512,092	78,615	366.8
Real-time OS	170,119	14,054	75,450	38,590	274.6
SI (customized)	698,116	273,916	411,287	9,110	3.3
<b>Subtotal</b>	<b>1,840,756</b>	<b>425,359</b>	<b>1,385,819</b>	<b>245,546</b>	<b>57.7</b>
Purchased products					
Others	146,565	27,359	151,201	11,969	43.5
<b>Total</b>	<b>1,987,321</b>	<b>1,537,020</b>	<b>1,537,020</b>	<b>257,515</b>	<b>56.9</b>

- Notes: 1. Amounts are calculated based on sales prices.  
2. The above amounts do not include consumption taxes.

### (4) Net sales

Yen in thousands

Product category	FY 2002		FY 2003		YoY change (%)
	From April 1, 2002 to March 31, 2003		From April 1, 2003 to March 31, 2004		
Manufactured products					
Communications		405,249		353,638	87.3
Internet protocol		526,121		503,213	95.6
Real-time OS		249,765		79,154	31.7
SI (customized)		579,757		618,313	106.7
<b>Subtotal</b>		<b>1,760,893</b>		<b>1,554,320</b>	<b>88.3</b>
Purchased products					
Others		127,543		179,083	140.4
<b>Total</b>		<b>1,888,436</b>		<b>1,733,403</b>	<b>91.8</b>

- Notes: 1. Amounts are calculated based on sales prices.  
2. Sales by major customer are not presented since no single customer represented more than 10% of aggregate net sales in the current consolidated interim period.  
3. The above amounts do not include consumption taxes.

\* This financial report is solely a translation of summary of "Kessan Tanshin" (in Japanese, including attachments), which has been prepared in accordance with accounting principles and practices generally accepted in Japan, for the convenience of readers who prefer an English translation.