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**宝印刷株式会社**

# Kyokuto Kaihatsu Kogyo Co., Ltd.

# Annual Report 2003

Year ended March 31, 2003

# FINANCIAL HIGHLIGHTS

Years ended March 31, 2003 and 2002

| | Millions of yen | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|
| | **2003** | 2002 | **2003** |
| **For the Year:** | | | |
| Net Sales | **55,269** | 47,982 | **459,812** |
| Operating income | **1,759** | 474 | **14,634** |
| Net income | **201** | 84 | **1,677** |
| **At Year-end:** | | | |
| Total assets | **78,943** | 76,360 | **656,767** |
| Total shareholders' equity | **52,737** | 52,512 | **438,750** |

| | Yen | | U.S. dollars (Note 1) |
|---|---|---|---|
| | **2003** | 2002 | **2003** |
| **Amounts per Share of Common Stock** (Note 2)**:** | | | |
| Net Income | **5.94** | 2.96 | **0.05** |
| Cash dividend attributable to the year | **6.00** | 6.00 | **0.05** |

Note 1. U.S. dollar amounts are translated for convenience only, at the rate of ¥120.20 to US$1.

2. The computations of net income per share of common stock are based on the weighted average number of shares outstanding during each year.

# CONTENTS

# TO OUR SHAREHOLDERS

## 1. Summary of Operations

We are pleased to report the business results of Kyokuto Kaihatsu Kogyo Co., Ltd. For the year ending March 31, 2003.

Katsushi Tanaka

Yoshihiro Tokunaga

### (1) Business Results

Japanese economy in this fiscal year has remained in a difficult situation with diminishing consumer spending and corporate investment that are caused by various factors such as prolonged deflation, disposal of the non-performing loans, depressed share prices in the market, deceleration of US economy, and spiraling military tensions in Iraq.

Special purpose vehicle business suffered a difficult situation in the first half of the year because of successive drop of truck demand. However, in the second half of the year, it experienced a slight recovery created by substitute demands anticipating gaseous emission control in Tokyo metropolitan area and increasing exports centered around China.

Environmental equipment and system business expected potential demands to be actualized by requirement for solving the problems related to dioxin and final processing site of waste disposal. But serious financial circumstances of each local government caused an increasingly fierce competition among the industry and consequently we had difficulties to get orders having a normal level of profitability.

Such being the circumstances, we have tried to expand our corporate value by efficient capital operation and improved profitability in the framework of our Medium-Range Management Planning “Plan 2001”. In this direction, we have made every effort to improve the business performance by developing new products, strengthening sales and service forces, reducing costs, expanding export business, and utilizing unused land.

Also, to reduce drastically the expenditure related to special purpose vehicle business, we established an overseas office as a purchasing base in China (Shanghai) in November 2002 and made a full-fledged start in purchasing parts and material from China.

Our business results in the consolidated basis thus obtained in this fiscal year are shown below in comparison with the last fiscal year: The sales revenue is 55,260 million yen achieving year-on-year increase of 7,280 million yen (+15%) mainly because of the increases of special purpose vehicles export to China and of plant construction sales of environmental equipment and systems. The ordinary income is 1,620 million yen achieving year-on-year increase of 1,110 million yen (+218%) along with the sales increase. However, the net income remains 200 millions yen making year-on-year increase of 110 million yen (+138%) because of the loss from revaluation of investment securities affected by the depressed stock prices in the market.

The summary of each business segment in the consolidated basis is reported below in comparison with the last fiscal year.

#### <Specialty Truck Division>

Our special purpose vehicle business suffered continued weak demand of trucks in the first half of the year. However in the second half of the year, the substitute demands anticipating gaseous emission control in Tokyo metropolitan area and the large-scale increase of export sales of construction-related trucks such as concrete pump and mixer trucks focusing mainly on China boosted the annual sales drastically. Consequently, the sales revenue is 32,330 million yen achieving year-on-year increase of 2,840 million yen (+10%). The operating income is 170 million yen achieving year-on-year increase of 540 million yen as a result of sales increase and cost-reduction recovering from the loss of 370 million yen of the last fiscal year.

#### <Environmental Equipment and Systems Division>

In a difficult market situation, our environmental equipment and systems business made every effort to maintain the appropriate level of the sales and orders received through various sales activities in recycle plaza and recycle center that are our mainline business, plant-related equipment such as RDF (Refuse Derived Fuel) equipment and leachate treatment facilities in final disposal sites, contracted business for maintenance and operation, and melting furnace for gasifying the waste that is our new business.

As a result, the sales revenue of environmental equipment and systems business is 14,830 million yen achieving year-on-year increase of 3,860 million yen (+35%) through steady growth of plant construction and increased sales of repair and maintenance. The operating income is 1,240 million yen achieving year-on-year increase of 510 million yen (+70%). On the other hand, the amount of orders received is 10,280 million yen causing year-on-year decrease of 770 million yen (-7%) because the order entry for recycle plaza and recycle center dropped down to 5 units although we received an order for the first melting furnace for gasifying the waste and 6 orders for operation contract.

#### <Automobile Sales Division>

For automobile sales business, we have enhanced sales and service capabilities to maintain the sales revenue as well as made every effort of cost reduction to improve the profitability. However, new vehicle sales decreased due to diminishing consumer spending. Consequently the sales revenue is 6,530 million yen making year-on-year decrease of 390 million yen (-6%). The operating loss is 70 million yen making year-on-year decrease of 110 million yen being affected by the sales revenue decline.

#### <Real Estate Rental Division>

Our company has been managing the real estate rental business long before to utilize effectively some of company owned assets. As its business scale expands, we have established newly real estate rental business as an independent section.

This business section has increased its sales revenue drastically. The income from lease of a shopping center that has been constructed in Mizuho-cho, Nishitama-gun, Tokyo and rented out to the Seiyu, Ltd. has mainly contributed in this sales increase.

As a result, the sales revenue of real estate rental business is 1,950 million yen achieving year-on-year increase of 990 million yen (+104%). The operating income is 390 million yen achieving year-on-year increase of 330 million yen (+642%).

### (2) State of Cash Flows

Cash and cash equivalent at the end of the current consolidated fiscal year including 520 million yen of net profit before adjustment of tax is 10,450 million yen making year-on-year decrease of 4,460 million yen (-30%) due to the increased sales credits and the expenditure for acquisition of fixed assets and company's own stocks. The breakdown of the total is as follows.

#### <Cash Flows from Operating Activities>

Operating activities during the current consolidated fiscal year have resulted in cash outflow of 330 million yen (year-on-year decrease of cash inflow of 3,960 million yen). This is because the sales credits have increased drastically through the sales increase in the second half of the year.

#### <Cash Flows from Investing Activities>

Investing activities during the current consolidated fiscal year have resulted in cash outflow of 3,670 million yen (year-on-year decrease of cash inflow of 440 million yen). This is because the cash outflow required for acquisition of fixed assets and securities is larger than the cash inflow created by sales of fixed assets and securities.

#### <Cash Flows from Financing Activities>

Financing activities during the current consolidated fiscal year have resulted in cash outflow of 460 million yen (year-on-year increase of cash inflow of 290 million yen). This is mainly because of acquisition of company's own stocks.

## 2. Concept and Practice related to Corporate Governance

Our company group is implementing reorganization of management system aiming at speedy decision making of management policy and strategy to meet the changing business environment, enhancement of supervisory function, and system reinforcement for business of corporation.

In respect to management system, we introduced operating officer system in June 2002 and are now performing business operation in this new management system. Based on this, we have reduced the limit number of directors stipulated in the statute of corporation from 20 to 12 directors in order to optimize the number of board members. Also, we have shortened the term of directors from two years to one year in our company and all our affiliate companies.

In respect to the audit system, we have adopted an auditor system and will increase the number of company auditors from three to four auditors after the general meeting of shareholders to be held in June 2003. The three auditors out of the four are outside auditors (currently two outside auditors).

## 3. Our objectives to challenge

Japanese economy will remain in a difficult situation because of various factors such as the worsening employment situation, weakness of the stock market, post-war problems in Iraq, depressed US economy, etc. while the recovery of corporate performance in limited companies and of corporate investment can be expected.

Such being the circumstances, our special purpose vehicle business can expect an expansion of sales revenue to be created by increasing truck demands resulted from the gaseous emission control focusing on Tokyo metropolitan area as well as increasing export sales generated by active construction investment in China. In respect to the environmental equipment and systems business, increasingly fierce competition is to be expected but at the same time the expansion of environmental investment can be expected.

We will steadily challenge various objectives by utilizing proactively the corporate resources. Such objectives include: increase of order reception and sales of special purpose vehicle and environmental equipment and systems business, development of new products, enhancement of service system, promotion of parts procurement in overseas, total cost reduction, etc. Thus, we will make our best to improve our business performance while developing the synergy effect with our group companies in order to assure the expansion of corporate value and successive development.

June, 2003

Yoshihiro Tokunaga

Yoshihiro Tokunaga
Chairman

Katsushi Tanaka
President

# CONSOLIDATED STATEMENTS OF INCOME AND RETAINED EARNINGS

Years ended March 31, 2003 and 2002

| | Millions of yen | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|
| | **2003** | 2002 | **2003** |
| **Net sales** | **55,269** | 47,982 | **459,812** |
| **Cost of sales** | **44,481** | 38,841 | **370,061** |
| Gross profit | **10,788** | 9,140 | **89,751** |
| Selling, general and administrative expenses | **9,028** | 8,666 | **75,116** |
| **Operating income (loss)** | **1,759** | 474 | **14,634** |
| **Other income (expenses)** | | | |
| Interest and dividend income | **45** | 50 | **378** |
| Interest expenses | **(94)** | (28) | **(782)** |
| Gain (loss) on sales of property and equipment | **776** | (31) | **6,462** |
| Gain (loss) on sales of securities | **(142)** | 72 | **(1,187)** |
| Write-down of investment securities | **(2,003)** | — | **(16,671)** |
| Other-net | **187** | (137) | **1,559** |
| **Income (loss) before income taxes** | **528** | 399 | **4,393** |
| **Income taxes** (Note 12) | | | |
| current | **290** | 424 | **2,420** |
| deferred (prepaid), net | **52** | (112) | **439** |
| Total income taxes | **343** | 311 | **2,860** |
| **Minority interest** | **(17)** | 2 | **(143)** |
| **Net income (loss)** | **201** | 84 | **1,677** |
| **Retained earnings:** | | | |
| Balance at beginning of period | **29,645** | 29,757 | **246,638** |
| Cash dividends paid | **(169)** | (171) | **(1,409)** |
| Bonuses to directors and statutory auditors | **(26)** | (24) | **(222)** |
| Adjustment of retained earnings for eliminations of treasury stock | **(8)** | — | **(74)** |
| Balance at end of period | **29,642** | 29,645 | **246,610** |

| | Yen | | U.S. dollars |
|---|---|---|---|
| **Per share of common stock:** | | | |
| Net income (loss) | **5.94** | 2.96 | **0.05** |
| Diluted net income (loss) | **5.94** | — | **0.05** |
| Cash dividend, applicable to earnings of the year | **6.00** | 6.00 | **0.05** |

*The accompanying notes are an integral part of this statements.*

# CONSOLIDATED BALANCE SHEETS

Years ended March 31, 2003 and 2002

| | Millions of yen | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|
| | **2003** | 2002 | **2003** |
| **ASSETS** | | | |
| **Current assets:** | | | |
| Cash and time deposits | **5,911** | 6,104 | **49,182** |
| Short-term investments (Note 3) | **4,616** | 8,991 | **38,407** |
| Trade note and accounts receivable | **24,836** | 19,972 | **206,623** |
| Less: Allowance for doubtful accounts | **(64)** | (82) | **(533)** |
| Inventories | **5,428** | 5,413 | **45,158** |
| Deferred income taxes (Note 12) | **555** | 386 | **4,624** |
| Prepaid expenses | **69** | 102 | **574** |
| Other current assets | **487** | 157 | **4,059** |
| **Total current assets** | **41,841** | 41,046 | **348,096** |
| **Investments and other assets:** | | | |
| Investments in securities (Note 3) | **3,575** | 3,268 | **29,746** |
| Deferred income taxes (Note 12) | **282** | 651 | **2,347** |
| Other | **3,793** | 3,546 | **31,556** |
| **Total investments and other assets** | **7,650** | 7,466 | **63,650** |
| **Property and equipment:** | | | |
| Land | **12,386** | 10,551 | **103,045** |
| Buildings and structures | **24,228** | 24,617 | **201,570** |
| Machinery and equipment | **6,953** | 6,627 | **57,847** |
| Construction in progress | **576** | 142 | **4,797** |
| Other | **2,254** | 2,211 | **18,753** |
| | **46,398** | 44,150 | **386,014** |
| Less — Accumulated depreciation | **(17,219)** | (16,750) | **(143,260)** |
| **Total property and equipment** | **29,179** | 27,399 | **242,753** |
| **Intangible assets** | | | |
| Cost in excess of net assets of subsidiaries | **40** | 213 | **332** |
| Other | **232** | 234 | **1,933** |
| **Total intangible assets** | **272** | 447 | **2,266** |
| **Total assets** | **78,943** | 76,360 | **656,767** |

| | Millions of yen | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|
| | **2003** | 2002 | **2003** |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | | |
| **Current liabilities:** | | | |
| Short-term bank loans (Note 4) | **2,608** | 2,428 | **21,697** |
| Current portion of long-term debt (Note 4) | **98** | — | **815** |
| Trade note and account payable | **12,354** | 9,981 | **102,780** |
| Accrued income and other taxes | **706** | 472 | **5,880** |
| Accrued expenses | **1,758** | 1,712 | **14,625** |
| Other current liabilities | **1,424** | 1,753 | **11,848** |
| **Total current liabilities** | **18,949** | 16,347 | **157,648** |
| **Long-term liabilities:** | | | |
| Long-term debt (Note 4) | **112** | 308 | **931** |
| Accrued retirement benefits (Note 5) | **1,726** | 1,685 | **14,359** |
| Directors' and statutory auditors' retirement benefits | **341** | 283 | **2,841** |
| Net assets of subsidiaries in excess of cost | **1** | 45 | **11** |
| Deferred income taxes (Note 12) | **286** | — | **2,383** |
| Other long-term liabilities | **4,578** | 4,948 | **38,090** |
| **Total long-term liabilities** | **7,045** | 7,270 | **58,618** |
| **Minority interests** | **210** | 229 | **1,749** |
| **Shareholders' equity:** | | | |
| Common stock, no par value (Note 10) | | | |
| Authorized — 120,000,000 shares | | | |
| Issued — 28,165,779 shares in 2003 and 28,310,779 shares in 2002 | **11,786** | 11,786 | **98,056** |
| Additional paid-in capital (Note 10) | **11,508** | 11,613 | **95,741** |
| Retained earnings | **29,642** | 29,645 | **246,610** |
| Net unrealized holding gains on securities | **70** | (533) | **588** |
| Treasury stock, at cost | **(270)** | — | **(2,246)** |
| **Total shareholders' equity** | **52,737** | 52,512 | **438,750** |
| **Total liabilities and shareholders' equity** | **78,943** | 76,360 | **656,767** |

# CONSOLIDATED STATEMENT OF CASH FLOWS

Years ended March 31, 2002, 2001 and 2000

| | Millions of yen | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|
| | **2003** | 2002 | **2003** |
| **Operating activities:** | | | |
| Net income before income taxes | **528** | 399 | **4,393** |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | | |
| Depreciation and amortization | **1,301** | 1,173 | **10,823** |
| Write-down of investment securities | **2,049** | 29 | **17,051** |
| Net gains (loss) on sales of marketable securities and investments | **124** | (72) | **1,034** |
| Net gains (loss) on sales of property | **(788)** | 22 | **(6,559)** |
| Provision (reversal) for accrued retirement benefits | **98** | 75 | **818** |
| Interest and dividend income | **(45)** | (49) | **(378)** |
| Interest expenses | **94** | 28 | **782** |
| Decrease (increase) in accounts receivable | **(3,998)** | (111) | **(33,265)** |
| Decrease (increase) in inventories | **(3)** | (507) | **(29)** |
| Decrease (increase) in prepaid expenses | **(247)** | 27 | **(2,061)** |
| Decrease (increase) in accounts payable | **2,216** | 111 | **18,443** |
| Decrease (increase) in accrued expenses | **(388)** | (78) | **(3,233)** |
| Decrease (increase) in income taxes payable | **374** | 4 | **3,116** |
| Other,net | **(1,181)** | 2,850 | **(9,826)** |
| **Sub total** | **133** | 3,901 | **1,110** |
| Interest and dividend income received | **42** | 53 | **350** |
| Interest expenses paid | **(29)** | (32) | **(245)** |
| Income taxes paid | **(434)** | (204) | **(3,611)** |
| Other,net | **(42)** | (78) | **(352)** |
| **Net cash provided by operating activities** | **(330)** | 3,639 | **(2,749)** |
| **Investing activities:** | | | |
| Decrease (increase) in time deposits | **—** | 1,277 | **—** |
| Payment for purchase of marketable securities and investments | **(1,791)** | (382) | **(14,905)** |
| Proceeds from sales of marketable securities and investments | **492** | 240 | **4,101** |
| Payment for purchase of facilities | **(3,141)** | (5,153) | **(26,133)** |
| Proceeds from sale of facilities | **1,159** | 783 | **9,646** |
| Disbursement of loan receivables | **(401)** | (1) | **(3,342)** |
| Collection of loan receivables | **7** | 7 | **58** |
| **Net cash provided by (used in) investing activities** | **(3,675)** | (3,229) | **(30,574)** |
| **Financing activities:** | | | |
| Increase (decrease) in short-term debt | **180** | 40 | **1,497** |
| Proceeds from long-term debt | **—** | 189 | **—** |
| Payment on long-term debt | **(98)** | (604) | **(815)** |
| Proceeds from issuance of common stock | **0** | — | **5** |
| Purchases of treasury stock | **(375)** | (211) | **(3,124)** |
| Dividends paid | **(170)** | (173) | **(1,416)** |
| **Net cash provided by (used in) financing activities** | **(463)** | (759) | **(3,853)** |
| **Effect of exchange rate change on cash and cash equivalents** | **—** | — | **—** |
| **Net increase in cash and cash equivalents** | **(4,469)** | (349) | **(37,177)** |
| **Cash and cash equivalents at beginning of year** | **14,927** | 15,246 | **124,185** |
| **Increase in cash and cash equivalents by increase of number of consolidated subsidiaries** | **—** | 30 | **—** |
| **Cash and cash equivalents at end of year** | **10,458** | 14,927 | **87,007** |

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 1. Basis of Presenting Consolidated Financial Statements

Kyokuto Kaihatu Co.,Ltd (the "Company") and its domestic subsidiaries maintain their accounts and records in accordance with the provisions set forth in the Commercial Code of Japan (the "Code") and the Securities and Exchange Law and in conformity with accounting principles and practices generally accepted in Japan.

The accompanying consolidated financial statements are prepared based on the consolidated financial statements of the Company and its subsidiaries (the "Group") which were filed with the Director of Kanto Local Finance Bureau as required by the Securities and Exchange Law.

In preparing the accompanying consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan.

The translation of the Japanese yen amounts into U.S. dollars is included solely for the convenience of the reader, using the approximate exchange rate at March 31, 2003, which was ¥120.20 to US$1.00. These convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

As permitted by the regulations under the Securities and Exchange Law of Japan, amounts of less than one million yen have been omitted. As a result, the totals shown in the accompanying consolidated financial statements (both in yen and in U.S.dollars) do not necessarily agree with the sums of the individual amounts.

## 2. Summary of Significant Accounting Policies

### (a) Consolidation Principles:

The consolidated financial statements include the accounts of the Company and its significant subsidiaries in accordance with the Securities and Exchange Law and related regulations of Japan. The minor differences arising from the cost of the companies' investments in subsidiaries and affiliates over the equity in their net assets at fair value are charged or credited to income in the year of acquisition. Significant differences are, as a rule, amortized over periods of 5 years. All significant inter-company accounts and transactions have been eliminated.

Investments in associates are accounted for by the equity method whereby the Group includes in net income its share of income or losses of these companies, and records its investments at cost adjusted for its share of income, losses or dividends received.

### (b) Consolidated Statement of Cash Flows:

In preparing the consolidated statements of cash flows, cash on hand, readily-available deposits and short-term highly liquid investments with maturity of not exceeding three months at the time of purchase are considered to be cash and cash equivalents.

### (c) Short-term investments and Investments in Securities:

For the Accounting Standards for Financial Instruments which was issued by the Business Accounting Deliberation Council, securities are classified into three categories: trading securities, held-to-maturity debt securities, equity investments in associates and other securities.

Those classified as other would be reported at fair value with unrealized gains, net of related taxes reported in equity. Under the Code, unrealized holding gains on securities, net of related taxes is not available for distribution as dividends and bonuses to directors and corporate auditors.

Other investments are carried at cost. The cost is determined by the moving average method.

(Trading securities)

Trading securities are held for resale in anticipation of short-term market movements. Trade securities, consisting of debt and marketable equity securities, are stated at fair value. Gains and losses, both realized and unrealized, are charged to income.

(Held-to-maturity debt securities and other securities)

Management determines the appropriate classification of debt securities at the time of purchase and reevaluates the classification as of each balance sheet date. Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Held-to-maturity debt securities are stated at amortized cost adjusted for the amortization of premiums and the accretion of discounts to maturity.

Marketable equity securities and debt securities not classified as held-to-maturity are classified as other securities. Other securities are carried at fair value with the unrealized gains and losses, net of tax, reported in a separate component of shareholders' equity. The amortized cost of debt securities in this category is adjusted for the amortization of premiums and the accretion of discounts to maturity. Realized gains and losses and declines in value judged to be other than temporary on other securities are charged to income.

(Golf club membership)

An impairment loss on deposits for golf club membership is required to be recognized in accordance with the new standard.

**(d) Inventories:**

Merchandise inventories are stated at cost, determined by the specific identification method. Materials and work in process are stated at cost, determined by the periodic average method. Supplies are stated at cost, determined by the last purchase cost method.

**(e) Depreciation:**

Depreciation is principally computed on the declining-balance method, based on the estimated useful lives of assets which are prescribed by Japanese income tax laws. Buildings are depreciated on a straight-line basis.

Amortization of intangible assets is computed by the straight-line method over periods prescribed primarily by the Japanese Commercial Code or Japanese income tax laws.

**(f) Stock and bond issue expenses:**

Stock and bond issue expenses are charged to income as incurred.

**(g) Accrued Retirement Benefits:**

To provide for the payment of retirement benefits and pension plans to employees, the Company and certain consolidated subsidiaries have entered an amount into a reserve equivalent to the amount recognized as necessary at the end of the period under review based on the expected retirement and severance obligations and the assets of pension plans at fiscal year-end.

The Company and its domestic subsidiaries provide for lump-sum severance benefits with respect to directors and corporate auditors. While the Company has no legal obligation, it is a customary practice in Japan to make lump-sum payments to a director or a corporate auditor upon retirement. Annual provisions are made in the accounts for the estimated costs of this termination plan, which is not funded. Any amounts payable to officers upon retirement are subject to approval at the shareholders' meeting.

**(h) Construction Contract:**

The construction contract takes longer than one year and the contract amount exceeded ¥0.5 billion, the percentage of completion method is applied.

**(i) Leases:**

In Japan finance leases other than those that are deemed to transfer the ownership of the leased assets to lessees are accounted for by a method similar to that applicable to ordinary operating leases.

**(j) Research and Development and Computer Software:**

Research and development expenditure is charged to income when incurred.

Expenditure relating to computer software developed for internal use is charged to income when incurred, except if it contributes to the generation of income or to future cost savings. Such expenditure is capitalized as an asset is amortized using the straight-line method over its estimated useful life which is in the range of 3 to 5 years.

**(k) Income Taxes:**

Income taxes consist of corporation, inhabitants and enterprise taxes for domestic companies and foreign income taxes.

Deferred income taxes are provided for the income tax expenses under the asset and liability method. Deferred income tax assets and liabilities are determined based on temporary differences between the financial statements and tax bases of assets and liabilities, using enacted tax rates in effect during the years in which the differences are expected to reverse, and on available tax credits carryforward.

**(l) Per Share Information**

The computation of basic net income per share is based on the weighted average number of shares of common stock outstanding during each period. The average number of shares used in the computation was 28,098 thousand shares for 2003 and 28,310 thousand shares for 2002.

Through March 31, 2002, diluted net income per share is not disclosed because potentially dilutive securities are not issued.

For the year ended 31, 2003, fully diluted net income per share of common stock assumes full exercise of right of the outstanding stock option plan at the beginning of the year.

Cash dividends per share shown in the statements of income are the amounts applicable to the respective years.

## 3. Short-Term Investments, Investments in Securities and Investments in and Advances to associates:

Short-term securities at March 31, 2003 and 2002 consisted of the following:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| Market value available: | | | |
| Trading securities ....... | ¥ 101 | ¥ 199 | $ 841 |
| Market value not available: | | | |
| M.M.F. and F.F.F. ....... | ¥4,515 | ¥7,792 | $37,566 |
| COMERCIAL PAPER ....... | — | ¥ 999 | — |
| Total .......................... | ¥4,616 | ¥8,991 | $38,407 |

| | Millions of yen<br>March 31, 2003<br>Other securities | | | |
|---|---|---|---|---|
| | Cost | Gross unrealized gains | Gross unrealized losses | Book Value (Estimated fair value) |
| Market value available: | | | | |
| Equity securities ........ | ¥ 2,383 | ¥ 256 | ¥ 135 | ¥ 2,504 |
| Bonds and debentures ... | — | — | — | — |
| Other securities ......... | — | — | — | — |
| | ¥ 2,383 | ¥ 256 | ¥ 135 | ¥ 2,504 |
| Market value not available | | | | 1,070 |
| Total .......................... | | | | ¥ 3,575 |

| | Thousands of U.S. dollars<br>March 31, 2002<br>Other securities | | | |
|---|---|---|---|---|
| | Cost | Gross unrealized gains | Gross unrealized losses | Book Value (Estimated fair value) |
| Market value available: | | | | |
| Equity securities ........ | ¥ 4,083 | ¥ 418 | ¥ 1,334 | ¥ 3,167 |
| Bonds and debentures ... | — | — | — | — |
| Other securities ......... | — | — | — | — |
| | ¥ 4,083 | ¥ 418 | ¥ 1,334 | ¥ 3,167 |
| Market value not available | | | | 101 |
| Total .......................... | | | | ¥ 3,268 |

| | Thousands of U.S. dollars | | | |
|---|---|---|---|---|
| | March 31, 2003 | | | |
| | Other securities | | | |
| | Cost | Gross unrealized gains | Gross unrealized losses | Book Value (Estimated fair value) |
| Market value available: | | | | |
| Equity securities ........ | $ 19,830 | $ 2,133 | $ 1,126 | $20,837 |
| Bonds and debentures ... | — | — | — | — |
| Other securities ......... | — | — | — | — |
| | $ 19,830 | $ 2,133 | $ 1,126 | $20,837 |
| Market value not available | | | | 8,908 |
| Total .......................... | | | | $29,746 |

## 4. Short-term bank loans and long-term debt:

The annual average interest rates applicable to short-term bank loans at March 31, 2003 and 2002 are 0.86% and 1.25%, respectively.

Long-term debt at March 31, 2003 and 2002 consisted of the following:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| 1.33% bank loans due 2004 ...................... | ¥ 98 | — | $ 815 |
| 1.08% bank loans due 2009 ...................... | ¥ 112 | ¥ 308 | $ 931 |
| 1.50% guarantee money due 2023 ...................... | ¥3,056 | ¥2,903 | $25,431 |
| | ¥3,266 | ¥3,211 | $27,178 |

Aggregate annual maturities of long-term debt subsequent to March 31, 2003 are as follows:

| Year ending March 31 | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| 2004 .......................................... | ¥ 98 | $ 815 |
| 2005 .......................................... | 41 | 341 |
| 2006 .......................................... | 18 | 149 |
| 2007 .......................................... | 18 | 149 |
| 2008 and thereafter ..................... | 3,091 | 25,722 |
| | ¥ 3,266 | $ 27,178 |

## 5. Accrued Retirement Benefits

The following tables sets forth the changes in benefit obligation, plan assets and funded status of the Company and its subsidiaries at March 31, 2003 and 2002.

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| Benefit obligation at end of year ......................... | ¥ 5,273 | ¥ 5,207 | $43,876 |
| Fair value of plan assets at end of year .............. | 2,711 | 3,167 | 22,557 |
| Funded status: | | | |
| Benefit obligation in excess of plan assets ..... | 2,562 | 2,039 | 21,319 |
| Unrecognized net transition obligation at date of adoption .......... | — | — | — |
| Unrecognized prior service cost .................. | — | — | — |
| Unrecognized actuarial loss .............................. | 849 | 368 | 7,065 |
| Prepaid expenses for plan assets at end of year ...... | (12) | (13) | (106) |
| Accrued pension liability recognized in the consolidation balance sheets ............. | 1,726 | 1,685 | 14,359 |

Note: Some domestic subsidiaries have adopted allowed alternative treatment of the accounting standards for retirement benefit for small business entity.

Severance and pension costs of the Company and its subsidiaries included the following components for the year ended March 31, 2003 and 2002.

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| Service cost .................. | ¥ 260 | ¥ 253 | $ 2,168 |
| Interest cost .................. | 153 | 157 | 1,280 |
| Expected return on plan assets ....................... | (65) | (79) | (544) |
| Amortization: | | | |
| Transition obligation at date of adoption ....... | — | — | — |
| Prior service cost ....... | — | — | — |
| Actuarial losses ......... | 75 | 45 | 630 |
| Net periodic benefit cost | ¥ 424 | ¥ 376 | $ 3,535 |

Assumption used in the accounting for the defined benefit plans for the year ended March 31, 2003 and 2002 is as follows:

| | 2003 | 2002 |
|---|---|---|
| Method of attributing benefit to periods of service | straight-line basis | straight-line basis |
| Discount rate ................................ | 2.5% | 3.0% |
| Long-term rate of return on fund assets .................................... | 3.0% | 3.0% |
| Amortization period for transition obligation at date of adoption ........ | — | — |
| Amortization period for prior service cost .................................. | — | — |
| Amortization period for actuarial losses ........................................... | 10 years | 10 years |

## 6. Contingencies

At March 31, 2003 and 2002, the Group was contingently liable as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| As an endorser of notes discounted or endorsed | ¥1,719 | ¥2,219 | $14,307 |
| As a guarantor of indebtedness of: | | | |
| Associates ................. | ¥ 450 | ¥ 450 | $ 3,743 |
| Others ....................... | 2 | 4 | 17 |
| | ¥ 452 | ¥ 454 | $ 3,761 |

## 7. Cash and Cash Equivalents

Cash and cash equivalents at March 31, 2003 and 2002 is as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| Cash and time deposits ... | ¥ 5,911 | ¥ 6,104 | $49,182 |
| Short-term investment .... | 4,616 | 8,991 | 38,407 |
| Less-time deposits with original maturities more than three months ......... | (70) | (70) | (582) |
| Less-stock ...................... | — | (98) | — |
| | ¥10,458 | ¥14,927 | $87,007 |

## 8. Leases

The Group leases certain machinery and equipment, and other assets. Total lease payments under these leases were ¥359 million ($2,990 thousand) , and ¥309 million for the years ended March 31, 2003 and 2002, respectively.

Pro forma information relating to acquisition costs, accumulated depreciation and future minimum lease payments for property held under finance leases which do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the years ended March 31, 2003 and 2002, is as follows:

| | Millions of yen | | |
|---|---|---|---|
| | 2003 | | |
| | Machinery and Equipment | Other | Total |
| Acquisition costs ........... | ¥ 1,214 | ¥ 629 | ¥ 1,844 |
| Accumulated Depreciation ................ | 429 | 305 | 735 |
| Net leased property ....... | ¥ 784 | ¥ 324 | ¥ 1,109 |

| | Millions of yen | | |
|---|---|---|---|
| | 2002 | | |
| | Machinery and Equipment | Other | Total |
| Acquisition costs ........... | ¥ 1,101 | ¥ 946 | ¥ 2,048 |
| Accumulated Depreciation ................ | 249 | 662 | 912 |
| Net leased property ....... | ¥ 852 | ¥ 283 | ¥ 1,135 |

| | Thousands of U.S. dollars | | |
|---|---|---|---|
| | 2003 | | |
| | Machinery and Equipment | Other | Total |
| Acquisition costs ........... | $10,105 | $ 5,237 | $15,342 |
| Accumulated Depreciation ................ | 3,576 | 2,539 | 6,116 |
| Net leased property ....... | $ 6,528 | $ 2,697 | $ 9,226 |

Future minimum lease payments under finance leases as of March 31, 2003 and 2002 were as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| Due within one year | ¥ 368 | ¥ 330 | $3,065 |
| Due after one year | 740 | 805 | 6,160 |
| Total | ¥1,109 | ¥1,135 | $9,226 |

The acquisition costs and future minimum lease payments under finance leases include the imputed interest expense portion.

Depreciation expense, which is not reflected in the accompanying consolidated statements of income, computed by the straight-line method, would have been ¥359 million ($2,990 thousand) for the year ended March 31, 2003.

## 9. Derivatives and Hedging Activities

Derivative financial instruments are utilized by the Company principally to reduce interest rate and foreign exchange rate risks. The Company has established a control environment which includes policies and procedures for risk assessment and for the approval, reporting and monitoring of transactions involving derivative financial instruments. The Company does not hold or issue derivative financial instruments for trading purposes.

At March 31, 2003 and 2002, all forward exchange contracts outstanding were entered into in order to hedge receivables and payables denominated in foreign currencies which have been translated and reflected at the corresponding contracted rates in the accompanying consolidated balance sheets at March 31, 2003 and 2002.

## 10. Shareholders' Equity

Changes in common stock and additional paid-in capital have resulted from the following.

| | | Millions of yen | |
|---|---|---|---|
| | Number of shares | Common stock | Additional paid-in capital |
| Balance of March 31, 2001 | 29,073,279 | 11,786 | 11,824 |
| Retirement of stock during 2002 | (762,500) | — | (201) |
| Balance of March 31, 2002 | 28,310,779 | 11,786 | 11,613 |
| Retirement of stock during 2003 | (145,000) | — | (105) |
| Balance of March 31, 2003 | 28,165,779 | 11,786 | 11,508 |

| | Thousands of U.S. dollars | |
|---|---|---|
| | Common stock | Additional paid-in capital |
| Balance of March 31, 2002 | 98,056 | 96,618 |
| Retirement of stock during 2003 | — | (876) |
| Balance of March 31, 2003 | 98,056 | 95,741 |

The Company adopted 100 shares of common stock as "low unit". A holder of shares representing less than one unit cannot exercise any voting rights with respect to such shares. However, the holder is entitled to receive dividends and other distributions. A holder of a fraction of a unit may at any time require the Company to purchase such shares at the prevailing market price. Shares so purchased must be sold or otherwise transferred to a third party within a reasonable time.

## 11. Research and Development and Computer Software

Research and development expenditure charged to income was ¥702 million ($5,843 thousand) and ¥644 million for the years ended March 31, 2003 and 2002, respectively.

## 12. Income Taxes

The Company and its domestic subsidiaries are subject to several taxes based on income, which in the aggregate resulted in statutory tax rates of approximately 40.6% and 42.0% for the years ended March 31, 2003 and 2002, respectively. Foreign subsidiaries are subject to income taxes of the countries in which they operate.

The effective rate for the two years ended March 31, 2003 differs from the Company's statutory tax rate for the following reasons:

| | 2003 | 2002 |
|---|---|---|
| Statutory tax rate | 42.0 | 42.0% |
| Dividend income | (8.0) | (2.1) |
| Expenses not deductible for income tax purposes | 9.7 | 13.5 |
| Per capital inhabitant tax | 11.8 | 15.4 |
| Other | 9.5 | 9.3 |
| Effective tax rate | 65.0 | 78.1% |

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets at March 31, 2003 and 2002 are presented below:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2003 | 2002 | 2003 |
| Deferred tax assets: | | | |
| Accrued expenses | ¥ 336 | ¥ 220 | $ 2,798 |
| Accrued retirement benefits | 760 | 686 | 6,325 |
| Depreciation | 221 | 267 | 1,843 |
| Unrealized profits | 302 | 173 | 2,517 |
| Tax loss carryforwards | 170 | 212 | 1,420 |
| Unrealized losses of other securities | — | 394 | — |
| Other | 365 | 340 | 3,043 |
| Total gross deferred tax assets | 2,157 | 2,294 | 17,948 |
| Less valuation allowance | (211) | (280) | (1,756) |
| Net deferred tax assets | 1,946 | 2,014 | 16,192 |
| Deferred tax liabilities: | | | |
| Special tax-purpose reserve for condensed booking of fixed assets | (1,345) | (966) | (11,193) |
| Unrealized gains of other securities | (49) | (9) | (410) |
| Total gross deferred tax liabilities | (1,394) | (975) | (11,603) |
| Net deferred tax assets | ¥ 551 | ¥1,038 | $ 4,588 |

In assessing the realizability of deferred tax assets, management of the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is entirely dependent upon the generation of future taxable income in specific tax jurisdictions during the periods in which those temporary differences become deductible. Although realization is not assured, management considered the projected future taxable income in making this assessment. Based on these factors, management believes it is more likely than not that the Company will realize the benefits of these deductible differences, net of the existing valuation allowance as of March 31, 2003.

Tax loss carryforwards will expire between 2004 and 2008.

## 13. Segment Information:

Information about operations in different industry segments of the Group for the years ended March 31, 2003 and 2002, is as follows:

**Industry Segments**

a. Sales and Operating Income

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2003 | | | | | |
| | Industry A | Industry B | Industry C | Industry D | Eliminations /Corporate | Consolidated |
| Sales to customers | ¥32,317 | ¥14,829 | ¥ 6,531 | ¥ 1,590 | ¥ — | ¥55,269 |
| Intersegment | 14 | 3 | — | 360 | (378) | — |
| Total sales | 32,332 | 14,833 | 6,531 | 1,951 | (378) | 55,269 |
| Operating expenses | 32,159 | 13,583 | 6,603 | 1,559 | (395) | 53,510 |
| Operating income | ¥ 172 | ¥ 1,249 | ¥ (71) | ¥ 391 | ¥ 16 | ¥ 1,759 |

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2002 | | | | | |
| | Industry A | Industry B | Industry C | Industry D | Eliminations /Corporate | Consolidated |
| Sales to customers | ¥29,476 | ¥10,967 | ¥ 6,925 | ¥ 612 | ¥ — | ¥47,982 |
| Intersegment | 16 | — | — | 344 | (360) | — |
| Total sales | 29,492 | 10,967 | 6,925 | 957 | (360) | 47,982 |
| Operating expenses | 29,863 | 10,232 | 6,883 | 904 | (375) | 47,508 |
| Operating income | ¥ (371) | ¥ 734 | ¥ 42 | ¥ 52 | ¥ 14 | ¥ 474 |

| | Thousands of U.S. dollars | | | | | |
|---|---|---|---|---|---|---|
| | 2003 | | | | | |
| | Industry A | Industry B | Industry C | Industry D | Eliminations /Corporate | Consolidated |
| Sales to customers | $268,867 | $123,376 | $ 54,336 | $ 13,232 | $ — | $459,812 |
| Intersegment | 124 | 26 | — | 3,000 | (3,151) | — |
| Total sales | 268,991 | 123,402 | 54,336 | 16,233 | (3,151) | 459,812 |
| Operating expenses | 267,552 | 113,006 | 54,933 | 12,974 | (3,289) | 445,178 |
| Operating income | $ 1,438 | $ 10,396 | $ (597) | $ 3,258 | $ 138 | $ 14,634 |

b. Assets, Depreciation and Capital Expenditures

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2003 | | | | | |
| | Industry A | Industry B | Industry C | Industry D | Eliminations /Corporate | Consolidated |
| Assets | ¥40,597 | ¥10,930 | ¥ 6,112 | ¥ 5,544 | ¥15,760 | ¥78,943 |
| Depreciation | 740 | 46 | 111 | 272 | — | 1,169 |
| Capital expenditure | 2,510 | 67 | 99 | 685 | — | 3,361 |

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2002 | | | | | |
| | Industry A | Industry B | Industry C | Industry D | Eliminations /Corporate | Consolidated |
| Assets | ¥36,539 | ¥ 7,793 | ¥ 6,162 | ¥ 5,633 | ¥20,233 | ¥76,360 |
| Depreciation | 849 | 34 | 109 | 83 | — | 1,075 |
| Capital expenditure | 340 | 50 | 314 | 3,912 | — | 4,616 |

| | Thousands of U.S. dollars | | | | | |
|---|---|---|---|---|---|---|
| | 2003 | | | | | |
| | Industry A | Industry B | Industry C | Industry D | Eliminations /Corporate | Consolidated |
| Assets | $337,743 | $ 90,936 | $ 50,851 | $ 46,122 | $ 131,113 | $656,767 |
| Depreciation | 6,151 | 385 | 920 | 2,266 | — | 9,724 |
| Capital expenditure | 20,880 | 557 | 821 | 5,697 | — | 27,957 |

Notes: Industry A consists of special equipment car.
Industry B consists of environmental equipment and systems.
Industry C consists of car sales business.
Industry D consists of real estate business.
Corporate assets consist primarily of cash and cash equivalents, investment in and advances to affiliates, investments in securities and the corporate headquarters assets.

With effect from the year ended March 31,2003, four-segment classification was presented due to an increasing materiality of real estate business segment, while three segments were presented in the consolidated financial statements previously reported for the year ended March 31,2002.

Segment information for the year 2002 disclosed above was reclassified to conform to the four-segment classification for comparative purposes.

## 14. Subsequent Event

The following appropriations of the Company's retained earnings in respect of the year ended March 31, 2003 were as proposed by the Board of Directors and approved by the shareholders at the annual general meeting held on 27 June, 2003:

| Appropriations | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| Cash dividends (¥3.0 per share) | ¥ 83 | $ 693 |
| Bonuses to directors | 23 | 195 |
| Total appropriations | ¥ 106 | $ 889 |

# REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Shareholders and
Board of Directors
of Kyokuto Kaihatsu Kogyo Co., Ltd.

We have audited the accompanying consolidated balance sheets of Kyokuto Kaihatsu Co., Ltd. and subsidiaries as of March 31, 2002 and 2003, and the related consolidated statements of income, stockholders' equity and cash flows for each of the years in the two-year period ended March 31, 2003. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kyokuto Kaihatsu Kogyo Co.,Ltd. and subsidiaries as of March 31, 2002 and 2003, and the results of their operations and their cash flows for each of the years in the two-year period ended March 31, 2003 in conformity with accounting principles generally accepted in Japan.

The accompanying consolidated financial statements as of and for the year ended March 31, 2003 have been translated into United States dollars solely for the convenience of the reader. We have recomputed the translation and, in our opinion, the consolidated financial statements expressed in yen have been translated into dollars on the basis set forth in note 1 to the consolidated financial statements.

Yukoh Audit Corporation

Osaka, Japan
June 27, 2003

# CORPORATE INFORMATION

**Kyokuto Kaihatsu Kogyo Co., Ltd.**

**Established:**
June, 1955

**Paid-in Capital:**
¥11,786 million (at March 31, 2003)

**Number of Shares Issued:**
28,165,779 shares (at March 31, 2003)

**Number of Employees:**
1,378 (at March 31, 2003)

**Head Office:**
1-45, Koshienguchi 6-chome, Nishinomiya City, Hyogo Prefecture,
663-8545, Japan
Tel: 0798-66-1000
Fax: 0798-66-8146

**Tokyo Office:**
1-1, Asahicho, Haneda, Ota-ku, Tokyo, 144-0042, Japan
Tel: 03-5737-2271
Fax: 03-5737-7791

**Plants:**

Yokohama Plant
Occupies 51,890m$^2$
Since March, 1962
Located in Yamato, Kanagawa

Nagoya Plant
Occupies 132,537m$^2$
Since June, 1970
Located in Komaki, Aichi

Miki Plant
Occupies 98,274m$^2$
Since October, 1979
Located in Miki, Hyogo

Fukuoka Plant
Occupies 66,832m$^2$
Since September, 1970
Located in Iizuka, Fukuoka

Hachinohe Plant
Occupies 57,600m$^2$
Since April, 1999
Located in Hachinohe, Aomori

# BOARD OF DIRECTORS AND STATUTORY AUDITORS

(at June 27, 2003)

**Chairman and Representative of the Board of Directors**
Yoshihiro Tokunaga

**President and Representative of the Board of Directors, CEO**
Katsushi Tanaka

**Senior Managing Director, Senior Managing Executive Officer**
Tadao Yasuda

**Managing Director, Managing Executive Officer**
Hiroki Uoi

**Director, Executive Officer**
Yukinori Matsuhashi
Norio Maeda
Ichiro Fujinami
Kazuyoshi Kira
Takeshi Kunisada
Takaaki Hudetani
Syunji Nakamura

**Executive Officer**
Ichiro Fujinami
Yukitoshi Masumura
Toshihide Sakai
Tomoki Ueyama
Genpachi Hashimoto
Rikio Sagawa
Kozo Ueda

**Standing Auditor**
Yasuhiko Tamaki

**Auditor**
Shunichi Suda
Rikuyuki Tentaku
Yasuo Mizuno

KYOKUTO KAIHATSU KOGYO CO., LTD.

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