

ANNUAL REPORT 2004

For the fiscal year ended December 31, 2004

Otsuka Corporation

C O N T E N T S

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Mission Statement

Mission

OTSUKA CORPORATION serves a wide range of companies, providing comprehensive support for their business activities by presenting, within a concrete framework, new business opportunities and management improvement strategies brought about by innovations in information and telecommunication technology. By so doing, we continue to facilitate the growth of our client companies and contribute to the development of our country and the creation of a spiritually enriching society.

Goals

- To become a corporate group that is recognized and trusted as a valuable corporate citizen.
- To encourage employee growth and self-realization through the attainment of personal goals and professional achievement.
- To demonstrate harmonious coexistence and growth with nature and society.
- To create business models that consistently keep pace with the changing times.

Principles

- Always thinking from the customer's perspective and acting through harmonious team work.
- Maintaining the spirit of challenge inherited from our predecessors, exercising our own critical judgment, and acting on our own initiative.
- Fully complying with all prevailing laws and regulations, and maintaining high ethical standards.

Otsuka Corporation

Forward-Looking Statements

The forecasts, plans and outlooks concerning future operating results that are described in this Annual Report are judgments believed to be reasonable by the Company's management, based upon the information available to OTSUKA CORPORATION and member companies of the OTSUKA Group at the time such future projections were created. Various factors that form the basis of these forward-looking statements may differ from the OTSUKA Group's assumptions, and actual results may differ significantly from those presented here. Such factors include changes to the economic situation in principal markets and to product demand, and changes in various domestic and international regulations, accounting standards and customary business practices.

Consolidated Financial Highlights

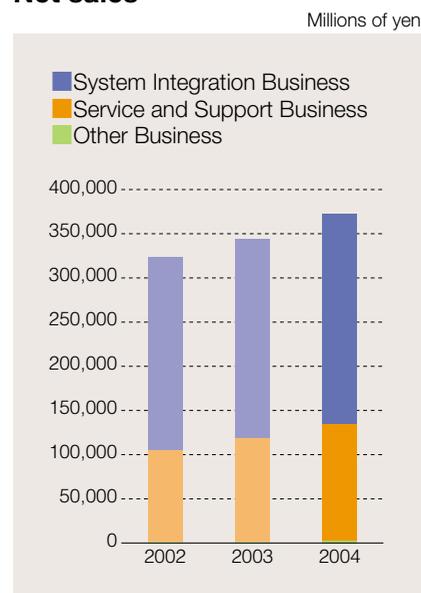
OTSUKA CORPORATION and its Consolidated Subsidiaries Years ended December 31, 2002, 2003 and 2004			Millions of yen	Thousands of U.S. dollars	%
	2002	2003	2004	2004	Change
Net sales	¥324,289	¥344,377	¥372,481	\$3,574,673	+8.2
System Integration Business	219,690	225,842	238,729	2,291,065	+5.7
Service and Support Business	103,380	116,665	130,959	1,256,804	+12.3
Other Business	1,219	1,869	2,792	26,794	+49.4
Operating income	7,990	9,221	17,009	163,234	+84.5
Recurring profit	7,766	9,055	17,036	163,493	+88.1
Income before income taxes and minority interests	4,706	4,619	18,548	178,003	+301.5
Net income	2,405	2,457	11,247	107,936	+357.7
Total assets	148,563	162,144	167,228	1,604,875	+3.1
Total interest-bearing debt	29,795	36,858	21,337	204,769	-42.1
Total shareholders' equity	42,351	43,978	54,667	524,635	+24.3
Net income per share (EPS) (Yen and U.S. dollars)	75.96	77.67	355.88	3.41	+358.2
Dividends per share of common stock (Yen and U.S. dollars)	20.00	20.00	55.00	0.52	+175.0
Cash flows from operating activities per share (Yen and U.S. dollars)	468.47	497.87	743.43	7.13	+49.3
Operating income to net sales ratio (%)	2.46	2.68	4.57	—	
Net income to net sales ratio (%)	0.74	0.71	3.02	—	
Total interest-bearing debt ratio (%)	20.06	22.73	12.76	—	
Shareholders' equity ratio (%)	28.51	27.12	32.69	—	
Return on equity (ROE) (%)	5.76	5.69	22.80	—	

Note:

Figures for ROE are calculated using average shareholders' equity.

U.S. dollar amounts are computed using the December 31, 2004 exchange rate of ¥104.2=US\$1.

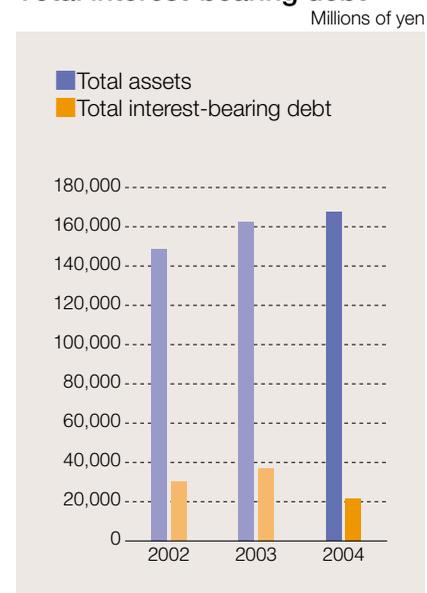
Net sales



Operating income, Recurring profit, Net income



Total assets, Total interest-bearing debt



Note:

During the fiscal year 2003, the Company changed its policy from rounding off sums of less than a million yen to rounding down.

To Our Shareholders and Investors



Yuji Otsuka, President

I am pleased to announce the results for the fiscal year ended December 31, 2004.

In the fiscal year under review, the OTSUKA Group posted record net sales of ¥372,481 million, which was an increase of 8.2% from the previous year. By segment, sales in the System Integration Business rose 5.7% to ¥238,729 million on the back of strong performance for color copiers, servers and security-related products. In the Service and Support Business, continued favorable performance in the “tanomail” office supply mail-order service contributed to a 12.3% increase in sales to ¥130,959 million.

As a result of the reduction of SG&A expenses and the recording of gain from the exemption from the obligation under the substitutional portion of social welfare pension fund, the OTSUKA Group achieved a record performance as operating income jumped 84.5% to ¥17,009 million, recurring profit rose 88.1% to ¥17,036 million and net income soared 357.7% to ¥11,247 million. Given such results, management has resolved to raise cash dividends from ¥20 in the previous term to ¥55 per share.

The OTSUKA group will further work toward achieving the tenets of our Mission Statement and pursue management reforms that respond to the trust of all stakeholders.

We would like to ask for the continued support of our shareholders and investors.

Yuji Otsuka, President

March, 2005

Overview of Consolidated Operations

■ Signs of Economic Recovery

In the fiscal year under review, the Japanese economy in the first half of the term made steady gains toward a recovery as improving global economic conditions fueled increased exports and the subsequent increase in production further fostered capital investment. Corporate earnings also made a dramatic comeback and spread from large to medium and small companies and from manufacturing to non-manufacturing industries. Unfortunately, this recovery slowed in the second half of the term amid skyrocketing crude oil and raw materials prices as well as the impact of typhoons, earthquakes and other natural disasters.

■ Full-scale Recovery in Computerization Investment

Previously delayed investment in computerization of corporate operations was finally initiated in IT-related industries, in which the OTSUKA Group operates, to produce a recovery in PCs and other computer-related equipment. Key factors included measurable progress made in “e-Japan Strategy” amid improved corporate earnings and the proliferation of broadband, an increasing interest in security countermeasures in preparation for the implementation of the Personal Information Protection Law, the need to replace systems originally purchased to address the Y2K problem as well as such government policies as the IT Investment Promotion Tax. However, this rebound has also been accompanied by an increasing demand on the part of customers to both quantitatively prove the efficacy of computerizing their systems while reducing costs.

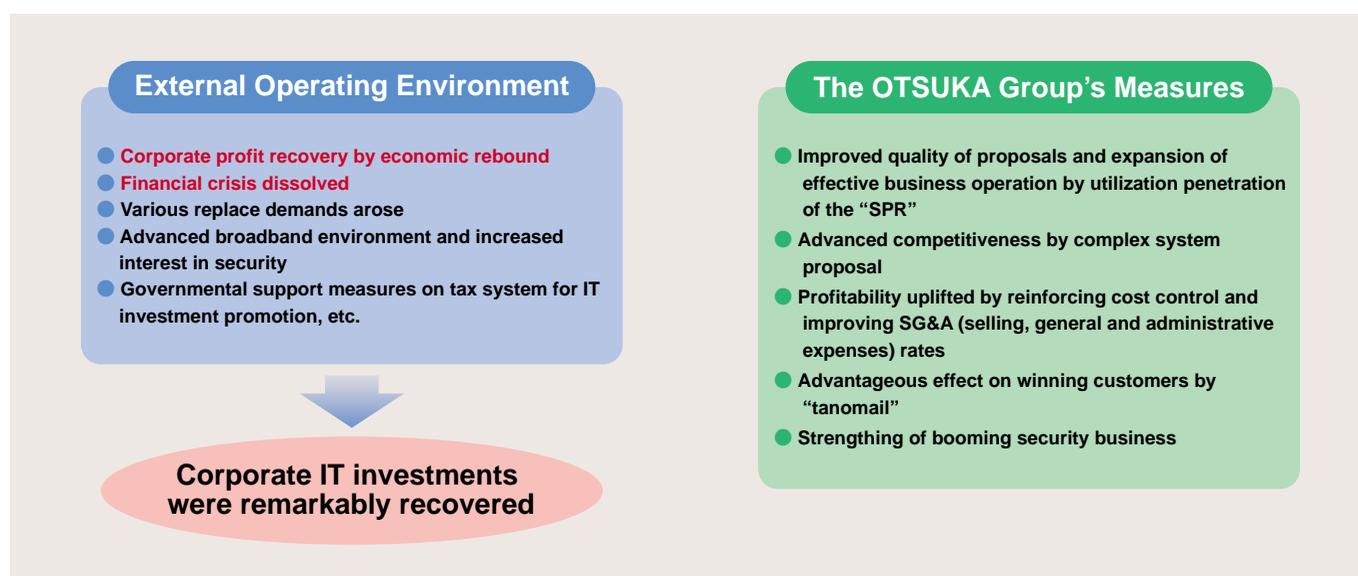
■ Proposals to Encourage IT Use for Improved Management Efficiency

Amid such conditions, the OTSUKA Group has rallied behind the slogan “Act from the Customer's Perspective and Respond to their Trust Utilizing Our Comprehensive Strengths” to focus on proposing IT-based solutions for improving operations. For example, the OTSUKA Group capitalized on the proliferation of broadband and a greater concern regarding security by offering composite systems and associated services that stem from the Group’s comprehensive capabilities. Concurrently, the OTSUKA Group raised the quality of its proposals and improved efficiency in operations by promoting greater use of “SPR,” as well as by focusing resources on the key strategic businesses of “tanomail,” “ODS21,” “SMILE” and “OSM.” Moreover, the Group continued to focus on resolving customer problems by dramatically overhauling and fusion mission critical systems and information systems that use the Internet.

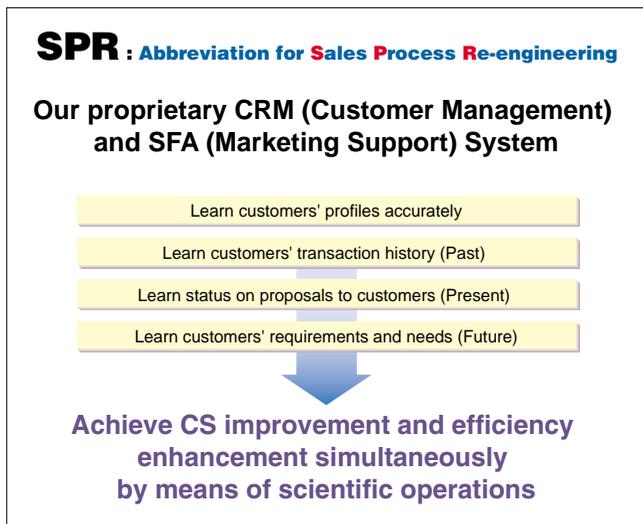
*See page 6 for a description of respective strategic businesses.

■ Achieving Increased Sales and Profits

On a consolidated basis, net sales rose 8.2% to ¥372,481 million; operating income jumped 84.5% to ¥17,009 million; recurring profit jumped 88.1% to ¥17,036 million; and net income soared 357.7% to ¥11,247 million.



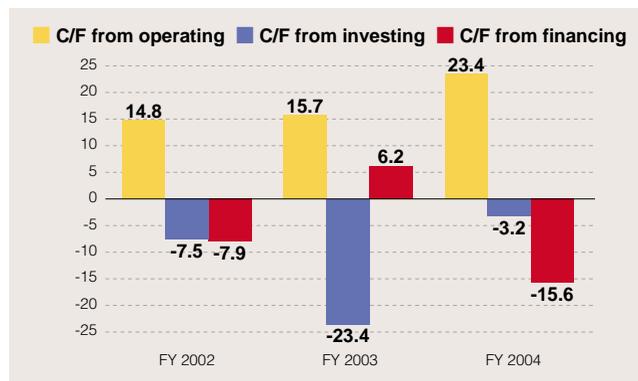
■ A Precise Systematic Approach Using “SPR”



The Company employs Sales Process Re-engineering (SPR) as a mechanism for efficiently providing optimal solutions that raise customer satisfaction. “SPR” is a system developed by OTSUKA CORPORATION and features functions that combine Customer Relationship Management (CRM) with Sales Force Automation (SFA). “SPR” naturally handles customer profile information, but also acts as a database for transaction histories (past), status reports for submitted proposals (present) and desires and needs (future). The database includes interviews and daily contact information for up to 20,000 companies as well as information on other companies. Analyzing and using this data in various and creative ways enables the Company to efficiently provide customers with optimal solutions.

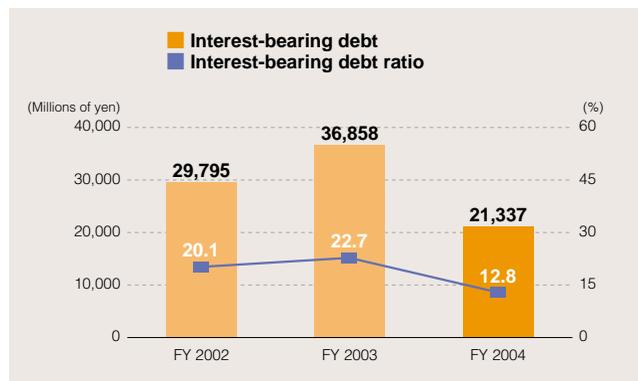
■ Cash Flows

(Billions of yen)



Cash provided by operating activities rose by ¥7,745 million on the back of positive business results. Cash used in investing activities decreased by ¥20,160 million following the acquisition of a new head office in the previous term, while cash used in financing activities increased by ¥21,901 million to fund such activities as the repayment of loans.

■ Interest-bearing debt



In the fiscal year under review, the Company finished redeeming corporate bonds previously issued. Despite the acquisition of a new head office building in the previous term that contributed to a temporary increase in loans, interest-bearing debt (including short-term and long-term loans and corporate bonds) declined by roughly ¥15.5 billion as a result of a reduction in loans against the backdrop of strong cash flows from operating activities.

Overview of Business Segments

■ System Integration Business

The System Integration Business provides optimized system services ranging from consulting to system design and introduction, transport and installation and network construction. As a result of focusing resources on the innovative “ODS21” knowledge management system and the “SMILE” integrated mission-critical operational system, sales of color copiers, computers and servers continued to be strong, and posted a 5.7% increase in net sales to ¥238,729 million.

■ Service and Support Business

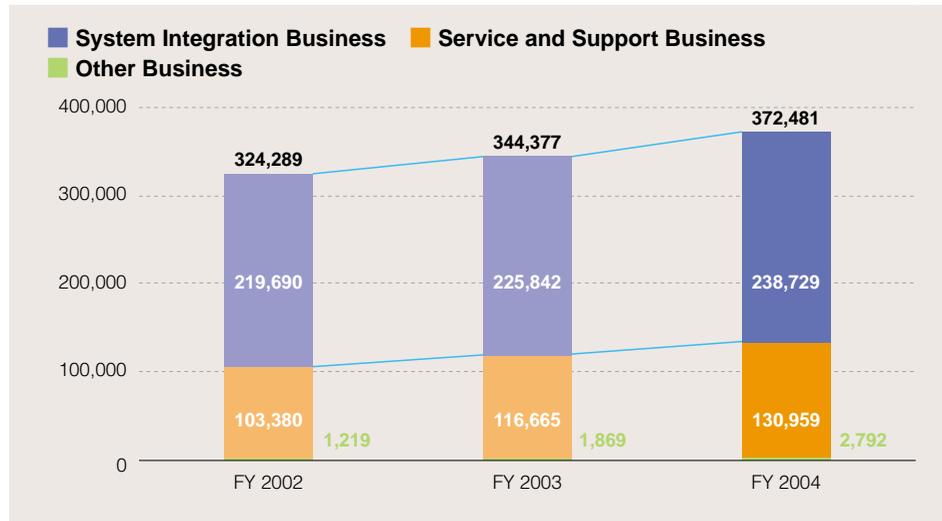
The Service and Support Business offers total support for systems installed by customers with supplies, hardware and software maintenance, telephone support and IT education. The “tanomail” office supply mail-order services via Website and catalog channels fueled continued growth in sales chiefly for OA supplies. Combined with a favorable performance in maintenance and similar fields, net sales increased 12.3% to ¥130,959 million.

■ Other Business

In Other Business, the construction industry, in which Fujimi Construction Co., LTD. operates, continued to be subjected to harsh conditions, but aggressive marketing activities resulted in a 49.4% increase in net sales to ¥2,792 million.

Net Sales by Segment

(Millions of yen)



Overview of Key Strategic Businesses (Non-consolidated)

OTSUKA CORPORATION has positioned “MRO,” “SMILE,” “ODS21” and “OSM” as its key strategic businesses and has concentrated resources accordingly. An overview of respective strategic businesses for this fiscal year is as follows.

Key Strategic Business

MRO

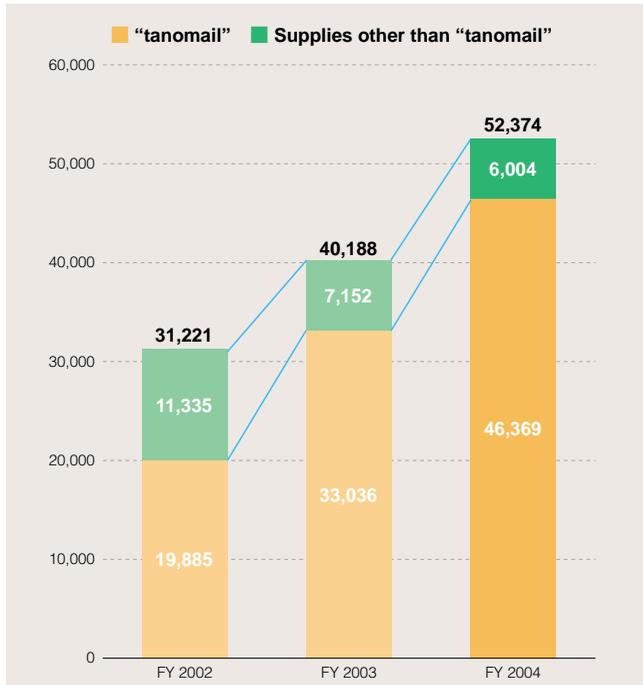
For the fiscal year under review, net sales rose **30.3%** to **¥52,374 million**.

of the above, “tanomail”:

For the fiscal year under review, net sales rose **40.4%** to **¥46,369 million**.

Net Sales of “MRO”

(Millions of yen)



The “MRO” business, which sells products such as stationary, daily necessities used in the office and OA supplies, recorded sales in excess of ¥52 billion due to the significant gains made by the “tanomail” office supply mail-order service, the core pillar of the “MRO” business.

In this respect, “tanomail” is the portal for OTSUKA CORPORATION’s one-stop solutions, and the Company is working to expand transactions for every aspect of customers’ systems.



“tanomail” catalog, Vol. 13



“tanomail” via Internet
<http://www.tanomail.com>

Key Strategic Business

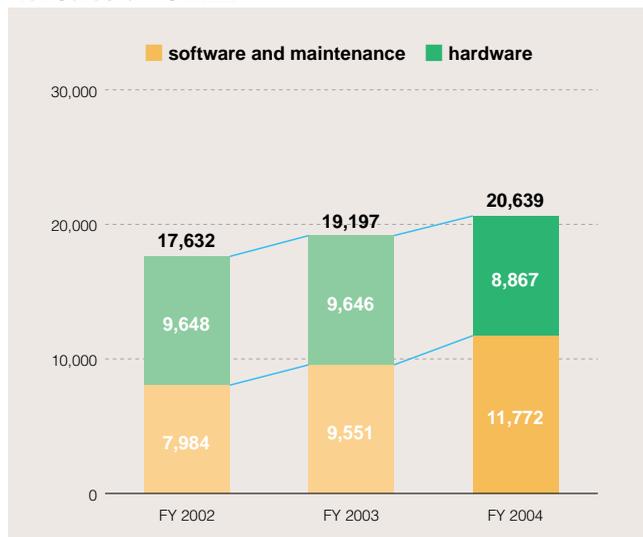
SMILE

For the fiscal year under review, net sales rose **7.5%** to **¥20,639 million**.

of the above, software and maintenance:

For the fiscal year under review, net sales rose **23.3%** to **¥11,772 million**.

Net Sales of "SMILE" (Millions of yen)



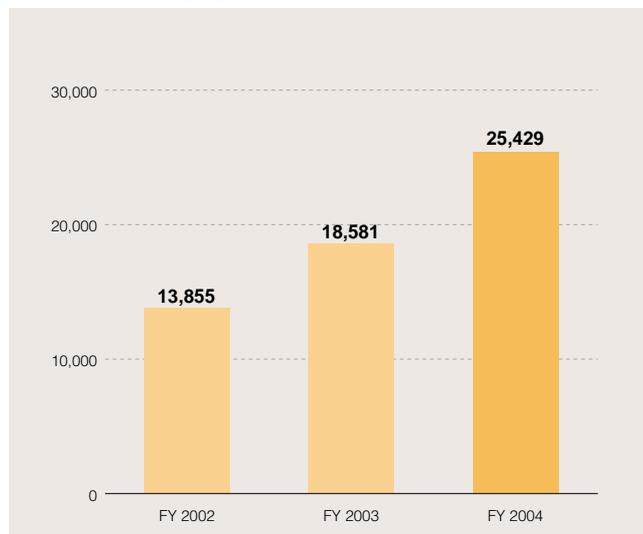
"SMILE" is the Company's proprietary integrated mission-critical operational system, which encompasses 26 years of experience extending back to the office computer days. OTSUKA CORPORATION boasts "SMILE α AD" geared to the needs of midsize companies and small-medium size businesses and "SMILE ie" for large and midsize companies. The system capitalizes on its ease of introduction into any customer's corporate system owing to the broad range of optional software for specific industries and operations, thereby ensuring strong sales in software and maintenance against the backdrop of companies revamping their mission-critical systems in line with management reforms.

Key Strategic Business

ODS21

For the fiscal year under review, net sales rose **36.9%** to **¥25,429 million**.

Net Sales of "ODS21" (Millions of yen)



"ODS21" is a knowledge management system that digitally captures paper-based information using copiers, allowing such information to be stored with other digital data at a centrally managed bank that can be shared and utilized. "ODS21" provides proposals to improve operations at midsize companies by relying on the unique strengths of OTSUKA CORPORATION for providing both copiers and computers, thereby contributing to strong sales for this business.

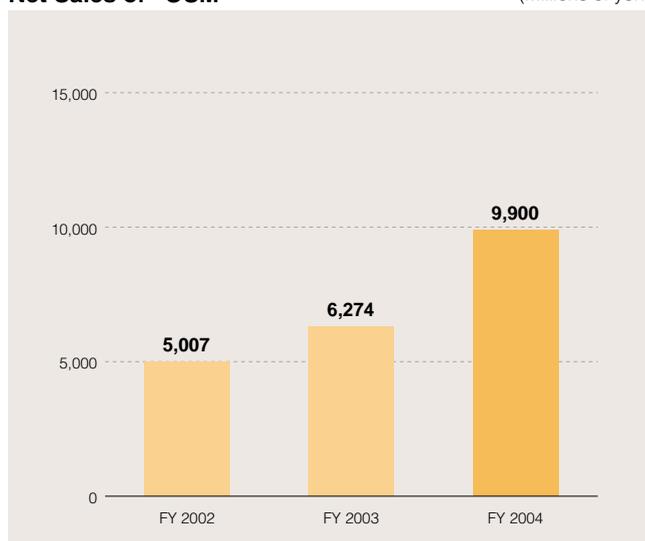
Key Strategic Business

OSM

For the fiscal year under review, net sales rose **57.8%** to **¥9,900 million**.

Net Sales of "OSM"

(Millions of yen)



OSM Otsuka Security Management

"OSM" is OTSUKA CORPORATION's name-brand security business, and has enjoyed robust performance as a result of rising interest in corporate security in preparation for implementation of the Personal Information Protection Law.

■ Corporate Alliance for Information Leakage Prevention

Nowadays, corporate management is being heavily impacted by the frequent occurrence of personal information leaks, which is becoming one of their most pressing issues. However, many companies are at a loss as to where to begin implementing concrete measures to prevent such occurrences. Also, there is no all-encompassing product that can prevent every possible leak. To address the problem, OTSUKA CORPORATION acted as a facilitator in forming a corporate alliance with integrated leak prevention solutions in line with the rising demand for companies that offer optimal products and specific countermeasures. The member alliance includes the top vendors in each field, covering every aspect from prevention to security in cases where personal information has been leaked.

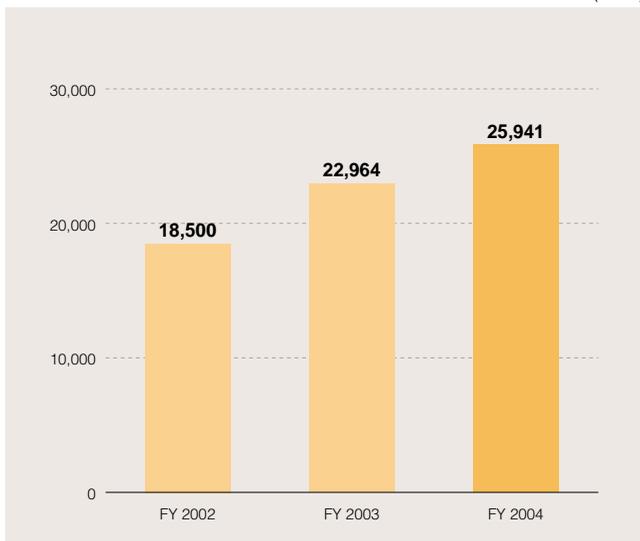
Nine-Member Corporate Alliance

RSA Security Japan Ltd.
MOTEX Inc.
OTSUKA CORPORATION
Quality Corporation
Citrix Systems Japan K.K.
SOMPO JAPAN INSURANCE INC.
Trend Micro Incorporated
Hitachi Software Engineering Co., Ltd.
Microsoft Corporation

Overview of Unit Sales for Computers and Copiers

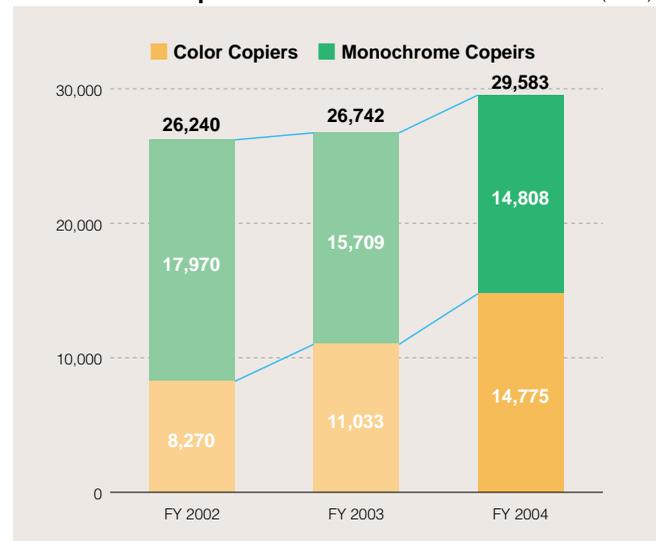
Unit Sales of Servers

(units)



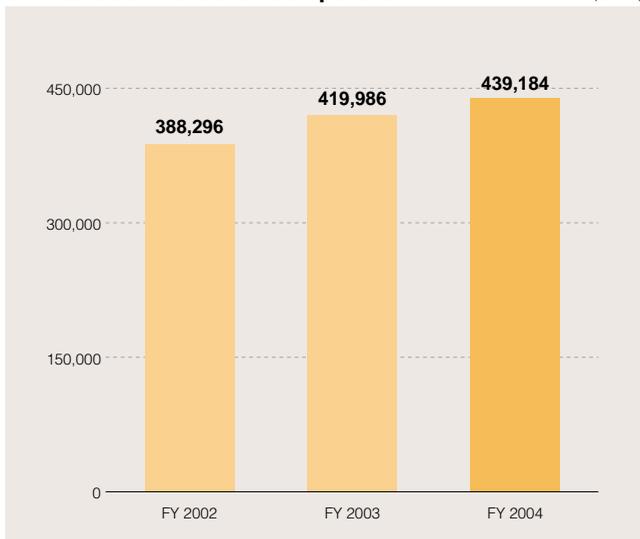
Unit Sales of Copiers

(units)



Unit Sales of Personal Computers

(units)



Challenges and Forecasts for Fiscal year 2005

■ Future of the IT Market

In the coming term, despite uncertain conditions regarding rising crude oil prices and appreciation of the yen, the Japanese economy is forecast to continue along the path of a prolonged, albeit mild, recovery.

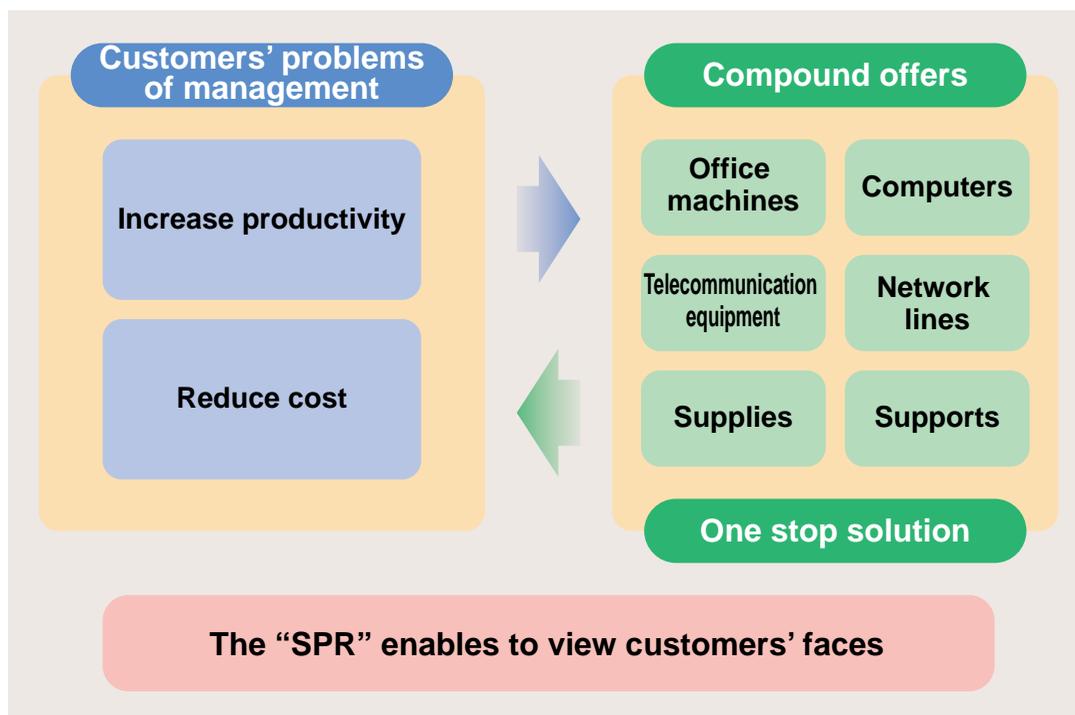
Against this backdrop, every company, regardless of size, is being forced to make aggressive use of IT and improve management. Behind this push lies the dramatic overhaul taking place in B2B trading and mission-critical systems, as well as advances in broadband, which will likely further fuel integration of data, voice and image. We are undoubtedly entering an era in which solutions will have to address customer needs in a more complex and comprehensive way, including through the fusion of mission-critical and information systems, infrastructure and applications, digital copiers and computers. This means that merely handling one field of expertise—be it in computer, copier or communication systems—will no longer enable companies to provide comprehensive solutions.

■ Growing Alongside Customers and Respond to the Trust

Since its founding, the OTSUKA Group has worked to meet customer needs while also expanding the number of solutions and services available within the Company from copiers to computers, communication devices and lines and IP telephones.

OTSUKA CORPORATION will strive to achieve its Mission Statement using the Company's medium-term management strategy and grow with customers by offering management solutions, thereby further enhancing corporate value.

Resolve customers' problems (being in need)



■ Specific Measures

Specifically, the Company will fully cultivate and expand its base of customers through the promotion of “New-Web Strategy.” At the same time, strategic efforts will focus on maintaining profitability and expanding sales by bolstering its “Total α Support 21” support business and by focusing resources on “tanomail,” “ODS21,” “SMILE” and “OSM” businesses, while also thoroughly evaluating designated projects. To that end, OTSUKA CORPORATION will commit further management resources to fields with promising growth prospects while enhancing Group management.

■ Forecasts for Fiscal year 2005

In the coming fiscal year, the Company forecasts a 5.0% increase in net sales to ¥391 billion, a 5.7% rise in recurring profit to ¥18 billion and a 22.5% decrease in net income to ¥8,720 million.

The Mid term goals and Activity principles

Basic principle

- Grow with customers by putting the Mission Statement into effect

Mid term plans

- Work-force basically remains flat
- Strive for expanding business by revenue increase and profit increase
Challenge 5% mark of the Operating income and Recurring profit to Net sales ratio
- Open up new demand by applying the customer asset data
- Effective use of individuals/materials/money and per head productivity increase

Topics

■ Launch of “Personal tanomail”

The Company launched “Personal tanomail” as a part of the “tanomail” service for individual customers.

In line with the expansion of products available through “tanomail,” and in response to requests from corporate customers to offer services to individual employees within their companies, “Personal tanomail” offers products attractive for use in their personal life that are slightly different from the office version of “tanomail.” Such products include personal computers, peripheral devices and beauty-related appliances, as well as leisure goods, sundries and cosmetics.

While payment via credit card is open to all users, the service also offers special sales, and auctions for those individuals who sign up as members.



“Personal tanomail” catalog, Vol. 3



“Personal tanomail” via Internet
<http://www.p-tano.com/>

■ Listing of 10art-ni Corporation on TSE Mothers Market

On August 5, 2004, OTSUKA CORPORATION’s consolidated subsidiary, 10art-ni Corporation (Code: 3744), was listed on the Tokyo Stock Exchange’s Mothers market.

10art-ni develops and offers solutions predominately using Linux and Java technologies.

<http://www.10art-ni.co.jp>

Linux: Linux is an open-source operating system whose freely available code is modified and improved by software programmers around the world.

Java: Java is a programming language developed by U.S.-based Sun Microsystems, Inc. that is spreading as the development language of choice for Web systems centered around the Internet, and is used widely in e-Commerce and internal company information systems.



Listing ceremony at the Tokyo Stock Exchange

■ Introduction of Internal Censure and Corrective System

As a means of ensuring the realization of its Mission Statement, OTSUKA CORPORATION began implementing an Internal Censure and Corrective System. This system aims to prevent and uncover abuses and misconduct as well as to collect suggestions for improved operational management.

■ Establishment of Personal Information Protection Policy

The Company stringently controls the considerable volume of personal and corporate information collected through its operations. The Company established and declared the Personal Information Protection Policy to tighten our efforts towards information management.

Personal Information Protection Policy

This policy lays down core practices that must be observed in order to properly protect personal information possessed by OTSUKA CORPORATION.

1. Compliance with Regulations and Standards

OTSUKA CORPORATION observes laws and other regulations regarding personal information.

2. Thorough Enforcement of Proper Personal Information Control

OTSUKA CORPORATION appoints administrators for personal information and has proper measures in place to protect personal information against illegal use, loss, destruction, alteration and leakage. Moreover, OTSUKA CORPORATION educates all employees about the treatment of personal information to ensure proper control. Corporate information is treated in the same manner as personal information and is subject to control.

3. Purpose and Limit of Data Collection

OTSUKA CORPORATION is explicit about how personal information will be used and collects only necessary information.

4. Use of Data Only for Expressed Purposes

OTSUKA CORPORATION never uses, releases or entrusts to third parties any information not authorized by the originating individual or their representative, or that exceeds limits required by laws.

5. Restrictions and Management of Release

OTSUKA CORPORATION properly handles personal information to ensure that it remains confidential and is used neither outside the authorized range nor beyond what regulations stipulate. When personal information that has been authorized for use must be released externally, OTSUKA CORPORATION monitors the process to ensure that data is handled with the utmost care.

6. Continuous Improvements

In order to properly handle personal information, OTSUKA CORPORATION continually revises its management processes and makes improvements by keeping abreast of changes in regulations, societal standards and information technologies.

Social Contributions and Environmental Preservation

Starting from our immediate surroundings, OTSUKA CORPORATION contributes to society and environmental preservation in a wide range of fields.

■ “A Gift from Tanokun” Social Contribution Program

“A Gift from Tanokun” is a social contribution program that makes donations to non-profit organizations in the form of “tanomail” products that have been returned due to damage of the outer packaging during shipping, but whose contents are undamaged.



■ Heartful Fund Program

The Heartful Fund Program is a matching gift program* in which the Company matches monthly voluntary donations from employees of ¥100. This fund is allocated toward providing handicapped assistance, environmental preservation and disaster relief. The year 2004 witnessed a record 10 typhoons as well as the Niigata Chuetsu earthquake. In response, many Company employees signed up for the Heartful Fund Program, enabling relief funds to be sent to affected areas.

* Matching gift program: A program in which the company adds to the amount donated by each employee. OTSUKA CORPORATION's policy is to match equally the donations of its employees.

■ Joint Project

OTSUKA CORPORATION pursues many joint projects with companies and non-profit organizations, including recycling used PCs in cooperation with leading IT-related companies, operating “Donation and Support Programs of PCs for Reuse” to donate PCs to nationwide non-profit organizations via the specified non-profit organization “earts” and participating in the World Wide Fund for Nature Japan, which is the world's largest nature conservation group.

■ Area Cleanup Activities

Employees nationwide regularly team up with local residents to clean up the areas around their offices, including the head office building.



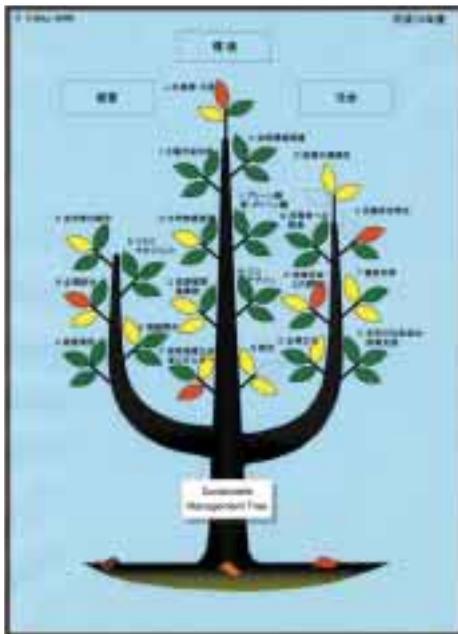
■ Blood Donation

Key offices of the OTSUKA Group, including the head office, invite staff of The Japanese Red Cross Society for blood drives.



■ Environmental Management Ranking (Environmental Management Assessment by Third Party)

In 2004, OTSUKA CORPORATION submitted the Company for review to the Sustainable Management Forum of Japan and received an environmental rating. The evaluation uses a branching tree illustration to give an overall picture of the Company from the three aspects of strategy, structure and results for the triple bottom lines of management, environment and society. The Company aims to make further improvements so as to become a pioneering environmental-friendly Company.



■ OTSUKA CORPORATION Environmental Report 2004

Every year, OTSUKA CORPORATION produces and widely releases its Environmental Report about the previous year's environmental activities. Rather than being printed, the report was posted on the Company homepage to promote resource savings of paper.



<http://www.otsuka-shokai.co.jp/eco/2004/index.html>

Environmental Solutions

OTSUKA CORPORATION develops and offers customers a broad selection of environmental solutions based on its track record and expertise in applying them to its in-house environmental protection efforts.

- Contributed to reduced paper use by shifting to a paperless environment using "ODS21"
- Promoted green procurement using "tanomail"
- Aided in improving environmental education using "Web Learning"
- Contributed to reduced resource use by promoting "the recycling of toner and PCs"

Board of Directors and Corporate Auditors (as of March 30, 2005)



President*

Yuji Otsuka



Senior Managing Director*

Akira Ishitani



Executive Managing Director
and Executive Vice President

Yoshiaki Nagashima



Executive Managing Director
and Executive Vice President

Youichi Harada



Managing Director
and Executive Vice President

Kazuhide Hamada



Managing Director
and Executive Vice President

Kazuyuki Katakura



Managing Director
and Executive Vice President

Katsuhiko Nakajima

Director and Executive Vice President

Yuuichi Itou

Kimio Shiokawa

Masakazu Tachibana

Shinji Usami

Toshiyasu Takahashi

Katsuhiko Yano

Standing Auditor

Tatsuzo Yoshida

Auditors

Katsuhiko Haneishi

Katsumi Furuhata

Jiro Makino

*Director with representation rights

Financial Section

Three-Year Financial Data

OTSUKA CORPORATION and Its Consolidated Subsidiaries
Years ended December 31, 2002, 2003 and 2004

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Total shareholders' equity	42,351	43,978	54,667	524,635
Net income per share (EPS) (Yen and U.S. dollars)	75.96	77.67	355.88	3.41
Dividends per share of common stock (Yen and U.S. dollars)	20.00	20.00	55.00	0.52
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Operating income to net sales ratio (%)	2.46	2.68	4.57	—
Net income to net sales ratio (%)	0.74	0.71	3.02	—
Total interest-bearing debt ratio (%)	20.06	22.73	12.76	—
Shareholders' equity ratio (%)	28.51	27.12	32.69	—
Return on equity (ROE) (%)	5.76	5.69	22.80	—

Notes:

Figures for ROE are calculated using average shareholders' equity.

U.S. dollar amounts are computed using the December 31, 2004 exchange rate of ¥104.2=US\$1.

Figures in parentheses are negative figures.

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Management's Analysis of Operating Results & Financial Position

Summary of Sales and Profits

			Millions of yen	
	2003	2004	Difference, year to year	% change, year to year
Net sales	¥344,377	¥372,481	+28,104	+8.2%
System Integration Business	225,842	238,729	+12,886	+5.7
Service & Support Business	116,665	130,959	+14,294	+12.3
Other Business	1,869	2,792	+923	+49.4
Cost of sales	266,651	285,655	+19,004	+7.1
Gross profit	77,725	86,825	+9,100	+11.7
Selling, general and administrative expenses	68,503	69,815	+1,312	+1.9
Operating income	9,221	17,009	+7,788	+84.5
Recurring profit	9,055	17,036	+7,981	+88.1
Income before income taxes and minority interests	4,619	18,548	+13,928	+301.5
Income taxes*	2,047	7,077	+5,029	+245.6
Net income	2,457	11,247	+8,789	+357.7

*Including adjustment amount for corporate and other taxes

Sales Summary

For the term, the System Integration Business and Service & Support Business both recorded robust sales. In combination with decent sales growth among the majority of consolidated subsidiaries, consolidated net sales rose 8.2% to a record ¥372,481 million.

System Integration Business

The System Integration Business provides optimized system services ranging from consulting to system design and development, transport and installation and network construction. As a result of focusing resources on the innovative "ODS21" knowledge management system and the "SMILE" integrated mission-critical operational system, continued brisk sales of color copiers, computers and servers resulted in a 5.7% rise in net sales to ¥238,729 million.

Service & Support Business

The Service & Support Business offers total support for systems installed by customers with supplies, hardware and software maintenance, telephone support and IT education. Continued strong growth in the "tanomail" office supply mail-order services via Website and catalog channels combined with favorable performance in maintenance and similar fields to fuel a 12.3% increase in net sales to ¥130,959 million.

Other Business

In Other Business, the construction industry, in which Fujimi Construction Co., Ltd. operates, continued to experience harsh conditions, but aggressive marketing activities resulted in a 49.4% increase in net sales to ¥2,792 million.

Summary of Income and Expenses

Despite a 7.1% increase in cost of sales to ¥285,655 million, gross profit increased 11.7% to ¥86,825 million as a result of increased net sales as well as a 0.7 percentage point increase in the gross profit margin to 23.3%.

Operating income jumped 84.5% to ¥17,009 million against the backdrop of increased gross profit and a 1.2 percentage point decline in SG&A expenses to net sales to 18.7%. Consequently, the operating income to net sales ratio improved 1.9 percentage points.

Recurring profit achieved a record high for the fourth-straight fiscal year to rise 88.1% to ¥17,036 million following a decrease in other expenses on the back of lower interest expenses.

Despite ¥1,724 million in amortization of transition amount arising from adopting new accounting standard for

retirement benefits as well as the recording of ¥1,491 million in impairment losses for a portion of fixed assets following implementation of asset impairment accounting two terms ahead of schedule, income before income taxes and minority interests soared 301.5% to ¥18,548 million from the contribution of ¥5,481 million in extraordinary income associated with the gain from the exemption from the obligation under the substitutional portion of social welfare pension fund.

In aggregate, net income soared 357.7% to ¥11,247 million and net income per share rose dramatically from ¥77.67 in the previous fiscal year to ¥355.88.

Financial Position

	Millions of yen			
	2003	2004	Difference, year to year	% change, year to year
Assets:	¥162,144	¥167,228	+5,084	+3.1%
Current assets	78,918	87,984	+9,065	+11.5
Fixed assets	83,226	79,244	-3,981	-4.8
Liabilities:	117,572	111,463	-6,108	-5.2
Current liabilities	100,683	100,409	-274	-0.3
Long-term liabilities	16,888	11,054	-5,834	-34.5
Minority interests	594	1,098	+503	+84.8
Shareholders' equity	43,978	54,667	+10,688	+24.3

Assets

Total assets edged up ¥5,084 million (3.1%) to ¥167,228 million. Current assets rose ¥9,065 million (11.5%) to ¥87,984 million on the back of higher cash, time deposits and other cash equivalents as well as accounts and notes receivable. Fixed assets edged down ¥3,981 million (4.8%) to ¥79,244 million from loss on sale of the former head office, valuation loss on a portion of fixed assets following early implementation of asset impairment accounting and accumulated depreciation on buildings and structures.

Liabilities

Total liabilities declined ¥6,108 million (5.2%) to ¥111,463 million. Current liabilities edged down ¥274 million (0.3%) to ¥100,409 million. Long-term liabilities fell ¥5,834 million (34.5%) to ¥11,054 million on account of repayment of long-term debts using surplus cash provided by operating activities.

Shareholders' Equity

Shareholders' equity grew ¥10,688 million (24.3%) to ¥54,667 million. The key factors for this growth were increased retained earnings and excess of land revaluation after tax-effect accounting following sale of land from the former head office.

The interest coverage ratio was 48.94 times; interest-bearing debt ratio was 12.76%; return on assets (ROA) was 10.36%; and return on equity (ROE) was 22.80%.

	2003	2004
Interest coverage ratio (times)	17.57	48.94
Interest-bearing debt ratio (%)	22.73	12.76
ROA* ¹ (%)	5.97	10.36
ROE* ² (%)	5.69	22.80

*1 ROA = Business profit/total assets (average during the year)

Business profit = Operating income + interest received + dividends received

*2 Figures for ROE are calculated using average shareholders' equity.

Cash flows

	Millions of yen			
	2003	2004	Difference, year to year	% change, year to year
Cash flows from operating activities	¥15,749	¥23,494	+7,745	+49.2%
Cash flows from investing activities	-23,405	-3,245	+20,160	—
Cash flows from financing activities	6,284	-15,617	-21,901	—
Cash and cash equivalents at end of year	3,020	7,717	+4,696	+155.5

Cash and cash equivalents at end of year jumped 155.5% to ¥7,717 million.

Cash provided by operating activities increased ¥7,745 million (49.2%) to ¥23,494 million. Key factors were increased income before income taxes and minority interests as well as accounts and notes payable.

Cash used in investing activities declined ¥20,160 million to ¥3,245 million, chiefly from a significant decline in payments for purchase of property, plant and investment. There were, however, other payments for purchase of property, plant and investment pertaining to the new head office in the previous fiscal term.

Cash used in financing activities was ¥15,617 million. Cash used in financing activities was ¥15,617 million, compared to cash provided by financing activities of ¥6,284 million in the previous term. The key factors were lower short-term bank loans and a decrease in proceeds from long-term debts.

Outlook

In the current fiscal year ending December 31, 2005, consolidated projections call for a 5.0% increase in net sales to ¥391 billion, a 5.7% rise in recurring profit to ¥18 billion and a 22.5% decline in net income to ¥8,720 million.

Consolidated Balance Sheets

OTSUKA CORPORATION and Its Consolidated Subsidiaries
December 31, 2003 and 2004

Thousands of
U.S. dollars
(Note 3)

	Millions of yen		2004
	2003	2004	
ASSETS			
Current assets			
Cash, time deposits and other cash equivalents (Notes 11 and 15)	¥ 4,353	¥ 9,043	\$ 86,785
Accounts and notes receivable:			
Trade	49,406	54,415	522,224
Unconsolidated subsidiaries and affiliates	30	11	107
Other	4,614	3,383	32,475
	54,051	57,810	554,807
Less: Allowance for bad debts	(336)	(299)	(2,873)
	53,714	57,511	551,933
Inventories (Note 6)	16,574	16,277	156,211
Deferred tax assets (Note 10)	1,499	1,794	17,226
Other current assets	2,776	3,357	32,221
Total current assets	78,918	87,984	844,377
Investments and advances			
Investments in securities (Note 4)	2,771	2,943	28,249
Investments in unconsolidated subsidiaries and affiliates	473	379	3,645
Guarantee deposits	2,807	2,699	25,905
Deferred tax assets non-current (Note 10)	2,725	2,437	23,389
Deferred tax assets on revaluation of land	8,386	6,228	59,779
Other investments	1,614	4,960	47,606
Less: Allowance for bad debts	(929)	(786)	(7,550)
	17,850	18,862	181,025
Property, plant and equipment (Notes 14 and 15)			
Land	18,926	17,592	168,833
Buildings and structures	67,224	65,111	624,874
Construction in progress	1	—	—
Others	9,629	11,218	107,667
	95,781	93,923	901,375
Less: Accumulated depreciation	(37,047)	(39,325)	(377,401)
Net property, plant and equipment	58,734	54,598	523,974
Intangibles and deferred charges			
Software	5,837	5,197	49,881
Others	804	586	5,624
	6,641	5,783	55,506
Total assets	¥162,144	¥167,228	\$1,604,883

The accompanying notes are an integral part of these statements.

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2003	2004	2004
LIABILITIES, MINORITY INTERESTS AND SHAREHOLDERS' EQUITY			
Current liabilities			
Short-term bank loans (Note 7)	¥ 22,756	¥ 13,850	\$ 132,917
Current maturities of long-term debts (Note 7)	8,224	6,208	59,580
Accounts and notes payable:			
Trade	36,411	42,918	411,886
Unconsolidated subsidiaries and affiliates	177	232	2,230
Other	18,977	20,531	197,038
	55,566	63,682	611,155
Income taxes payable (Note 10)	2,418	3,112	29,872
Other current liabilities	11,718	13,555	130,092
Total current liabilities	100,683	100,409	963,619
Long-term liabilities			
Long-term debt (Note 7)	5,878	1,279	12,274
Reserve for retirement benefits (Note 8)	10,778	9,572	91,866
Deferred tax liabilities non-current (Note 10)	79	26	253
Other long-term liabilities	151	176	1,693
	16,888	11,054	106,088
Minority interests in consolidated subsidiaries	594	1,098	10,539
Contingent liabilities (Note 9)			
Shareholders' equity			
Common stock:			
Authorized: 112,860,000 shares			
Outstanding: December 31, 2003 31,667,020 shares			
December 31, 2004 31,667,020 shares	10,374	10,374	99,566
Capital surplus	16,254	16,254	155,995
Retained earnings	29,485	36,932	354,439
Excess of land revaluation after tax-effect accounting (Note 14)	(12,219)	(9,075)	(87,098)
Unrealized gain on investment securities after tax-effect accounting	325	413	3,965
Foreign currency translation adjustment	(133)	(122)	(1,178)
Less: Treasury stock			
December 31, 2003 63,800 shares			
December 31, 2004 63,990 shares	(108)	(109)	(1,053)
Total shareholders' equity	43,978	54,667	524,636
Total liabilities, minority interests and shareholders' equity	¥162,144	¥167,228	\$1,604,883

The accompanying notes are an integral part of these statements.

Consolidated Statements of Income

OTSUKA CORPORATION and Its Consolidated Subsidiaries
For the years ended December 31, 2003 and 2004

Thousands of
U.S. dollars
(Note 3)

	Millions of yen		2004
	2003	2004	
Net sales (Note 18)	¥344,377	¥372,481	\$3,574,679
Cost of sales (Notes 17 and 18)	266,651	285,655	2,741,417
Gross profit	77,725	86,825	833,261
Selling, general and administrative expenses (Notes 17 and 18)	68,503	69,815	670,018
Operating income	9,221	17,009	163,243
Other income (expenses)			
Interest and dividend income	55	54	522
Interest expenses	(528)	(348)	(3,345)
Gain on sale of property, plant and equipment	136	—	—
Gain on sale of investments in securities	25	9	86
Gain on sale of investments in unconsolidated subsidiaries	—	456	4,382
Transfer from allowance for bad debts	—	93	892
Gain from the exemption from the obligation under the substitutional portion of social welfare pension fund	—	5,481	52,607
Dilution gain from change in equity interest	—	248	2,380
Loss on sale / disposal of property, plant and equipment	(346)	(808)	(7,760)
Impairment losses(Notes2(16)and16)	—	(1,491)	(14,315)
Loss on revaluation/ sale of investments in securities	(798)	(253)	(2,433)
Loss on revaluation/ sale of investments in unconsolidated subsidiaries	(32)	(26)	(250)
Loss on revaluation of membership	(15)	(23)	(229)
Loss on withdrawal from over-the-counter sales business activities(Note16)	(661)	—	—
Removal costs for head office(Note16)	(607)	—	—
Amortization of transition amount arising from adopting new accounting standard for retirement benefits	(2,135)	(1,724)	(16,551)
Losses on the settlement of the retirement benefits plan	—	(448)	(4,304)
Other, net	306	321	3,082
	(4,602)	1,538	14,764
Income before income taxes and minority interests	4,619	18,548	178,007
Income taxes (Note 10)			
Current	3,886	5,040	48,373
Deferred	(1,839)	2,036	19,544
	2,047	7,077	67,918
Minority interests in net gains of consolidated subsidiaries	114	224	2,152
Net income	¥ 2,457	¥ 11,247	\$ 107,937
		yen	U.S. dollars (Note 3)
Net income and dividends per share (Note 2(14))			
Net income	¥77.67	¥355.88	\$3.41
Cash dividends	20.00	55.00	0.52

The accompanying notes are an integral part of these statements.

Consolidated Statements of Shareholders' Equity

OTSUKA CORPORATION and Its Consolidated Subsidiaries								Millions of yen	
For the years ended December 31, 2003 and 2004									
	Number of shares of common stock	Common stock	Capital surplus	Retained earnings	Excess of land revaluation	Unrealized gain on investment securities	Foreign currency translation adjustment	Treasury stock	
Balance at December 31, 2002	31,667,020	¥10,375	¥16,255	¥27,745	¥(12,134)	¥212	¥(102)	¥ (0)	
Increase due to inclusion of									
subsidiaries in the consolidation	—	—	—	119	—	—	—	—	
Sale of land	—	—	—	(203)	203	—	—	—	
Decrease due to changes in tax rates	—	—	—	—	(288)	—	—	—	
Unrealized gain on investment securities	—	—	—	—	—	113	—	—	
Foreign currency translation adjustment	—	—	—	—	—	—	(32)	—	
Net income for the year	—	—	—	2,457	—	—	—	—	
Cash dividends paid	—	—	—	(633)	—	—	—	—	
Purchase of treasury stock	—	—	—	—	—	—	—	(108)	
Balance at December 31, 2003	31,667,020	¥10,374	¥16,254	¥29,485	¥(12,219)	¥325	¥(133)	¥(108)	
Sale of land	—	—	—	(3,143)	3,143	—	—	—	
Retirement of treasury stocks relating to merger	—	—	—	(24)	—	—	—	—	
Unrealized gain on investment securities	—	—	—	—	—	88	—	—	
Foreign currency translation adjustment	—	—	—	—	—	—	11	—	
Net income for the year	—	—	—	11,247	—	—	—	—	
Cash dividends paid	—	—	—	(632)	—	—	—	—	
Purchase of treasury stock	—	—	—	—	—	—	—	(0)	
Balance at December 31, 2004	31,667,020	¥10,374	¥16,254	¥36,932	¥ (9,075)	¥413	¥(122)	¥(109)	

Thousands of U.S. dollars (Note 3)								
	Number of shares of common stock	Common stock	Capital surplus	Retained earnings	Excess of land revaluation	Unrealized gain on investment securities	Foreign currency translation adjustment	Treasury stock
Balance at December 31, 2003	31,667,020	\$99,566	\$155,995	\$282,971	\$(117,268)	\$3,119	\$(1,285)	\$(1,044)
Sale of land	—	—	—	(30,170)	30,170	—	—	—
Retirement of treasury stocks relating to merger	—	—	—	(233)	—	—	—	—
Unrealized gain on investment securities	—	—	—	—	—	845	—	—
Foreign currency translation adjustment	—	—	—	—	—	—	106	—
Net income for the year	—	—	—	107,937	—	—	—	—
Cash dividends paid	—	—	—	(6,065)	—	—	—	—
Purchase of treasury stock	—	—	—	—	—	—	—	(9)
Balance at December 31, 2004	31,667,020	\$99,566	\$155,995	\$354,439	\$ (87,098)	\$3,965	\$(1,178)	\$(1,053)

The accompanying notes are an integral part of these statements.

Consolidated Statements of Cash Flows

OTSUKA CORPORATION and Its Consolidated Subsidiaries
December 31, 2003 and 2004

Thousands of
U.S. dollars
(Note 3)

	Millions of yen		2004
	2003	2004	
Cash flows from operating activities:			
Income before income taxes and minority interests	¥ 4,619	¥18,548	\$ 178,007
Depreciation and amortization	6,704	6,162	59,145
Amortization of difference between cost of investment and equity in net assets of consolidated subsidiaries	63	37	355
Increase(decrease) in reserve for retirement benefits	2,742	(4,531)	(43,489)
Increase(decrease) in allowance for bad debts	148	(179)	(1,722)
Interest and dividend income	(55)	(54)	(522)
Interest expenses	528	348	3,345
Loss on sale / disposal of property, plant and equipment	346	808	7,760
Impairment losses	—	1,491	14,315
Loss on revaluation of investments in securities	798	253	2,431
Gain on sale of investments in consolidated subsidiaries	—	(456)	(4,382)
Loss on revaluation of investments in securities in unconsolidated subsidiaries	32	—	—
Loss on revaluation of membership	15	23	229
Loss on withdrawal from over-the-counter business activities and removal costs for head office	980	—	—
Dilution gain from change in equity interest	—	(248)	(2,380)
Increase in accounts and notes receivable	(1,292)	(2,995)	(28,751)
Decrease (increase) in inventories	(556)	292	2,804
Increase (decrease) in accounts and notes payable	(1,253)	7,544	72,401
Other	5,353	1,087	10,438
Subtotal	19,174	28,132	269,986
Interest and dividend income received	58	55	532
Interest expenses paid	(540)	(351)	(3,376)
Income taxes paid	(2,943)	(4,341)	(41,667)
Net cash provided by operating activities	15,749	23,494	225,475
Cash flows from investing activities:			
Payments for purchase of property, plant and equipment	(22,559)	(3,081)	(29,574)
Proceeds from sale of property, plant and equipment	1,116	1,482	14,226
Payments for software developed	(1,902)	(1,877)	(18,020)
Payments for purchase of investments in securities	(228)	(367)	(3,522)
Proceeds from sale of investments in securities	57	79	767
Proceeds from sale of investments in consolidated subsidiaries(Note 11(3))	—	449	4,314
Payments for long-term loans receivable	(16)	(5)	(47)
Proceeds from long-term loans receivable	36	28	277
Other	90	45	433
Net cash used in investing activities	(23,405)	(3,245)	(31,146)
Cash flows from financing activities:			
Increase(Decrease) in short-term bank loans, net	2,560	(8,910)	(85,508)
Proceeds from long-term debts	16,850	1,800	17,274
Repayments for long-term debts	(12,385)	(8,378)	(80,411)
Proceeds from issue of new shares	—	520	4,998
Cash dividends paid	(631)	(633)	(6,077)
Other	(108)	(15)	(151)
Net cash provided by (used in) financing activities	6,284	(15,617)	(149,876)
Effect of exchange rate changes on cash and cash equivalents	(9)	3	37
Net Increase(Decrease) in cash and cash equivalents	(1,381)	4,635	44,491
Cash and cash equivalents at beginning of year	4,297	3,020	28,985
Increase in cash and cash equivalents for newly consolidated subsidiaries	104	—	—
Increase in cash and cash equivalents due to merger (Note 11(2))	—	60	583
Cash and cash equivalents at end of year (Note 11(1))	¥ 3,020	¥ 7,717	\$ 74,059

The accompanying notes are an integral part of these statements.

Notes to Consolidated Financial Statements

OTSUKA CORPORATION and Its Consolidated Subsidiaries

1. Basis of Presenting the Consolidated Financial Statements

Accounting Principles

The accompanying consolidated financial statements of OTSUKA CORPORATION (the "Company") and its subsidiaries are prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to application and disclosure requirements from International Financial Reporting Standards, and are compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan.

Certain items presented in the consolidated financial statements submitted to the Director of the Kanto Finance Bureau in Japan have been reclassified for the convenience of readers outside Japan.

The consolidated financial statements are not intended to present the consolidated financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

2. Summary of Significant Accounting Policies

(1) Scope of consolidation

The Company had 20 subsidiaries (majority-owned companies) and 16 subsidiaries as at December 31, 2003 and 2004, respectively. The consolidated financial statements include the accounts of the Company and 12 subsidiaries and 11 subsidiaries for the years ended December 31, 2003 and 2004, respectively.

The 11 subsidiaries which were consolidated in the year ended December 31, 2004 are listed below:

	Equity ownership percentage
OSK Co., LTD.	100.0%
Netplan Co., LTD.	100.0%
Alpha Techno Co., LTD.	100.0%
Fujimi Construction Co., LTD.	100.0%
Alpha System Co., LTD.	100.0%
Alpha Net Co., LTD.	100.0%
Otsuka Information Technology Corp.	100.0%
Otsuka Auto Service Co., LTD.	100.0%
Net World Corporation	68.4%
Otsuka Business Service Co., LTD.	65.0%
10art-ni Corporation	53.9%

JPSS Co., LTD. were excluded from consolidation from this fiscal year due to the sale of ownership.

The Company and its consolidated subsidiaries are hereinafter referred to as the "Companies."

Generally, Companies that are more than 50 % owned are classified as subsidiaries and companies that are more than 20 % owned are classified as affiliates. However, companies that are between 40 % and 50 % owned may also be classified as subsidiaries and companies that are between 15 % and 20 % owned may also be classified as affiliates, if the Company substantially controls the investees' management or has significant influence and relationships with the investees, respectively.

The consolidated subsidiaries listed above apply a fiscal year ending on December 31 of each year, which is the same as that of the Company.

The accounts of the remaining 8 and 5 unconsolidated subsidiaries as at December 31, 2003 and 2004, respectively, consisted of insignificant amounts in terms of total assets, net sales, net income and retained earnings, and they have, therefore, been excluded from consolidation.

(2) Elimination of intercompany accounts

For the purposes of preparing the consolidated financial statements, all significant intercompany transactions, account balances and unrealized profits among the Companies have been eliminated in full, and the portion attributable to minority interests is charged/credited to minority interests.

For the elimination of investments in the common stock of consolidated subsidiaries, together with the equity in

the net assets of such subsidiaries, any difference between such investment costs and the amount of underlying equity in the net assets of the subsidiary is deferred and amortized to income over five years on a straight-line basis.

(3) Investments in unconsolidated subsidiaries and affiliates

The Company had 8 unconsolidated subsidiaries and 5 affiliates at December 31, 2003 and 5 unconsolidated subsidiaries and 6 affiliates at December 31, 2004.

No investments in affiliates for the years ended December 31, 2003 and 2004, were accounted for by the equity method. Investments in unconsolidated subsidiaries and affiliates not accounted for by the equity method were carried at cost or less, since they did not have a material impact on consolidated net income and retained earnings in the consolidated financial statements.

(4) Translation of foreign currency

All monetary assets and liabilities denominated in foreign currencies, whether long-term or short-term, are translated into Japanese yen at the exchange rates prevailing at the balance sheet date. Resulting gains and losses are included in net profit or loss for the period.

Assets and liabilities of the foreign subsidiaries and affiliates are translated into Japanese yen at the exchange rates prevailing at the balance sheet date. The shareholders' equity at the beginning of the year is translated into Japanese yen at the historical rates. Profit and loss accounts for the year are translated into Japanese yen using the average exchange rate during the year. Differences in yen amounts arising from the use of different rates are presented as "Foreign currency translation adjustment" in shareholders' equity.

(5) Cash and cash equivalents

Cash and cash equivalents in the consolidated statements of cash flows are composed of cash in hand, bank deposits which can be withdrawn on demand and short-term investments with an original maturity of three months or less and which represent a minor risk of fluctuation in value.

(6) Inventories

Inventories are valued by methods according to the category of inventories as follows:

Merchandise and maintenance parts:	Merchandise and maintenance parts are stated at cost mainly determined by the moving-average method
Work-in-process:	Work-in-process is stated at cost determined by the individual cost method
Supplies:	Supplies are stated at cost determined by the latest purchase price

(7) Financial instruments

(a) Securities

Securities held by the Company and its subsidiaries are classified into two categories:

• Equity investment in subsidiaries and affiliates

Investments of the Company in equity securities issued by unconsolidated subsidiaries and affiliates are accounted for by the equity method. In exceptional cases, investments in certain unconsolidated subsidiaries and affiliates are stated at cost, mainly determined by the moving-average method, because the effect of application of the equity method would be immaterial.

• Other securities

Securities with a market quotation are stated at fair value, based on market prices at the balance sheet date. (Unrealized gains/losses from valuation of marketable securities are charged directly to shareholders' equity at a net-of-tax amount, while cost of sale is determined by the moving-average method.)

Securities without a market quotation are stated at cost; this is calculated by the moving-average method.

(b) Derivatives

All derivatives are stated at fair value, with changes in fair value included in net profit or loss for the period in which they arise, except for derivatives that are designated as "hedging instruments."

(c) Hedge accounting

Gains or losses arising from changes in fair value of the derivatives designated as "hedging instruments" are deferred

as an asset or liability and included in net profit or loss in the same period during which the gains and losses on the hedged items or transactions are recognized.

Also, if interest rate swap contracts are used as a hedge and meet certain hedging criteria, the amount to be paid or received under the interest rate swap contract is added to or deducted from the interest on the assets or liabilities for which the swap contract was executed.

The derivatives designated as hedging instruments by the Companies are principally interest swaps, forward exchange contracts and currency swaps. The related hedged items are trade bank loans and accounts payable.

The Companies have a policy of utilizing the above hedging instruments in order to reduce the Companies' exposure to the risks of interest and foreign exchange rate fluctuation. Thus, the Companies' purchases of the hedging instruments are limited to, at maximum, the amounts of the hedged items.

The Company evaluates the effectiveness of its hedging activities by reference to the accumulated gains or losses on the hedging instruments and the related hedged items from the commencement of the hedges.

(8)Property, plant and equipment

Depreciation is computed using the reducing-balance method, at rates based on the estimated useful lives of assets, which are prescribed by Japanese income tax laws. Depreciation of buildings newly acquired after April 1, 1998 has been provided based on the straight-line method in conformity with Japanese tax laws.

Normal repairs and maintenance, including minor renewals and improvements, are charged to income as incurred.

(9)Accounting for leases

Leases that transfer substantially all the risks and rewards of ownership of the assets to lessees are accounted for as capital leases, except that leases that do not transfer ownership of the assets at the end of the lease term are accounted for as operating leases, in accordance with accounting principles and practices generally accepted in Japan.

(10)Software

The amortization of the costs of software developed for external sales is computed at an amount based on sales of depreciation of the quantity during the year to the total estimated sales quantity. However, the amortization costs should not be lower than the amount computed based on asset purchase value on a straight-line basis over the estimated remaining useful life of the asset, which is 3 years.

Software developed for internal use is amortized on a straight-line basis over the estimated useful life of the asset, which is 5 years.

(11)Accounting for income taxes

Income taxes of the Company and its domestic subsidiaries consist of corporate income taxes, local taxes and enterprise taxes.

The Company and its subsidiaries have adopted the deferred tax accounting method. Income taxes were determined using the asset and liability approach, whereby deferred tax assets and liabilities were recognized in respect of temporary differences between the tax basis of assets and liabilities and those as reported in the consolidated financial statements.

(12)Allowance for bad debts

An allowance for bad debts is provided at an amount of potential losses from uncollectable receivables based on the actual historical rate of losses from bad debts for ordinary receivables, and on the estimated recoverability of specific doubtful receivables.

(13)Reserve for retirement benefits

(a) Retirement benefits for employees

The reserve for retirement benefits represents the estimated present value of projected benefit obligations in excess of the fair value of the plan assets, except that the unrecognized transition amount arising from adopting the new accounting standard is amortized on a straight-line basis over 5 years, the unrecognized actuarial differences are amortized on a straight-line basis over a period of 12 years from the year following the year in which they arise, and the unrecognized prior service cost is amortized on a straight-line basis over a period of 12 years.

(Fiscal year 2003)

- Termination of substitute portion employee pension fund

The employees' pension fund of the OTSUKA Group was permitted immunity from future payments by the Minister of Health, Labour and Welfare.

In accordance with the JICPA's revised Accounting for Retirement Benefits, the Company and its consolidated subsidiaries did not record a gain on the termination of the requirement to make pension contributions to the government assuming the obligation for the government portion of the Company's employment pension scheme and related assets have been transferred to the government. The unrecognized prior service cost generated in this period is calculated in accordance with Note 8 (4) "Computation basis of pension liabilities."

(Fiscal year 2004)

On February 1, 2004, the Company and certain domestic subsidiaries were granted the approval by the government relieving them of the obligation to pay benefits related to past employee services under the substitutional portion. Since then on August 17, 2004, the Company and 7 consolidated subsidiaries restituted substitutional portion.

On April, 2004, the Company and certain of its subsidiaries changed the type of a termination allowance plan. It was changed from a defined-benefit to an agreement-type corporate pension plan.

(b) Retirement benefits for directors

The Company and 4 consolidated subsidiaries have provided for accrued retirement benefits to directors at an amount equivalent to 100% of the benefits the Company would be required to pay had all eligible directors retired at the balance sheet date.

(Fiscal year 2004)

Along with the maintenance of bylaw, 4 consolidated subsidiaries have provided for accrued retirement benefits to directors from this fiscal year. The effect is negligible.

(14) Net income and dividends per share

Net income per common share is based upon the weighted average number of common shares outstanding during each year. Cash dividends per share shown for each year in the consolidated statements of income represent dividends declared as applicable to the respective year.

(Fiscal year 2003)

Effective from the fiscal year 2003, the Company adopted the Statement of Accounting Standard No.2 "Accounting Standard for Earnings per Share" and of Accounting Standard Implementation Guideline No.4 "Implementation Guidance on Accounting Standard for Earnings per Share" issued by the Accounting Standards Board of Japan for the computation of net income per share of common stock. The adoption of these statements did not have any material impact on the financial statements.

(15) Accounting for the consumption tax

The Japanese Consumption Tax Law generally imposes consumption tax at a flat rate on all domestic consumption of goods and services. The consumption tax withheld upon sale is not included in the amount of "Net sales" in the accompanying consolidated statements of income but is recorded as a liability. Consumption tax, which is paid by the Company and domestic subsidiaries on purchases of goods and services, is not included in the amounts of costs/expenses in the consolidated statements of income, but is offset against the balance withheld, and the net balance is included in "Other current liabilities" in the consolidated balance sheets.

(16) Change of accounting policy

(Fiscal year 2003)

During the year ended December 31, 2003, the Company changed the consolidated statement of income classification for the system engineering costs relating to commissioned business from selling, general and administrative expenses to cost of sales, according to man-hours. This change was made due to the growth in the significance of the system engineering costs and the restructuring of the Company's cost accounting system. This reclassification resulted in an increase in cost of sales and decrease in selling, general and administrative expenses of 1,761 millions yen for the year ended December 31, 2003, as compared with the amounts which would have been reported if the previous policy had been applied consistently. This reclassification did not have an impact on operating income and income before taxes.

(Fiscal year 2004)

Accounting standard for impairment of Fixed Assets

On August 9, 2002, the Business Accounting Council in Japan issued "Accounting Standard for Impairment of Fixed Assets." The standard requires that fixed assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss shall be recognized in the income statement by reducing the carrying amount of impaired assets or groups of assets to the recoverable amount to be measured as the higher of net selling price and value in use.

The standard shall be effective for fiscal years beginning April 1, 2005. However, earlier adoption is permitted for fiscal years beginning January 1, 2005 and for fiscal years ending between December 31, 2004 and December 31, 2005.

The Company and its subsidiaries adopted this standard with effect from the year ended December 31, 2004. As a result of this adoption, income before income taxes decreased by 1,491 million yen (14,315 thousand U.S. dollars). The impairment loss was included in accumulated depreciation.

(17) Rounding of amounts

Sums of less than a million yen are rounded down.

3. U.S. Dollar Amounts

Amounts in U.S. dollars are included solely for the convenience of readers outside Japan. The rate of ¥104.2=US\$1, the rate of exchange on December 31, 2004, has been used in translation. The inclusion of such amounts is not intended to imply that Japanese yen have been or could be readily converted, realized or settled in U.S. dollars at this or any other rate.

4. Investments in Securities

At December 31, 2003 and 2004 investments in securities were as follows:

(1) Other securities with fair value

	Millions of yen						Thousands of U.S. dollars		
	2003			2004			2004		
	Cost	Carrying amount	Differences	Cost	Carrying amount	Differences	Cost	Carrying amount	Differences
Fair value greater than cost									
Stocks	¥667	¥1,214	¥546	¥ 747	¥1,444	¥697	\$ 7,173	\$13,862	\$6,689
Bonds	—	—	—	—	—	—	—	—	—
Other securities	96	114	17	38	62	24	368	599	230
	¥764	¥1,328	¥564	¥ 785	¥1,506	¥721	\$ 7,542	\$14,462	\$6,919
Fair value less than or equal to cost									
Stocks	¥127	¥ 111	¥(16)	¥ 350	¥ 333	¥(17)	\$ 3,366	\$ 3,201	\$ (165)
Bonds	—	—	—	—	—	—	—	—	—
Other securities	—	—	—	51	50	(0)	489	484	(5)
	¥127	¥ 111	¥(16)	¥ 401	¥ 384	¥(17)	\$ 3,856	\$ 3,685	\$ (171)
Total	¥892	¥1,440	¥548	¥1,187	¥1,890	¥703	\$11,398	\$18,147	\$6,748

(2) Other securities sold in 2003 and 2004 (for the years ended December 31, 2003 and 2004)

						Millions of yen	Thousands of U.S. dollars		
2003			2004			2004			
Amount for sale	Total gains on sale	Total losses on sale	Amount for sale	Total gains on sale	Total losses on sale	Amount for sale	Total gains on sale	Total losses on sale	
¥18	¥25	¥—	¥79	¥9	¥0	\$767	\$92	\$2	

(3) Securities not stated at fair value

		Millions of yen	Thousands of U.S. dollars
2003		2004	2004
Stated amount on consolidated balance sheets		Stated amount on consolidated balance sheets	Stated amount on consolidated balance sheets
Other securities			
Unlisted stocks	¥1,319	¥1,040	\$9,985
Mid-term government bonds fund	2	2	20
Preferred subscription certification	10	10	95

(4) Prospected amounts of redemption of other securities with maturity dates subsequent to the consolidated balance sheet dates

		Millions of yen		Thousands of U.S. dollars	
2003		2004		2004	
Within one year	More than one year	Within one year	More than one year	Within one year	More than one year
Others	—	¥10	—	—	\$95
Total	—	¥10	—	—	\$95

5. Derivative Information

At December 31, 2003 and 2004 derivatives were as follows:

Currency

				Millions of yen	
				2003	
Contractual value or notional principal amount				Valuation gain(loss)	
Total		Over one year		Fair value	
Currency swap Purchased U.S.dollar	¥377	¥377	¥336	¥(41)	

				Millions of yen	
				2004	
Contractual value or notional principal amount				Valuation gain(loss)	
Total		Over one year		Fair value	
Currency swap Purchased U.S.dollar	¥377	¥377	¥328	¥(48)	

				Thousands of U.S. dollars	
				2004	
Contractual value or notional principal amount				Valuation gain(loss)	
Total		Over one year		Fair value	
Currency swap Purchased U.S.dollar	\$3,621	\$3,621	\$3,155	\$(465)	

(Note)

Except for derivatives that are designed as hedging instruments

6. Inventories

Inventories at December 31, 2003 and 2004 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Merchandise and maintenance parts	¥14,820	¥15,356	\$147,376
Work-in-process	1,587	746	7,167
Supplies	166	173	1,666
	¥16,574	¥16,277	\$156,211

7. Short-term Bank Loans and Long-term Debt

The annual average interest rates applicable to short-term bank loans at December 31, 2003 and 2004 were 0.77% and 0.74%, respectively.

Long-term debt at December 31, 2003 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Long-term loans from banks with annual interest rates from 0.70% to 3.12%	¥12,102	¥7,487	\$71,855
0.75% secured Japanese yen bonds due March 2004	2,000	—	—
	14,102	7,487	71,855
Less : Current maturities of long-term debts	(8,224)	(6,208)	(59,580)
	¥ 5,878	¥1,279	\$12,274

Aggregate annual maturities of long-term debt subsequent to December 31, 2004 are as follows:

Year ending December 31	Millions of yen	Thousands of U.S. dollars
2005	¥6,208	\$59,580
2006	759	7,284
2007	490	4,702
2008	30	287
	¥7,487	\$71,855

8. Reserve for Retirement Benefits

(1) Retirement benefit plan

(Fiscal year 2003)

The Company and certain of its subsidiaries operate a qualified pension plan, a welfare pension plan and a termination allowance plan as defined-benefit pension plans.

(Fiscal year 2004)

The Company and certain of its subsidiaries operate a fund-type corporate pension plan, an agreement-type corporate pension plan and a termination allowance plan as defined-benefit pension plans.

(2) The reserve for retirement benefits as of December 31, 2003 and 2004 is analyzed as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Projected benefit obligations	¥(58,148)	¥(35,894)	\$(344,476)
Plan assets	34,325	27,708	265,915
	(23,822)	(8,186)	(78,560)
Unrecognized transition amount	4,271	1,668	16,008
Unrecognized prior service cost	(2,714)	(7,770)	(74,573)
Unrecognized actuarial differences	12,212	8,758	84,052
	(10,052)	(5,530)	(53,073)
Prepaid pension cost	—	(3,734)	(35,840)
Reserve for retirement benefits	¥(10,052)	¥ (9,264)	\$ (88,913)

The balance of the reserve for retirement benefits in the accompanying consolidated balance sheets at December 31, 2003 and 2004 included retirement benefits for directors in the amounts of 726 million yen and 307 million yen (2,953 thousand U.S. dollars), respectively.

(Fiscal year 2003)

The above table includes the amounts related to the portion subject to the Japanese Welfare Pension Insurance Law.

(3) Pension expenses related to retirement benefits for the year ended December 31, 2003, and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Service cost	¥2,905	¥2,708	\$25,992
Interest cost	1,248	667	6,403
Expected return on plan assets	(1,107)	(1,128)	(10,828)
Amortization of transition amount	2,135	1,724	16,551
Amortization of the unrecognized prior service cost	(252)	(539)	(5,173)
Amortization of the unrecognized actuarial differences	974	530	5,090
Additional benefits for employees' early retirement	3	—	—
Net pension expense	¥5,908	¥3,963	\$38,036
Gain from the exemption from the obligation under the substitutional portion of social welfare pension fund	—	(5,481)	(52,607)
Loss on revaluation of investments in securities in unconsolidated subsidiaries	—	448	4,304

Service cost includes the pension costs of subsidiaries under the simplified method

(4) Computation Basis of Pension Liabilities

As of December 31, 2003 and 2004

	2003	2004
Discount rate	2.0%	1.5%
Expected rate of return on plan assets	3.9%	3.7%
Periodic allocation principle for projected benefit obligation	Standard of fixed-amount-for-period	Standard of fixed-amount-for-period
Amortization of unrecognized prior service cost	12 years	12 years
Amortization of transition amount	5 years	5 years
Amortization of unrecognized actuarial differences	12 years from the fiscal year following occurrence	12 years from the fiscal year following occurrence

9. Contingent Liabilities

The Company was contingently liable for guarantees of loans at December 31, 2003 and 2004 as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Loans taken out by:			
NACOS COMPUTER SYSTEMS CORP.	¥48	¥40	\$383
	¥48	¥40	\$383

10. Income Taxes

The statutory tax rate used for calculating deferred tax assets and liabilities at December 31, 2004 was 42.1%.

At December 31, 2004, the reconciliation of the statutory tax rate to the effective income tax rate was as follows:

Statutory tax rate		42.1%
Entertainment expenses		0.7
Inhabitants' tax per capita		0.7
Valuation allowance		(3.2)
Consolidated adjustment account		0.1
Effect on deferred tax assets and deferred tax liabilities from a change in the tax regulations		(0.5)
Deduction for investment in information technologies		(2.0)
Others		0.3
Effective tax rate		38.2%

At December 31, 2003 and 2004, significant components of the deferred tax assets and liabilities were as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Deferred tax assets:			
Allowance for bad debts	¥ 254	¥ 208	\$ 2,004
Enterprise taxes	304	357	3,430
Accrued bonuses	737	970	9,311
Retirement benefits for employees	3,412	3,730	35,796
Retirement benefits for directors	327	137	1,317
Membership	303	303	2,915
Impairment losses	—	951	9,128
Software cost	157	225	2,167
Operating loss carryforwards	884	412	3,955
Eliminated unrealized profits	461	411	3,949
Other	652	651	6,248
Total deferred tax assets	7,495	8,359	80,226
Less: Valuation allowance	(714)	(229)	(2,206)
Net deferred tax assets	6,781	8,129	78,020
Deferred tax liabilities:			
Reserve for computer program	2,397	2,103	20,191
Prepaid pension cost	—	1,522	14,607
Unrealized gain on investment securities	223	283	2,721
Other	19	17	166
Total deferred tax liabilities	2,640	3,927	37,687
Net deferred tax assets	¥4,141	¥4,202	\$40,333

(Fiscal year 2003)

On March 31, 2003, the Japanese National Diet approved various changes to the calculation of the statutory local enterprise tax for companies with capital in excess of 100 million yen effective April 1, 2004.

This resulted in a reduction in deferred taxes assets of 67 million yen and a deferred tax assets revaluation of 288 million yen, and an increase in excess of land revaluation after tax-effect accounting of 288 million yen and unrealized gain on investment securities after tax-effect accounting by 7 million yen as compared with the amounts that would have been reported if the previous tax rate had been fully applied consistently for the fiscal year 2003. Deferred income tax was also reduced by 74 million yen as a result of these changes in statutory local enterprise tax regulations.

11. Supplementary Cash Flow Information

(1) Cash and cash equivalents consisted of:

	Millions of yen		Thousands of
	2003	2004	U.S. dollars
Cash, time deposits and other cash equivalents	¥4,353	¥9,043	\$86,785
Time deposits with deposit terms of more than three months	(1,332)	(1,326)	(12,725)
Cash and cash equivalents at end of year	¥3,020	¥7,717	\$74,059

(2) The property and the debt that were taken over from Quark Co., LTD., which merged with the Alpha System Co., LTD (consolidated subsidiary), were as follows:

(Fiscal year 2004)

	Millions of yen	Thousands of
		U.S. dollars
Current assets	¥ 99	\$953
Non-current assets	3	37
Total assets	¥103	\$990
Current liabilities	¥ 51	\$492
Non-current liabilities	8	84
Total liabilities	¥ 60	\$576

(3) The main items of property and debt of JPSS Co., LTD. excluded from the scope of consolidation through share transfer are as follows:

(Fiscal year 2004)

	Millions of yen	Thousands of
		U.S. dollars
Current assets	¥258	\$2,478
Non-current assets	34	328
Current liabilities	(211)	(2,032)
Non-current liabilities	(22)	(217)
Minority interests in consolidated subsidiaries	(1)	(10)
Consolidated adjustment account	16	158
Gain on sale of investments in securities	226	2,175
Amount for sale of investments in securities	300	2,879
Cash and cash equivalents	(110)	(1,063)
Proceeds from sale of investments in securities	¥189	\$1,815

12. Subsequent Events

(1) Appropriation

The following appropriation of the Company's retained earnings in respect of the year ended December 31, 2004 was as proposed by the Board of Directors and approved by the shareholders at the annual general meeting held on March 30, 2005:

Appropriation	Millions of yen	Thousands of U.S. dollars
Cash dividends (¥55.00 per share)	¥1,738	\$16,681

(2) Termination of substitute portion employee pension fund

(Fiscal year 2003)

On February 1, 2004, the Company and its seven consolidated subsidiaries obtained governmental approval for the separation of the substitute portion employee pension fund service under the substitutional portion (second approval) from the Ministry of Health, Labour and Welfare. In accordance with Article 44-2 of Practical Guidelines on Accounting for Post-retirement Benefits (Interim Report) issued by the JICPA, the Company and its seven consolidated subsidiaries recognized a one-off profit resulting from the separation of the substitutional portion of the EPF amounting to 5,481 million yen at the date of the approval.

13. Lease Transactions

Acquisition costs, accumulated depreciation and net book values of leased assets at December 31, 2003 and 2004 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Acquisition cost	¥6,465	¥4,589	\$44,049
Accumulated depreciation	(4,298)	(3,005)	(28,841)
Net book value	¥2,167	¥1,584	\$15,208

Accumulated depreciation at December 31, 2004 included an accumulated impairment loss of 0 million yen (3 thousand U.S. dollars).

Future minimum lease payments under finance leases at December 31, 2003 and 2004 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Due within one year	¥1,141	¥ 717	\$ 6,890
Due after one year	1,063	859	8,595
	¥2,205	¥1,613	\$15,485
Accumulated impairment loss on leaseholds	¥ —	¥ 0	\$ 3

Lease rental expenses, depreciation and interest expenses for the years ended December 31, 2003 and 2004 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Lease rental expenses	¥1,650	¥1,223	\$11,746
Depreciation	1,506	1,158	11,121
Release of accumulated impairment loss on leaseholds	—	—	—
Interest expenses	73	42	407
Impairment loss on leaseholds	—	0	3

Depreciation expense is calculated using the straight-line method, with the lease period as the useful life and a residual value of zero.

The amounts of future lease payments on operating leases at December 31, 2003 and 2004 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Due within one year	¥204	¥337	\$3,236
Due after one year	150	520	4,990
	¥355	¥857	\$8,227

14. Land Revaluation

Pursuant to the Law on Land Revaluation, the Company revalued land used for business activities on December 31, 2001. The excess of the revalued carrying amount over the book value before revaluation was recorded as "Excess of land revaluation after tax-effect accounting" in shareholders' equity in the accompanying consolidated balance sheets. The land prices used for the revaluation were determined based on the prices in the official notice published by the Commissioner of the National Tax Agency in accordance with Article 2, Paragraphs 3 and 4 of the Enforcement Ordinance on Land Revaluation, after making reasonable adjustments. Revaluation is permitted once only. The excess of the book value after revaluation over the fair value is 1,382 million yen (13,263 thousand U.S. dollars).

15. Pledged Assets

At December 31, 2003 and 2004, assets pledged as collateral for accounts and notes payable and loan from banks were as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2004	2004
Land	¥1,117	¥ 816	\$ 7,834
Buildings	835	832	7,993
Time deposits	11	43	418
	¥1,964	¥1,692	\$16,245

16. Explanatory Notes of Other Income and Expenses

(Fiscal year 2003)

- Loss on withdrawal from over-the-counter sales business activities

"Loss on withdrawal from over-the-counter sales business activities" represents a loss on disposal of equipment and systems due to withdrawal from over-the-counter sales business activities.

- Removal cost of head office

"Removal cost of head office" represents a loss on disposal of equipment and moving costs.

(Fiscal year 2004)

- Impairment losses

The Company acknowledged "Loss on impairment of Fixed Assets" as follows;

a. Grouping

The assets of the Company are grouped into each business department, assets held by hotel business, leaseholds and common assets.

b. Assessment of recoverable value

Recoverable value is assessed net sale value.

c. Assets subject to impairment

- Leaseholds whose fair values have diminished significantly compared to their book value due to the recent decline in land prices.
- Assets which provided a low level operating profit (hotel business) due to excessive depreciation costs arising from investments during the past year.

d. Details of impairment loss

Assets held by hotel business (location: Shizuoka)

	Millions of yen	Thousands of U.S. dollars
Land	¥ 246	\$ 2,368
Buildings and structures	1,082	10,393
Other tangible assets	16	154
Other intangible assets	24	237
Guarantee deposits	0	0
Leaseholds	0	3

Leaseholds (location: Saitama)

	Millions of yen	Thousands of U.S. dollars
Land	¥120	\$1,158

The impairment loss was included in accumulated depreciation.

17. Research and Development Costs

Research and development costs included in cost of sales and selling, general and administrative expenses for the years ended December 31, 2003 and 2004 amounted to 918 million yen and 721 million yen (6,922 thousand U.S. dollars), respectively.

18. Segment Information

The business segment information of the Company and its consolidated subsidiaries for the years ended December 31, 2003 and 2004 is summarized as follows:

(1) Business segment information

	Millions of yen					
	System Integration	Service & Support	Other	Total	Elimination or corporate	Consolidated total
2003						
Net sales to:						
Outside customers	¥225,842	¥116,665	¥1,869	¥344,377	¥ —	¥344,377
Inter-segment sales/transfers	115	131	1,982	2,229	(2,229)	—
	225,958	116,796	3,851	346,606	(2,229)	344,377
Operating expenses	218,793	109,700	3,765	332,258	2,896	335,155
Operating income	¥ 7,165	¥ 7,096	¥ 86	¥ 14,347	¥ (5,126)	¥ 9,221
Assets, depreciation and capital expenditure:						
Assets	¥ 84,943	¥ 54,440	¥2,703	¥142,088	¥20,055	¥162,144
Depreciation and amortization	3,444	2,629	42	6,115	588	6,704
Capital expenditure	13,599	7,570	2	21,172	3,324	24,496

	Millions of yen					
	System Integration	Service & Support	Other	Total	Elimination or corporate	Consolidated total
2004						
Net sales to:						
Outside customers	¥238,729	¥130,959	¥2,792	¥372,481	¥ —	¥372,481
Inter-segment sales/transfers	78	151	2,152	2,382	(2,382)	—
	238,807	131,111	4,945	374,863	(2,382)	372,481
Operating expenses	225,160	122,664	4,858	352,683	2,788	355,471
Operating income	¥ 13,647	¥ 8,446	¥ 86	¥ 22,180	¥ (5,170)	¥ 17,009
Assets, depreciation and capital expenditure:						
Assets	¥ 85,641	¥ 55,667	¥1,959	¥143,268	¥23,960	¥167,228
Depreciation and amortization	3,053	2,461	37	5,552	610	6,162
Impairment losses	—	1,370	—	1,370	120	1,491
Capital expenditure	2,558	2,125	21	4,705	414	5,120

	Thousands of U.S. dollars					
	System Integration	Service & Support	Other	Total	Elimination or corporate	Consolidated total
2004						
Net sales to:						
Outside customers	\$2,291,067	\$1,256,811	\$26,799	\$3,574,679	\$ —	\$3,574,679
Inter-segment sales/transfers	751	1,452	20,658	22,862	(22,862)	—
	2,291,819	1,258,264	47,457	3,597,542	(22,862)	3,574,679
Operating expenses	2,160,847	1,177,199	46,628	3,384,675	26,761	3,411,436
Operating income	\$ 130,972	\$ 81,065	\$ 829	\$ 212,867	\$ (49,623)	\$ 163,243
Assets, depreciation and capital expenditure:						
Assets	\$ 821,892	\$ 534,237	\$18,805	\$1,374,935	\$229,947	\$1,604,883
Depreciation and amortization	29,308	23,622	355	53,285	5,859	59,145
Impairment losses	—	13,156	—	13,156	1,158	14,315
Capital expenditure	24,550	20,402	209	45,162	3,982	49,144

Notes ;

1. Business segments are defined in consideration of the operations of the companies.
2. Significant operations of each segment are as summarized below;
 - (a)The system integration business provides optimized system services ranging from consulting to system design and development, transport and installation and network construction.
 - (b)The service & support business offers total support for systems installed by customers with supplies, hardware and software maintenance, telephone support and IT training.
 - (c)Other business includes the construction industry, automobile maintenance and direct mail production and shipment outsourcing, etc.
3. Significant components of "Eliminations or Corporate" are as follows;

	Millions of yen		Thousands of
	2003	2004	U.S. dollars
Non-allocable operating expenses	¥5,193	¥5,239	\$50,278
Corporate assets	22,102	25,615	245,830

Non-allocable operating expenses include administrative expenses incurred by the management control department of the Company.

Corporate assets include surplus funds, long-term investments (investment securities) and assets used by the management control department of the Company.

Corporate assets include deferred tax assets on the revaluation of land.

4. Depreciation and amortization and capital expenditure include amortization and increase of long-term prepaid expenses.

(2) Segment information by geographic area is not disclosed pursuant to regulations on consolidated financial statements in Japan, since both net sales and assets of the Company and its domestic consolidated subsidiaries, taken as a whole, were more than 90% of consolidated net sales and assets.

(3) Information on overseas sales is not disclosed pursuant to regulations on consolidated financial statements in Japan, since the aggregate of the overseas sales of the Company and its domestic consolidated subsidiaries and overseas consolidated subsidiaries, was less than 10% of consolidated net sales.

(Change of accounting policy)

(Fiscal year 2003)

During the year ended December 31, 2003, the Company changed the consolidated statement of income classification for the system engineering costs relating to commissioned business from selling, general and administrative expenses to cost of sales, according to man-hours. This reclassification resulted in an decrease in the operating expenses of System lintegration of 217 million yen and an increase in the operating income of System lintegration of the same amount, and an increase in the operating cost of Service & Ssupport of 217 million yen and increase in the operating income of Service & Ssupport of the same amount, for the year ended December 31,2003, as compared with the amounts which would have been reported if the previous policy had been applied consistently.

(Fiscal year 2004)

Accounting standard for impairment of Fixed Assets

As described in 'Note 2(16) Change of accounting policy' the Companies and its subsidiaries adopted "Accounting Standard for impairment of Fixed Assets" with effect from the year ended December 31, 2004. The effect of this adoption was to recognize impairment losses on the Service & Support business and the corporate, amounting to 1,370 million yen (13,156 thousand U.S. dollars), 120 million yen (1,158 thousand U.S. dollars), respectively. Operating assets of these business decreased by 1,370 million yen (13,156 thousand U.S. dollars), 120 million yen (1,158 thousand U.S. dollars), respectively.

Report of Independent Auditors

To the Board of Directors and Shareholders of
OTSUKA CORPORATION

We have audited the accompanying consolidated balance sheets of OTSUKA CORPORATION and its subsidiaries as of December 31, 2003 and 2004, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in Japanese yen. 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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated 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 consolidated financial position of OTSUKA CORPORATION and its subsidiaries as of December 31, 2003 and 2004, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

In note

1. As described in note 2(16), during the year ended December 31, 2003, the Company changed the consolidated statement of income classification for the system engineering cost relating to commissioned business from selling, general and administrative expenses to cost of sales, according to man-hours.
2. As described in note 12(2), on February 1, 2004, the Company and its seven consolidated subsidiaries obtained governmental approval for the separation of the substitute portion employee pension fund service under substitutional portion (second approval) from the Ministry of Health, Labour and Welfare.
3. As described in Note 2(16), effective for the year ended March 31, 2004, OTSUKA CORPORATION and its subsidiaries adopted "Accounting Standard for impairment of Fixed Assets" with effect from the year ended December 31, 2004.

The amounts expressed in U.S. dollars, which are provided solely for the convenience of the reader, have been translated on the basis set forth in Note 3 to the accompanying consolidated financial statements.



ChuoAoyama PricewaterhouseCoopers

Tokyo, Japan
March 30, 2005

Principal Group Companies (as of December 31, 2004)

The OTSUKA Group (OTSUKA CORPORATION and its subsidiaries) consists of 16 subsidiaries, including 11 consolidated subsidiaries as well as 6 affiliated companies that carry out System Integration, Service and Support, and Other Business. The 11 consolidated subsidiaries are listed below.

Company Name	Establishment	Capital (¥ million)	Controlling Share	Scope of Business
■ System Integration Business				
OSK Co., Ltd.	1984	300	100.0%	• Development and sale of packaged software
Netplan Co., LTD.	1992	400	100.0%	• Electronic communications construction and interior construction
Alpha System Co., LTD.	1967	80	100.0%	• Consigned software development, packaged software development and ERP consulting business
Net World Corporation	1990	585	68.4%	• Sales and technology support for network-related equipment
10art-ni Corporation	1997	945	53.9%	• Java- and Linux-related product development and corporate information systems construction
Otsuka Information Technology Corp. (Taiwan)	1997	NT\$116 million	100.0%	• Sale of CAD/CAM solutions
■ Service and Support Business				
Alpha Techno Co., LTD.	1996	50	100.0%	• Emergency repair of PCs and peripheral equipment, disposal and data recovery service
Alpha Net Co., LTD.	1997	400	100.0%	• Comprehensive service and support for network systems
■ Other Business				
Fujimi Construction Co., LTD.	1964	99	100.0%	• Construction, building maintenance and management
Otsuka Auto Service Co., LTD.	1987	50	100.0%	• Sale, maintenance and body work for automobiles, and commissioned sales of insurance
Otsuka Business Service Co., LTD.	1992	50	65.0%	• Creation and commissioned shipment of direct mail materials, data management and processing as well as commissioned creation of Websites

Corporate Data (as of December 31, 2004)

Name	OTSUKA CORPORATION
Founded	July 17, 1961 (registered as joint-stock company on December 13, 1961)
Paid-in Capital	¥10,374,851,000
Number of Employees	6,294 (including consolidated subsidiaries: 7,625)
Business	<p>System Integration Business :</p> <p>Sales of computers, copiers, communication equipment and software, and software development of consigned software, other activities</p> <p>Service and Support Business :</p> <p>Supplies, maintenance, and educational support, other activities</p>
Main Banks	<p>The Bank of Yokohama, Ltd.</p> <p>The Bank of Tokyo-Mitsubishi, Ltd.</p> <p>Mizuho Bank, Ltd.</p> <p>UFJ Bank Limited</p>

Base (as of December 31, 2004)

Head Office	2-18-4 Iidabashi, Chiyoda-ku, Tokyo, 102-8573 TEL 03-3264-7111		
Branch Offices	<p>Metropolitan Office</p> <p>2-18-4 Iidabashi, Chiyoda-ku, Tokyo, 102-8573 TEL 03-3264-7111</p> <p>Kansai Office</p> <p>6-14-1 Fukushima, Fukushima-ku, Osaka-shi, Osaka, 553-8558 TEL 06-6456-2711</p> <p>Chubu Office</p> <p>3-5-33 Masaki, Naka-ku, Nagoya-shi, Aichi, 460-0024 TEL 052-350-4811</p>		
Local Area Sales Groups	Chuo Sales Group 1	Chuo Sales Group 2	Josai Sales Group
	Johoku Sales Group	Tama Sales Group	Keiyo Sales Group
	Kanagawa Sales Group	Saitama Sales Group	Osaka Northern Sales Group
	Osaka Southern Sales Group		
Regional Offices	Sapporo Branch	Sendai Branch	Utsunomiya Branch
	Nagoya Branch	Mikawa Branch	Kyoto Branch
	Kobe Branch	Hiroshima Branch	Fukuoka Branch

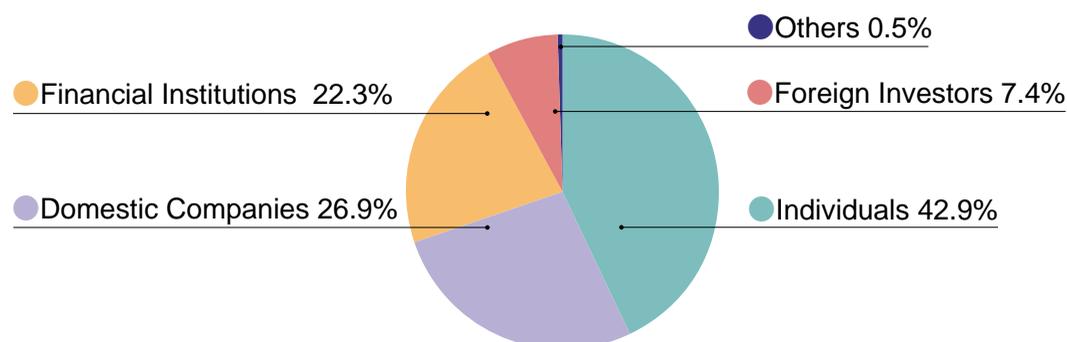
Stock Information (as of December 31, 2004)

Authorized Common Stock	112,860,000 shares
Issued Common Stock	31,667,020 shares
Number of Shares of Unit Stock	100 shares
Number of Shareholders	8,491

Major Shareholders

Name	Investment in OTSUKA CORPORATION		Investment in Major Shareholders by OTSUKA CORPORATION	
	Number of Shares Held	Voting right ratio (%)	Number of Shares Held	Voting right ratio (%)
Otsuka Sobi Co., Ltd.	8,112,730	25.67	—	—
Yuji Otsuka	2,622,580	8.29	—	—
Japan Trustee Services Bank, Ltd.(Trust Account)	2,413,400	7.63	—	—
Minoru Otsuka	1,895,490	5.99	—	—
OTSUKA CORPORATION Employee Stock-Sharing Plan	1,695,720	5.36	—	—
The Master Trust Bank of Japan, Ltd.(Trust Account)	1,373,100	4.34	—	—
Atsushi Otsuka	1,255,550	3.97	—	—
Terue Otsuka	645,500	2.04	—	—
Trustee of Individually Operated Designated Money Trusts(Shiteitan)Mitsui Asset Trust and Banking Company, Limited(Account 1)	589,600	1.86	—	—
Trust & Custody Services Bank, Ltd.(Trust Account B)	316,500	1.00	—	—

Breakdown of Shareholders (Based on total shares)



OTSUKA CORPORATION WEBSITE
<http://www.otsuka-shokai.co.jp>

Otsuka Corporation

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