

The background of the cover is a vibrant yellow, featuring a central bright light source from which numerous thin, white rays radiate outwards. Scattered throughout the scene are several 3D-rendered yellow spheres of varying sizes, some appearing to float in the foreground and others further away, creating a sense of depth and movement.

# **ANNUAL REPORT 2008**

For the fiscal year ended December 31, 2008

***Otsuka Corporation***

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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 in the economic situation in principal markets and in product demand, and changes in various domestic and international regulations, accounting standards and customary business practices.

# Consolidated Financial Highlights

OTSUKA CORPORATION and Consolidated Subsidiaries Years ended December 31, 2006, 2007 and 2008			Millions of yen	Thousands of U.S. dollars	%
	2006	2007	2008	2008	Change
Net sales	¥433,617	¥469,481	<b>¥467,154</b>	<b>\$5,133,002</b>	-0.5
System Integration business	263,425	279,753	<b>266,476</b>	<b>2,927,996</b>	-4.7
Service and Support business	168,701	187,358	<b>198,761</b>	<b>2,183,950</b>	+6.1
Other business	1,490	2,370	<b>1,916</b>	<b>21,055</b>	-19.2
Operating income	26,158	30,051	<b>27,089</b>	<b>297,657</b>	-9.9
Recurring profit	26,494	30,520	<b>27,628</b>	<b>303,576</b>	-9.5
Income before income taxes and minority interests	26,350	33,597	<b>25,934</b>	<b>284,964</b>	-22.8
Net income	15,621	18,856	<b>14,371</b>	<b>157,910</b>	-23.8
Total assets	189,357	200,383	<b>196,946</b>	<b>2,164,006</b>	-1.7
Interest-bearing debt	10,854	10,051	<b>9,630</b>	<b>105,812</b>	-4.2
Equity	72,848	87,259	<b>96,876</b>	<b>1,064,458</b>	+11.0
Net income per share (EPS) (Yen and U.S. dollars)	494.30	596.69	<b>454.76</b>	<b>5.00</b>	-23.8
Dividends per share of common stock (Yen and U.S. dollars)	115.00	130.00	<b>130.00</b>	<b>1.43</b>	—
Cash flows from operating activities per share (Yen and U.S. dollars)	440.14	527.02	<b>422.35</b>	<b>4.64</b>	-19.9
Operating income to Net sales ratio (%)	6.03	6.40	<b>5.80</b>	—	
Net income to Net sales ratio (%)	3.60	4.02	<b>3.08</b>	—	
Interest-bearing debt ratio (%)	5.73	5.02	<b>4.89</b>	—	
Equity ratio (%)	38.47	43.55	<b>49.19</b>	—	
Return on equity (ROE) (%)	23.71	23.55	<b>15.61</b>	—	

Note:

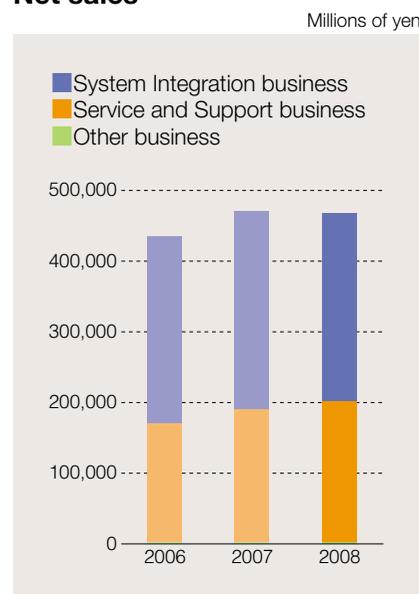
Equity = Total net assets - Share subscription rights - Minority interests

Figures for ROE are calculated using average equity.

U.S. dollar amounts are computed using the December 31, 2008 exchange rate of ¥91.01 = US\$1.

The dividends for 2006 include a ¥10 special dividend commemorating the 45th anniversary of the Company.

## Net sales



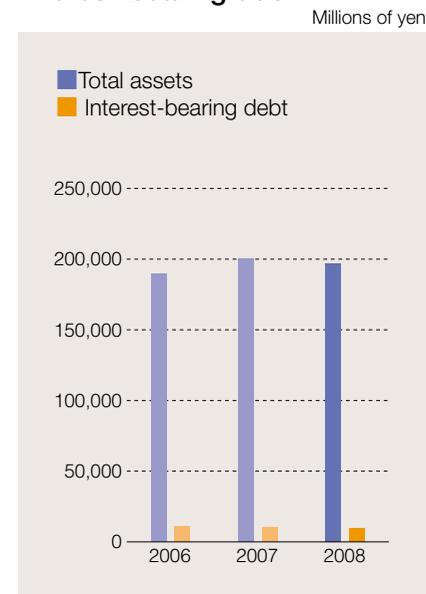
Note:

Sums of less than a million yen are rounded down.

## Operating income, Recurring profit, Net income



## Total assets, Interest-bearing debt



## To Our Shareholders and Investors



I am pleased to announce the results for the fiscal year ended December 31, 2008 and to thank our shareholders and investors for their loyal support.

During the fiscal year under review, global financial uncertainties from autumn led to a rapid worsening of the economy, creating a harsh economic environment. Although the OTSUKA Group made various proposals for achieving cost reductions and raising productivity, net sales declined 0.5% from the previous fiscal year to ¥467,154 million, reflecting the growing trend among companies to curb IT investments.

At the earnings level, the decrease in net sales, coupled with an increase in selling, general and administration (SG&A) expenses, resulted in lower profits, as operating income declined 9.9% to ¥27,089 million, recurring profit decreased 9.5% to ¥27,628 million and net income was down 23.8% to ¥14,371 million. The double-digit decline in net income was also due in part to the effect of an extraordinary gain on the transition of retirement benefit plan amounting to ¥4,298 million that was recorded in fiscal 2007.

Management has resolved to pay year-end dividends per share of ¥130 in line with our efforts to return profits to shareholders, who have given us their support.

In the coming fiscal year, although the severe environment is likely to persist, we will work to strengthen our ties with customers by offering proposals and support from a customer perspective. In working to realize our Mission Statement, the OTSUKA Group will continue to pursue management reforms to ensure the trust of all stakeholders. Your ongoing support is greatly appreciated as we move forward with these endeavors.

Yuji Otsuka, President & Chief Executive Officer

March 2009

# Overview of Consolidated Operations

## ■ Rapid Deterioration of Economy

During the first half of the fiscal year, the Japanese economy entered a recessionary phase owing to the effects of soaring crude oil and raw materials prices, a weak U.S. dollar and falling stock prices. In the second half, amid worldwide financial uncertainties and a credit crunch triggered by the bankruptcy of U.S.-based Lehman Brothers, overseas economies decelerated and large declines in exports and the sharp appreciation of the yen led to a worsening of corporate earnings, primarily in export-oriented industries. Moreover, corporate fund-raising became increasingly difficult, and bankruptcies of profit-making companies spread from the construction and real estate industries to a broad range of other industries. Reflecting these factors, the economy deteriorated rapidly and the management environment became exceedingly harsh.

Amid such circumstances, there was solid demand by companies for raising productivity and reducing costs by utilizing IT as well as stable latent demand for implementing information security countermeasures and renovating existing information system infrastructures. Nevertheless, the postponement of purchases due to the worsening economy was evident, while cut-backs in IT investments accelerated, particularly from the fourth quarter.

## ■ Promoting Combined System Proposals to Achieve Cost Reductions

Under our fiscal 2008 slogan, “Respond to customers’ trust from their viewpoint and make a leap forward together with customers,” the OTSUKA Group worked to raise levels of customer satisfaction and enhance operational efficiency by strengthening our community-based sales structure; bolstering functionality and making greater use of “SPR,” a proprietary, independently developed system by OTSUKA CORPORATION that combines the functions of customer relationship management (CRM) and sales force automation systems; and expanding the operations of the “Sales Support Center.” Additionally, the Group worked to strengthen our support structure and raise system development quality and productivity.

### External Environment

#### Drastic Change in Market Conditions from Autumn

**Entering a worldwide recession due to the financial crisis**

**The credit crunch and worsening of fund-raising environment**

**Sharp decline in stock markets**

**Steep appreciation of the yen**

**Increased sense of uncertainty about the future**

**Despite needs for IT utilization, investments in IT are being curtailed or postponed**

### OTSUKA Group’s Activities

- **Strengthening “community-based sales structure”**
- **Assessment of IT investment trends by size of each enterprise and promoting combined system proposals and comprehensive proposals**
- **Proposing specific cost reductions**
- **Enhancing efficiency of sales activities by reinforcing the functions of “SPR” and making full use of the “Sales Support Center”**
- **Strengthening accumulated business**

In carrying out activities for making proposals to customers, while closely focusing on the needs and IT investment trends by size of enterprise, we strived to help customers achieve cost reductions and productivity improvements by promoting combined system proposals and comprehensive proposals that integrate such products as copiers, computers, facsimiles, telephones and communications lines. We also continued to focus efforts on the “OSM” information security-related business, “ODS21” knowledge management system and “SMILE” integrated mission-critical systems, as well as on the “tanomail” office supply mail-order service and “tayoreru” IT and business support service.

- SPR:** OTSUKA CORPORATION’s proprietary Customer Relationship Management (CRM) and Sales Force Automation (SFA) system
- OSM:** Business brand in the information security-related business
- ODS21:** Knowledge management system that digitally captures paper-based information, bringing it under the same central management as other digital information, and in turn, facilitating the sharing and utilization of such information
- SMILE:** OTSUKA Group’s proprietary integrated mission-critical operational system
- “tanomail”:** Business brand of the office supply mail-order service
- “tayoreru”:** Business brand that supports customer information systems and customers’ overall corporate activities

## ■ Sales and Income Rise in the First Half But Decline for the Full Fiscal Year

As a result of the aforementioned circumstances, consolidated net sales declined 0.5% to ¥467,154 million, operating income fell 9.9% to ¥27,089 million, recurring profit decreased 9.5% to ¥27,628 million and net income declined 23.8% to ¥14,371 million. The double-digit decline in net income was also due in part to the effect of an extraordinary gain on the transition of a retirement benefit plan amounting to ¥4,298 million that was recorded in the previous fiscal year.

(Millions of yen)

	FY 2007	FY 2008	
	Amount	Amount	Change to Last Year
Net sales	469,481	<b>467,154</b>	<b>-0.5%</b>
Operating income	30,051	<b>27,089</b>	<b>-9.9%</b>
Recurring profit	30,520	<b>27,628</b>	<b>-9.5%</b>
Net income	18,856	<b>14,371</b>	<b>-23.8%</b>

## Overview of Business Segments

### ■ System Integration Business

#### — Impacted by Postponements of Purchases —

The System Integration business provides optimized system services ranging from consulting to system design and development, transport and installation work and network construction. During the fiscal year, we focused efforts on our information security-related business, color copiers and the knowledge management system and CAD systems. Nevertheless, postponements of purchases due to curtailments of IT investments led to a 4.7% decline in net sales to ¥266,476 million.

### ■ Service and Support Business

#### — Steady Growth Achieved —

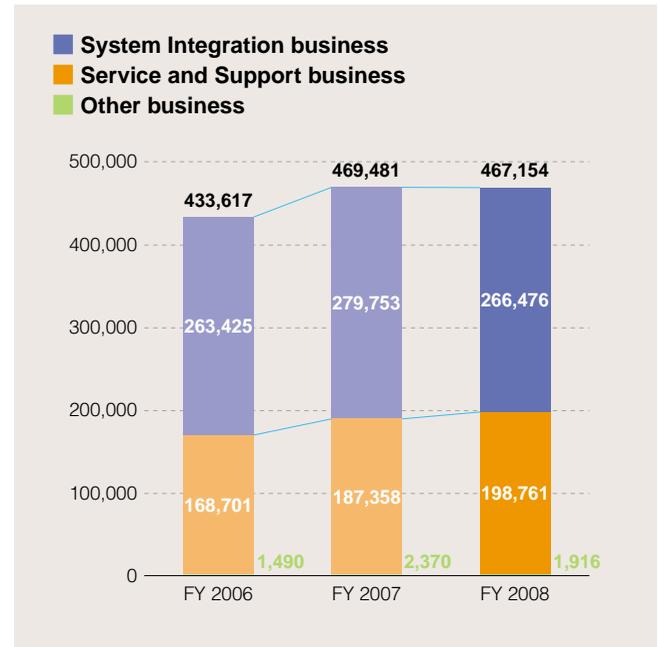
The Service and Support business provides customers with total support for their business operations and installed systems encompassing supplies, hardware and software maintenance, telephone support, IT education and outsourcing. We recorded steady growth in our “tanomail” office supply mail-order service via the Company’s Website and catalog channels, as well as in our “tayoreru” service that offers maintenance support to customers. As a result, net sales rose 6.1% from the previous year to ¥198,761 million.

### ■ Other Business

In the Other business, net sales declined 19.2% from the previous fiscal year to ¥1,916 million.

### Net Sales by Segments

(Millions of yen)



# Overview of Key Strategic Businesses (Non-consolidated)

<Amount>

(Millions of yen)

	FY 2006	FY 2007		FY 2008	
	Amount	Amount	Change to Last Year	Amount	Change to Last Year
MRO	75,306	86,270	+14.6%	<b>92,438</b>	<b>+7.1%</b>
(of which "tanomail")	71,088	82,493	+16.0%	<b>89,192</b>	<b>+8.1%</b>
SMILE (software)	7,150	6,938	-3.0%	<b>6,858</b>	<b>-1.1%</b>
ODS21	35,132	38,320	+9.1%	<b>37,650</b>	<b>-1.7%</b>
OSM	27,066	39,985	+47.7%	<b>43,448</b>	<b>+8.7%</b>

<Units>

(Units)

	Units	Units	Change to Last Year	Units	Change to Last Year
	Copiers	30,235	30,615	+1.3%	<b>29,288</b>
(of which color copiers)	18,584	20,413	+9.8%	<b>20,595</b>	<b>+0.9%</b>
Servers	40,862	35,741	-12.5%	<b>35,014</b>	<b>-2.0%</b>
Personal computers	547,061	481,502	-12.0%	<b>508,967</b>	<b>+5.7%</b>

Key strategic businesses were generally impacted by overall curtailments in IT investments and reductions in expenses, whereby growth rates slackened and fell below levels recorded in the previous fiscal year. Among key strategic businesses, the MRO business, centered on the "tanomail" office supply mail-order service business, recorded steady growth, while the personal computers business staged a recovery.

# Focusing Efforts on the Accumulated Business

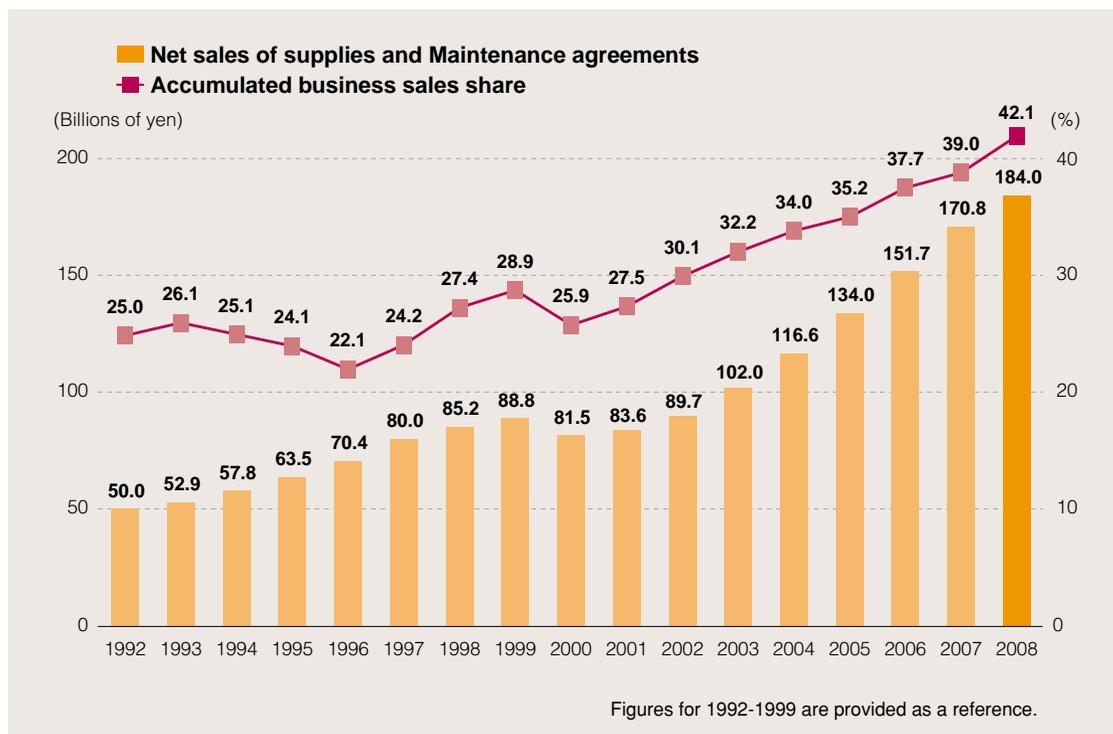
OTSUKA CORPORATION places special emphasis on office supply and maintenance agreement services as the “accumulated business” within the Service and Support business.

The accumulated business is not easily impacted by fluctuations in the economy and is steadily achieving growth annually. As such, this can be said to be a cumulative or accumulation business.

In fiscal 2008, the accumulated business (non-consolidated basis) accounted for more than 40% of net sales, owing in part to a 4.9% decline (non-consolidated basis) in the System Integration business.

OTSUKA CORPORATION will continue to focus on the accumulated business as it works to raise the stability of its operations.

## ■ Accumulated Business (Non-consolidated)



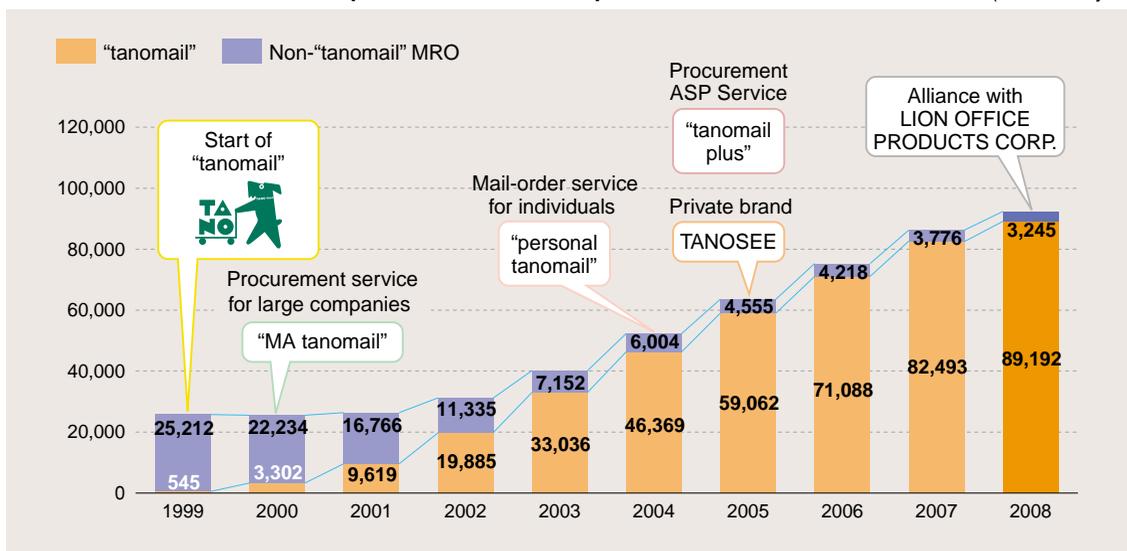
“tanomail” and “tayoreru” are the core pillars of the accumulated business.

# たのめーる “tanomail”

Although growth rates are slowing, our MRO business, centered on the “tanomail” office supply mail-order service business, is steadily expanding, and net sales surpassed ¥90 billion in fiscal 2008.

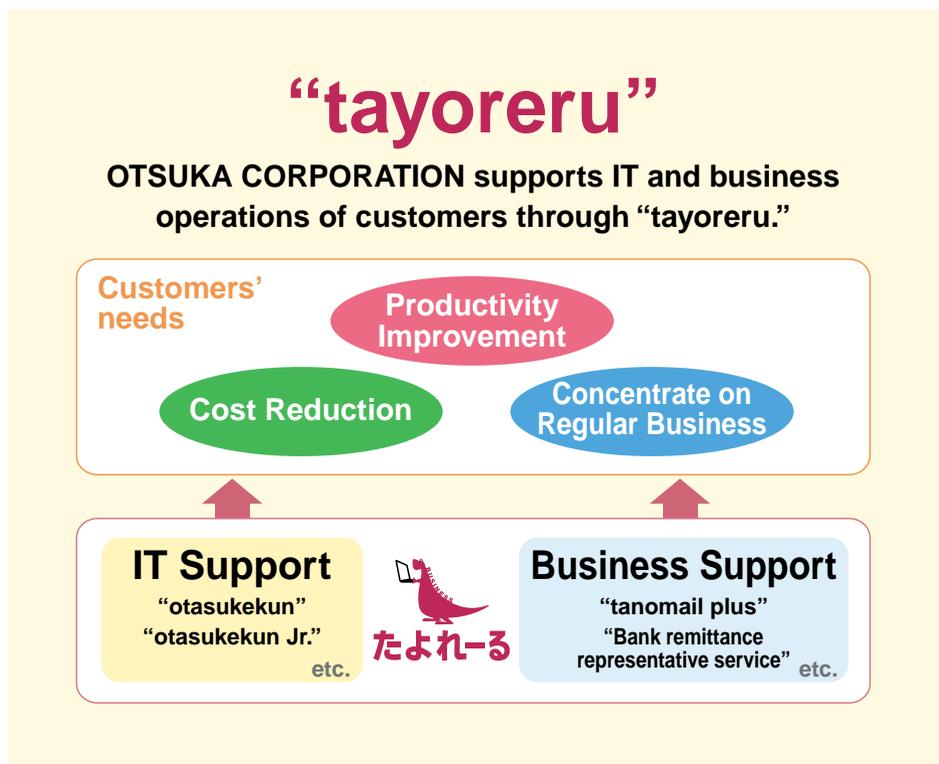
Trends in MRO Business (Non-consolidated)

(Millions of yen)



# たよれーる “tayoreru”

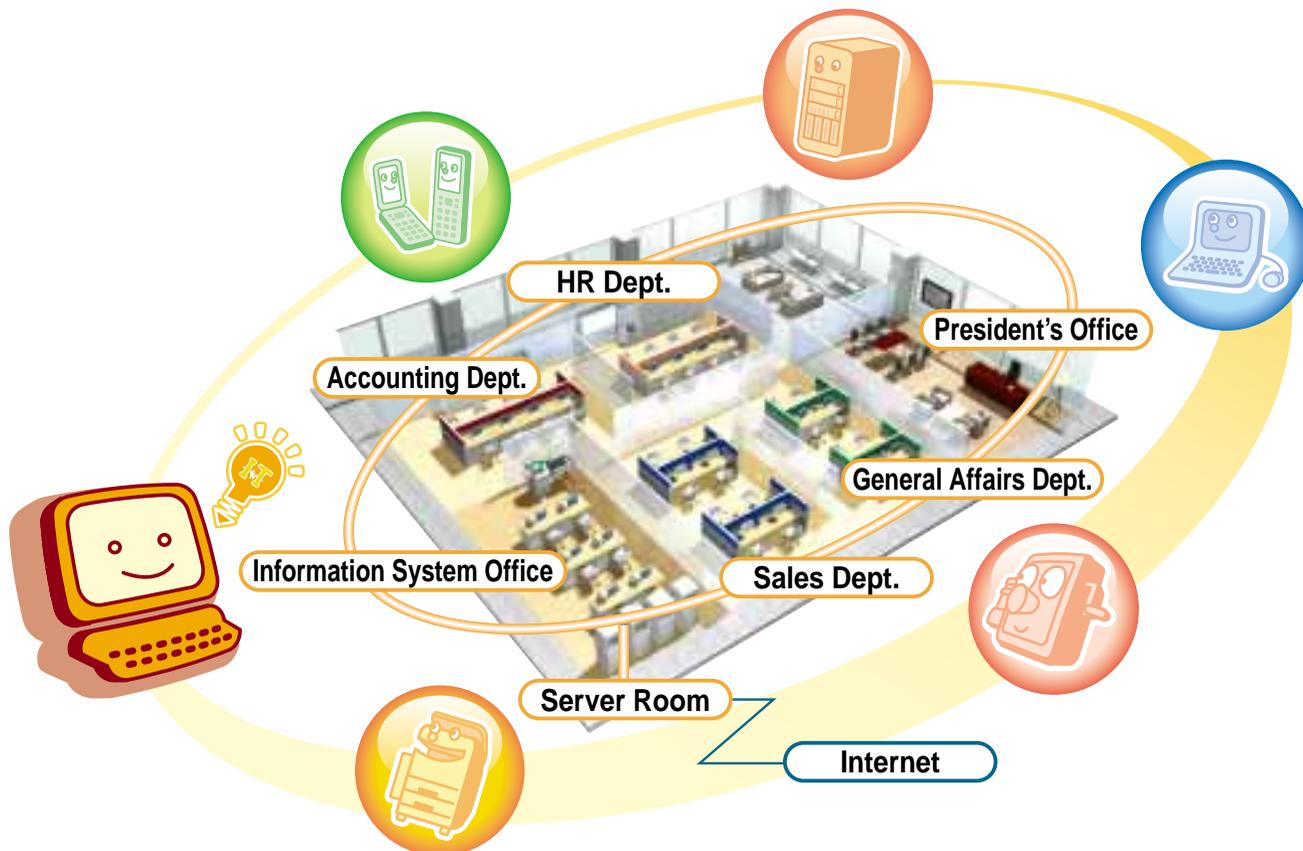
Supporting customer information systems and corporate activities, “tayoreru” service supports customers’ IT and business operations.  
OTSUKA CORPORATION aims to be an indispensable presence in customers’ business infrastructure.



# OTSUKA CORPORATION— A Partner to Our Customers

OTSUKA CORPORATION offers one-stop solutions and even one-stop support that integrates the various kinds of business equipment, information and telecommunication devices essential to corporate offices.

OTSUKA CORPORATION aims to be a partner that grows together with our customers.

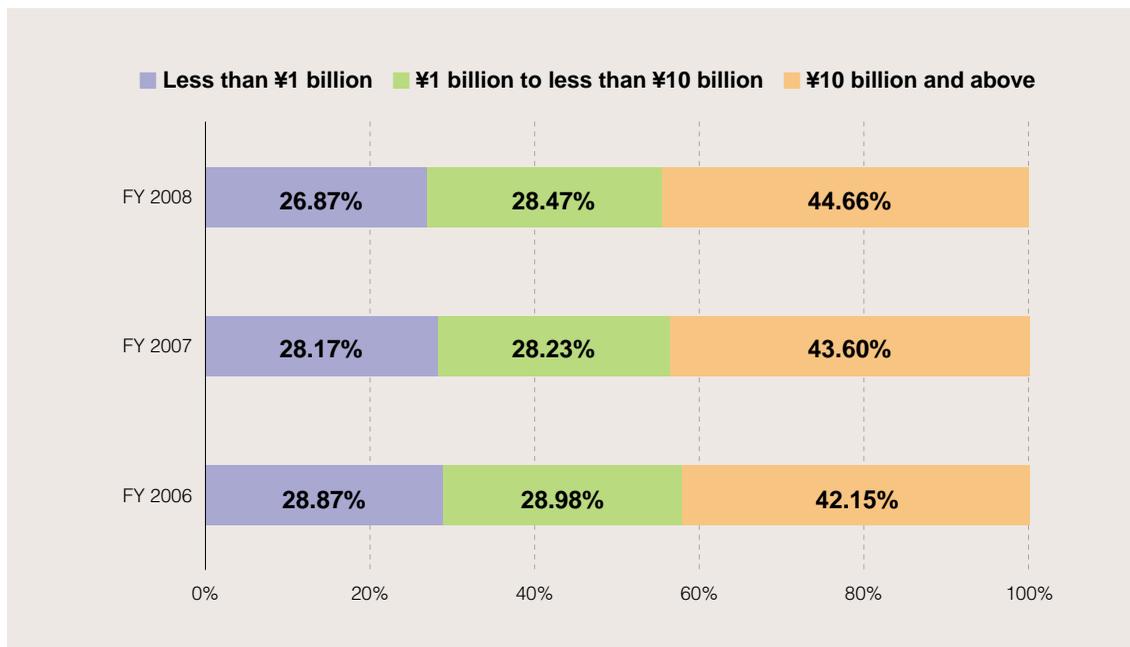


# OTSUKA CORPORATION—Backed by a Diverse Range of Customers

OTSUKA CORPORATION maintains a well-balanced customer base, with the corporate scale of the Company's customers ranging from major enterprises to small- and medium-sized firms.

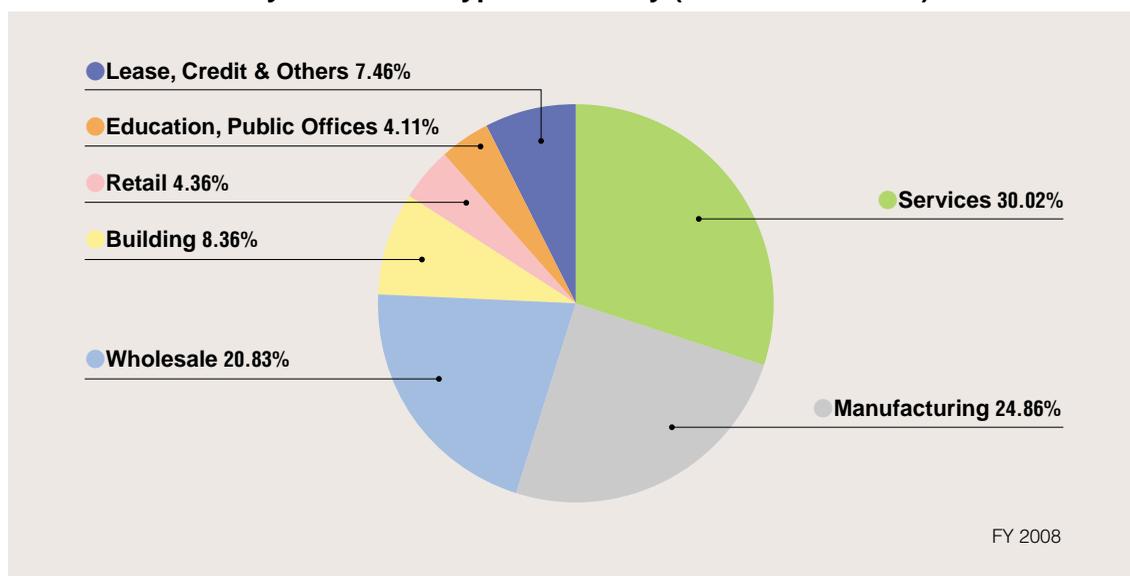
In terms of annual net sales, in fiscal 2008 the percentage of companies with annual net sales of ¥1 billion and above increased. Of particular note, the percentage of companies with sales of ¥10 billion and above exceeded 44%.

## Net sales structure on Customers' total annual business scale (Non-consolidated)



We also have a well-balanced customer base that is not skewed toward any particular industry. In fiscal 2008, there was no major change in the sales breakdown of customers by type of industry.

## Sales Breakdown by Customers' type of Industry (Non-consolidated)



# Outlook for Fiscal 2009

## ■ Utilization of IT Essential

Looking ahead, despite such underlying support factors as a decline in raw materials prices, it is believed that the economy could worsen due to slumping domestic and overseas demand, the appreciation of the yen and a decrease in capital investment, as well as owing to the impact of concerns about an escalation of the global financial crisis and a further downturn in the world economy.

Under these conditions, there is a strong need for utilizing IT to reduce costs and raise productivity. This is accompanied by solid demand for upgrading information system infrastructures as well as strategic IT investments being made by companies to ensure their survival. Nonetheless, companies are expected to continue restraining IT investments.

Within such an environment, the OTSUKA Group has formulated the corporate slogan “Vitalize office via IT and live up to customers’ trust” for fiscal 2009. Accordingly, in undertaking customer proposal activities, we will utilize such support measures as Tax incentive to help strengthen information infrastructure for business while proactively proposing systems suited to the particular circumstances and needs of each customer. Moreover, we will bolster our community-based sales structure and support structure, further bolster functionality and make greater use of “SPR,” as well as improve our one-stop response capabilities and work together with customers in finding solutions to challenges and tasks. In addition, we have positioned our “tanomail” office supply mail-order service business as a key strategic business and will undertake efforts to cultivate new customers.

By business segment, in the System Integration business the OTSUKA Group will continue to focus on the information security-related business, “SMILE” integrated mission-critical operational system, “ODS21” knowledge management system and CAD systems. Concurrently, we will progress with combined system proposals and comprehensive proposals that utilize the OTSUKA Group’s strengths, while responding to demand for the upgrading of information system infrastructures.

In the Service and Support business, the OTSUKA Group

will strive to further expand its “tanomail” office supply mail-order service business by expanding sales of LED lighting, which are new products, as well as bolster our business alliances and fortify our lineup of TANOSEE private brand products.

In our “tayoreru” support services, we will upgrade our lineup of services and strengthen our support structure. By implementing these measures, we aim to steadily increase the proportion of sales generated by such accumulated businesses as supplies and maintenance agreement services, which are expected to generate stable earnings in the future.

## Basic Principle and Medium-term Plan

### Basic principle

- Grow with customers through realization of the Mission Statement

### Medium-term plan

- Workforce basically remains flat
- Strive to expand business by increasing revenues and profits  
Target operating income and recurring profit to net sales ratio of 7%
- Spur new demand with the help of customer information
- Effective use of individuals/materials/capital and increasing productivity

## ■ Specific Policies

Our slogan for fiscal 2009 is:

“Vitalize office via IT and live up to customers’ trust”

Specific Policies

### 1. Maintain business and deepen ties with existing customers

OTSUKA CORPORATION has 770,000 customers that range in size from very large enterprises to small and medium-sized firms. We will work to strengthen our relationships with respective entities while expanding the range and volume of items handled.

### 2. Reinforce community-based sales structure

We will fortify frontline sales and further raise the level of contact with customers.

### 3. Strengthen accumulated business

We will further promote the acquisition of customers through “tanomail,” and by upgrading our lineup of “tayoreru” support services, we will also provide one-stop support for customers’ IT and business operations.

## ■ Forecast for Fiscal 2009

In fiscal 2009, in view of the expected ongoing harsh economic environment, the Company forecasts a 4.3% decrease in consolidated net sales to ¥447,000 million, a 31.7% decline in operating income to ¥18,500 million, a 31.2% decrease in recurring profit to ¥19,000 million and a 35.6% fall in net income to ¥9,260 million.

By segment, we forecast a 10.6% decline in net sales to ¥238,300 million in the System Integration business, a 4.0% increase to ¥206,710 million in the Service and Support business and a 3.8% rise to ¥1,990 million in the Other business.

### Forecast for Consolidated Net Sales and Income (Millions of yen)

	Fiscal 2008	Fiscal 2009 (Forecast)	
	Amount	Amount	Change to Last Year
Net sales	467,154	<b>447,000</b>	<b>-4.3%</b>
Operating income	27,089	<b>18,500</b>	<b>-31.7%</b>
Recurring profit	27,628	<b>19,000</b>	<b>-31.2%</b>
Net income	14,371	<b>9,260</b>	<b>-35.6%</b>

### Forecast for Consolidated Net Sales by Segment (Millions of yen)

	Fiscal 2008	Fiscal 2009 (Forecast)	
	Amount	Amount	Change to Last Year
System Integration business	266,476	<b>238,300</b>	<b>-10.6%</b>
Service and Support business	198,761	<b>206,710</b>	<b>+4.0%</b>
Other business	1,916	<b>1,990</b>	<b>+3.8%</b>

## Topics

### ■ Business and Capital Alliance Established with LION OFFICE PRODUCTS CORP.

OTSUKA CORPORATION has formed a business and capital alliance with LION OFFICE PRODUCTS CORP., a long-established stationery and office equipment company. Looking ahead, we plan to promote collaboration in numerous areas that include supplying office furniture and office design services through the “tanomail” office supply mail-order service.



### ■ Participation in “Nikkei IR Fair 2008”

On August 22 and 23, 2008, we participated in “Nikkei IR Fair 2008” (hosted by Nikkei Inc.) held at Tokyo Big Sight. At the fair, numerous individual investors visited the OTSUKA CORPORATION booth, and we held direct investors relations (IR) meetings with more than 100 people.



### ■ Participation in Electronic Voting Platform for Institutional Investors

OTSUKA CORPORATION is participating in the Electronic Voting Platform for institutional investors being promoted by the Tokyo Stock Exchange and operated by Investor Communications Japan (ICJ), Inc. (Our participation will begin from the Annual General Meeting of Shareholders, which will convene in March 2009.) By participating in this platform, we have proceeded with creating an environment that makes it easy for institutional investors, including foreign investors, to exercise their voting rights.

# Social Contribution and Environmental Preservation Activities

Starting from our immediate surroundings, OTSUKA CORPORATION is participating in activities for contributing to society and helping to preserve the environment in a diverse range of fields. Some of the highlights for fiscal 2008 are introduced herein.

## ■ Registering as a Japanese Red Cross Society “Blood Donation Supporter”

For many years, OTSUKA CORPORATION has invited staff of the Japanese Red Cross Society to its head office and other main business offices for in-house blood drives. With the aim of contributing to further awareness about and spread of blood donation activities, we filed an application for becoming a “Blood Donation Supporter” and subsequently received approval from the Japanese Red Cross Society.



## ■ OTSUKA CORPORATION CSR Report 2008

We have published our CSR Report 2008. Besides introducing our social contribution and environmental preservation activities, this report explains our relationship with various stakeholders including customers, shareholders, investors, business partners, local communities and employees. In creating our CSR Report, we make every effort to conserve paper resources by posting this report on our Website rather than printing copies.



<http://www.otsuka-shokai.co.jp/corporate/csr/report/2008/>

## ■ Participation in the Green IT Promotion Council

The Ministry of Economy, Trade, and Industry (METI) is advocating the “Green IT Initiative,” as a means of achieving a balance between environmental protection and economic growth. In promoting this initiative, the Green IT Promotion Council is carrying out activities under the “Green IT Initiative” to realize “IT Energy Conservation” and “Energy Conservation through IT.” We participated in the Green IT Promotion Council.



グリーンIT推進協議会  
Green IT Promotion Council

## ■ Environmental Solutions

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

We offer customers “offices that are friendly to the global environment and beneficial for business.”

<http://www.otsuka-shokai.co.jp/products/greenit/>

### 8 Benefits of Green IT

Reduction in materials consumption

Reduction in consumption of electric power and energy

Reduction in movements of people

Reduction in movements of materials

Enhanced efficiency of office space

Reduction in materials storage

Enhanced efficiency of business operations

Reduction in waste materials

# Corporate Governance

## ■ Basic Stance Regarding Corporate Governance

Based on a corporate ethic and spirit of compliance spelled out in its Mission Statement, the OTSUKA Group aims to adapt nimbly to changes in the environment and augment its competitiveness by ensuring thorough compliance and raising both operational transparency and fairness.

## ■ Current Status of Implementation of Corporate Governance Measures

As a company with a Corporate Auditors system, OTSUKA CORPORATION aims to augment corporate governance by further enhancing the General Shareholders Meeting, augmenting the auditing capabilities of Corporate Auditors, reforming the Board of Directors and making an active and ongoing commitment to disclosure and investor relations (IR) activities.

### 1. Enhancement of the General Shareholders Meeting

The OTSUKA Group believes that enhancement of the General Shareholders Meeting is crucial to improving corporate governance, and is working to ensure that as many shareholders as possible attend meetings, while concurrently introducing an electronic voting system that will allow shareholders to exercise their voting rights via the Internet.

### 2. Board of Directors

As of December 31, 2008, the Board of Directors consisted of 15 Directors, of which 13 board members concurrently serve as Executive Officers responsible for making decisions and overseeing business operations based on actual on-site conditions. There are no outside directors at present.

The Board of Directors meets regularly once a month to discuss critical management issues as well as to deliberate on progress regarding businesses performance and make swift decisions toward resolving relevant issues. Group Management Meetings comprising top management of all Group companies are also held to clarify operational conditions at each company and make progress in achieving profitability in addition to working to strengthen corporate governance.

As of March 27, 2009, there were 12 Directors.

### 3. Executive Officer System

OTSUKA CORPORATION introduced the Executive Officer System on July 1, 2003, and has since been working to realize more rapid decision-making in regard to management policies and execution of business operations as well as to strengthen the oversight structure for more efficient business operations. Consequently, the Board of Directors handles overall decision-making for important management matters as well as supervisory functions pertaining to business operations. Executive Officers elected by the Board of Directors are responsible for execution of business operations as decided by the Board of Directors and under the direction of the President. As of December 31, 2008, there were 31 Executive Officers, (13 of whom are Directors).

As of March 27, 2009, there were 32 Executive Officers (11 of whom are Directors).

### 4. Corporate Auditors System

OTSUKA CORPORATION uses a Corporate Auditors system. The Board of Corporate Auditors is comprised of four auditors that include two outside auditors, all of whom attend such important meetings as Board of Directors meetings and management meetings to monitor that the management of operations is being properly carried out. The Corporate Auditors reinforce auditing at the operational level through such means as identifying potential problems at an early stage by regularly engaging in dialogue with management via the Board of Corporate Auditors along with independent auditors, as well as by collaborating and coordinating with internal departments conducting auditing of subsidiaries and affiliates.

No personal, capital or business interests exist between outside auditors and OTSUKA CORPORATION.

## 5. Corporate Audits

- Independent Auditor

Ernst & Young ShinNihon LLC

On July 1, 2008 Ernst & Young ShinNihon transitioned to a limited liability company structure. Accordingly, Ernst & Young ShinNihon LLC has become the Company's independent auditor.

There are no interests among Ernst & Young ShinNihon LLC, Managing Partners responsible for auditing the Company and OTSUKA CORPORATION.

The names of CPAs involved in auditing-related operations and composition of staff assisting in auditing-related operations for the fiscal year under review are as follows.

Ernst & Young ShinNihon LLC

Kenichi Akiyama, Designated Employee with Limited Liability and Managing Partner

Juntaka Sakai, Designated Employee with Limited Liability and Managing Partner

Makoto Mukai, Designated Employee with Limited Liability and Managing Partner

Number of Staff Assisting in Accounting-related Operations

CPAs 6

Assistant CPAs 2

Other individuals 11

\*Summarized, as all members have less than seven years of continuous auditing experience

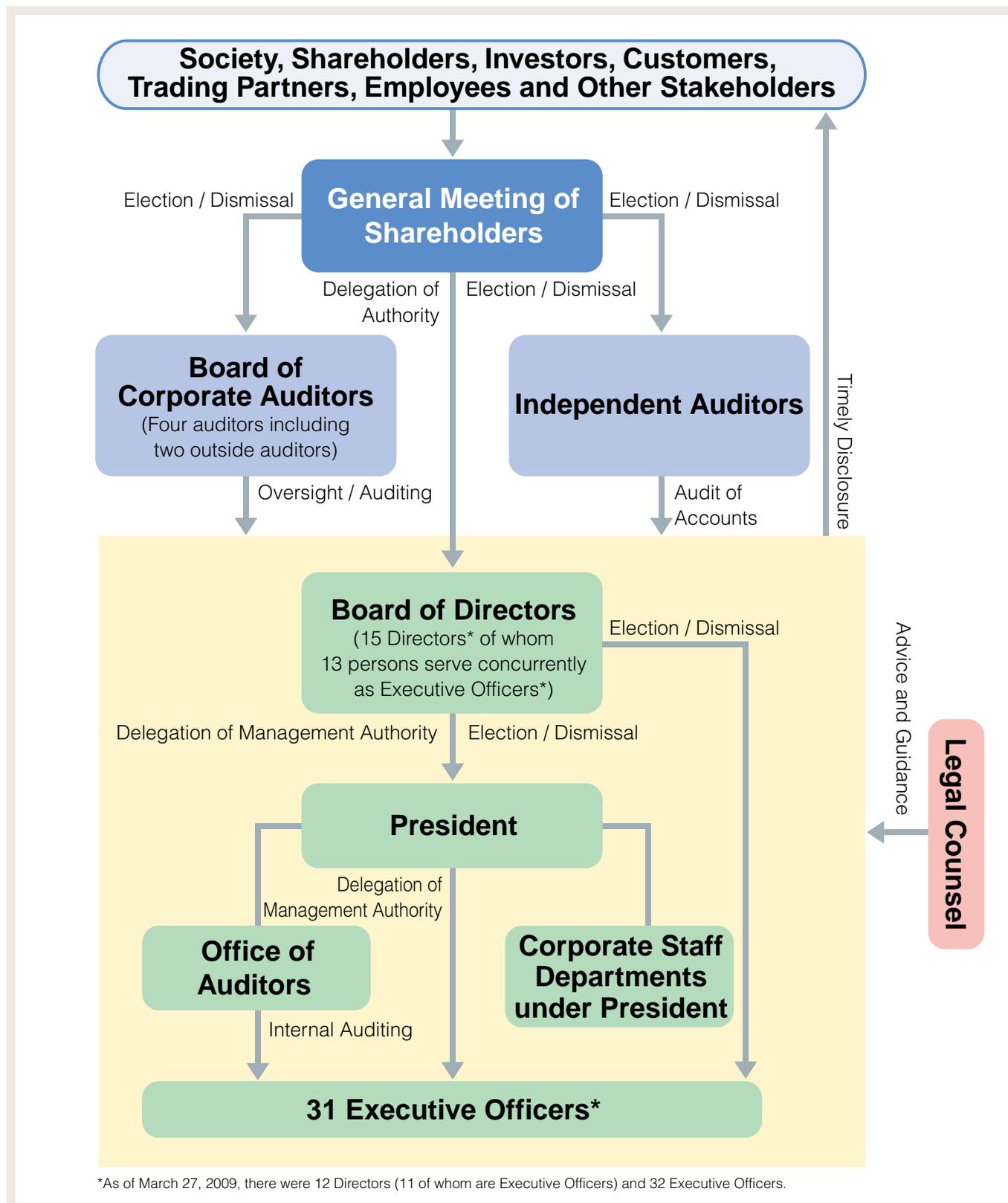
## 6. Status of Monitoring Operations

Critical items that impact operations and performance are reported immediately to the Board of Directors and the Board of Corporate Auditors as they arise. Moreover, the Office of Auditors under the direction of the President has been established to conduct periodic and on-demand internal audits of all operations and assess the adequacy of policies, plans and procedures, the effectiveness of their implementation in operations and progress in compliance, as well as to offer concrete advice and recommendations for improving operations and raising awareness. The Office of Auditors has 14 staff as of December 31, 2008.

OTSUKA CORPORATION has established and operates an Internal Reporting and Improvement Proposal System that allows employees to directly report and propose improvements to the President. The purpose of the system is as follows:

- To quickly identify, address and prevent occurrences pertaining to dishonesty and misconduct in relation to corporate ethics and fair trade
- To assess, suitably handle and prevent such incidences as abuse of authority and sexual harassment
- To receive proposals and consultation, as well as to individually address issues related to business operations and work flows

As of December 31, 2008, the structure for corporate management decision-making, business operations and oversight is as follows:



## ■ The following measures were implemented recently to strengthen corporate governance.

(As of March 2009)

### 1. Participation in Electronic Voting Platform for institutional investors

Beginning from the Annual General Meeting of Shareholders convened in March 2009, OTSUKA CORPORATION is participating in the Electronic Voting Platform for institutional investors operated by Investor Communications Japan (ICJ), Inc. By participating in this platform, we have progressed with the creation of an environment that makes it easy for institutional investors, including foreign investors, to exercise their voting rights.

## ■ Remuneration for Board Members and Auditors

1) Remuneration for Directors and Corporate Auditors in the current fiscal year is as follows.

Directors 15 ¥425 million

Auditors 4 ¥30 million (two of which are outside auditors, ¥8 million)

Notes:

1. Remuneration to Directors does not include compensation for services rendered outside the realm of their directorships.
2. The amount of annual remuneration for Directors is up to ¥650 million as approved at the General Meeting of Shareholders on March 13, 1990 (although this does not include employee compensation).
3. The amount of annual remuneration for auditors is up to ¥50 million as approved at the General Meeting of Shareholders on March 30, 2005.
4. The above remuneration includes the increased amount of retirement benefits for Directors in the current fiscal year.

2) Remuneration for Independent Auditors in the current fiscal year is as follows.

Independent Auditor Ernst & Young ShinNihon LLC

Remuneration for Auditing & Attestation ¥67 million

Remuneration for Other Services ¥10 million

## ■ Number of Directors

The Company's Articles of Incorporation as of December 31, 2008 stipulate that the number of Company Directors shall be 19 or fewer.

## ■ Requirements for Resolution of Director Appointments

The Company's Articles of Incorporation stipulate that a resolution for appointment of Director requires attendance by shareholders with more than one-third of the voting rights of shareholders capable of exercising such rights, and is decided by a majority of shareholders. In addition, a resolution for appointment of Director shall not be decided by cumulative voting.

## ■ Requirements for Special Resolution of the General Meeting of Shareholders

The Company's Articles of Incorporation stipulate that a special resolution of the General Meeting of Shareholders, pursuant to Article 309, Paragraph 2 of the Companies Act, shall be adopted when it is approved by a vote of two-thirds or more of the voting rights present at a General Meeting of Shareholders, a quorum for which shall be the presence of shareholders of one-third of the aggregate voting rights of the total shareholders capable of exercising such rights. This aims to facilitate efficient operation of the General Meeting of Shareholders through the moderation of special resolutions at the General Meeting of Shareholders.

## ■ Purchase of Own Shares

The Company's Articles of Incorporation stipulate that the Company shall be able to purchase its own shares through market transactions based on a resolution of the Board of Directors as prescribed under Article 165, Paragraph 2 of the Companies Act to enable the execution of a flexible capital policy that responds to changes in economic conditions.

## ■ Interim Dividends

The Company's Articles of Incorporation stipulate that based on a resolution of the Board of Directors, the Company can pay interim dividends with the date of record being June 30 of each year.

## Board of Directors and Corporate Auditors (As of March 27, 2009)



President & Chief Executive Officer

Yuji Otsuka



Managing Director & Senior Executive Operating Officer

Yoshiaki Nagashima



Managing Director & Senior Executive Operating Officer

Youichi Harada



Managing Director & Senior Executive Operating Officer

Kazuhide Hamada



Managing Director & Senior Executive Operating Officer

Kazuyuki Katakura



Managing Director & Executive Operating Officer

Katsuhiko Nakajima



Managing Director & Operating Officer

Toshiyasu Takahashi



Managing Director & Operating Officer

Kimio Shiokawa

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Director & Senior Managing Officers

Katsuhiro Yano

Koji Yama

Hironobu Saito

Yasuhiro Wakamatsu

Standing Auditor

Tatsuzo Yoshida

Auditors

Yuuichi Itou

Jiro Makino

Mikio Sugiyama

# Business Risks

The most common risks that could potentially impact the Group's business performance results and financial condition are outlined below. While these are the most common risks, they do not represent all potential risks.

The items covered herein are possible future occurrences determined by the OTSUKA Group as of March 27, 2009.

## ■ Customer-related Risks

The OTSUKA Group's customers range from large enterprises to small firms that span a broad range in terms of company scale and industries. Consequently, its level of dependency on any specific customer is low.

However, the Group's operations could be impacted by convergent changes in IT investment trends by a large number of companies as a result of unexpected changes in the economic environment.

## ■ Supplier-related Risks

The OTSUKA Group is supplied with high-quality products, services and technologies (hereafter called "products") by numerous suppliers for respective segments in order to optimally resolve the problems of each customer. While working to deepen its relationship with suppliers to ensure stable supply of these "products," the Group is constantly working to acquire information on newer "products" as well.

However, the Group's operations could be impacted by the inability to supply "products" in the quantity demanded by customers because of insufficient supply of "products" due to issues at supplier sites, as well as by the Group's inability to obtain substitutes.

## ■ Information Leakage Risks

The OTSUKA Group possesses an abundance of individual and corporate information pertaining to operations that is handled carefully.

The Group received approval to use the Privacy Mark of the Japan Information Processing Development Corporation, and its Internet Data Center acquired certification for Information Security Management Systems (ISMS).

As a concrete measure to manage data, the Group has released an internal and external Personal Information Protection Policy, as well as established regulations on personal information protection, confidentiality and information system security. The Group has its employees take a pledge of confidentiality as well as works to prevent information leakage outside of the Group and raises awareness of information management through its proprietary educational "CP (Compliance Program) License System" and other measures. Even with these measures, however, the Group's operations could be impacted by assuming liabilities for damage and loss of trust by society in the unlikely event that personal or corporate information is leaked outside the Group.

# Financial Section

## Three-year Financial Data

OTSUKA CORPORATION and Consolidated Subsidiaries  
Years ended December 31, 2006, 2007 and 2008

	Millions of yen			Thousands of U.S. dollars
	2006	2007	2008	2008
Net sales	¥433,617	¥469,481	<b>¥467,154</b>	<b>\$5,133,002</b>
System Integration business	263,425	279,753	<b>266,476</b>	<b>2,927,996</b>
Service and Support business	168,701	187,358	<b>198,761</b>	<b>2,183,950</b>
Other business	1,490	2,370	<b>1,916</b>	<b>21,055</b>
Operating income	26,158	30,051	<b>27,089</b>	<b>297,657</b>
Recurring profit	26,494	30,520	<b>27,628</b>	<b>303,576</b>
Income before income taxes and minority interests	26,350	33,597	<b>25,934</b>	<b>284,964</b>
Net income	15,621	18,856	<b>14,371</b>	<b>157,910</b>
Total assets	189,357	200,383	<b>196,946</b>	<b>2,164,006</b>
Interest-bearing debt	10,854	10,051	<b>9,630</b>	<b>105,812</b>
Equity	72,848	87,259	<b>96,876</b>	<b>1,064,458</b>
Net income per share (EPS) (Yen and U.S. dollars)	494.30	596.69	<b>454.76</b>	<b>5.00</b>
Dividends per share of common stock (Yen and U.S. dollars)	115.00	130.00	<b>130.00</b>	<b>1.43</b>
Cash flows from operating activities per share (Yen and U.S. dollars)	440.14	527.02	<b>422.35</b>	<b>4.64</b>
Operating income to Net sales ratio (%)	6.03	6.40	<b>5.80</b>	—
Net income to Net sales ratio (%)	3.60	4.02	<b>3.08</b>	—
Interest-bearing debt ratio (%)	5.73	5.02	<b>4.89</b>	—
Equity ratio (%)	38.47	43.55	<b>49.19</b>	—
Return on equity (ROE) (%)	23.71	23.55	<b>15.61</b>	—

Note:

Equity = Total net assets - Share subscription rights - Minority interests

Figures for ROE are calculated using average equity.

U.S. dollar amounts are computed using the December 31, 2008 exchange rate of ¥91.01 = US\$1.

The dividends for 2006 include a ¥10 special dividend commemorating the 45th anniversary of the Company.

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# Management's Analysis of Operating Results and Financial Position

## Summary of Sales and Profits

	2007	2008	Millions of yen	
			Difference to Last Year	% Change to Last Year
Net sales	¥469,481	<b>¥467,154</b>	-2,327	-0.5%
System Integration business	279,753	<b>266,476</b>	-13,276	-4.7
Service & Support business	187,358	<b>198,761</b>	+11,403	+6.1
Other business	2,370	<b>1,916</b>	-453	-19.2
Cost of sales	360,435	<b>359,754</b>	-681	-0.2
Gross profit	109,046	<b>107,399</b>	-1,646	-1.5
Selling, general and administrative expenses	78,994	<b>80,310</b>	+1,315	+1.7
Operating income	30,051	<b>27,089</b>	-2,961	-9.9
Recurring profit	30,520	<b>27,628</b>	-2,891	-9.5
Income before income taxes and minority interests	33,597	<b>25,934</b>	-7,662	-22.8
Income taxes				
Current	13,239	<b>11,212</b>	-2,027	-15.3
Deferred	1,253	<b>117</b>	-1,135	-90.6
Net income	18,856	<b>14,371</b>	-4,485	-23.8

### Sales Summary

In the fiscal year under review, the OTSUKA Group recorded consolidated net sales of ¥467,154 million, a decrease of ¥2,327 million (0.5%) from the previous fiscal year.

### System Integration Business

The System Integration business provides optimized system services ranging from consulting to system design and development, transport and installation work and network construction. During the fiscal year, we focused efforts on our information security-related business, color copiers and the knowledge management system and CAD systems. Nevertheless, postponements of purchases due to curtailments of IT investments led to a 4.7% decline in net sales to ¥266,476 million.

### Service and Support Business

The Service and Support business provides customers with total support for their business operations and installed systems encompassing supplies, hardware and software maintenance, telephone support, IT education and outsourcing. We recorded steady growth in our "tanomail" office supply mail-order service via the Company's Website and catalog channels, as well as in our "tayoreru" service that offers maintenance support to customers. As a result, net sales rose 6.1% from the previous year to ¥198,761 million.

### Other Business

In the Other business, net sales declined 19.2% from the previous fiscal year to ¥1,916 million.

### Summary of Income and Expenses

Gross profit declined 1.5% to ¥107,399 million, and the gross profit margin was 23.0%.

Operating income declined 9.9% to ¥27,089 million due in part to an increase in selling, general and administrative expenses.

Despite a rise in non-operating income resulting from a foreign exchange gains, recurring profit declined 9.5% from the previous fiscal year to ¥27,628 million.

Income before income taxes and minority interests declined 22.8% to ¥25,934 million due to such factors as a ¥1,736 million extraordinary losses that resulted from the disposal of fixed assets.

As a result, net income declined 23.8% to ¥14,371 million, and net income per share was ¥454.76.

## Financial Position

	Millions of yen			
	2007	2008	Difference to Last Year	% Change to Last Year
<b>Assets:</b>	¥200,383	<b>¥196,946</b>	-3,437	-1.7%
Current assets	130,353	<b>129,178</b>	-1,174	-0.9
Fixed assets	70,030	<b>67,767</b>	-2,262	-3.2
<b>Liabilities:</b>	112,382	<b>99,155</b>	-13,227	-11.8
Current liabilities	108,551	<b>95,880</b>	-12,671	-11.7
Fixed liabilities	3,831	<b>3,275</b>	-555	-14.5
<b>Net assets</b>	88,000	<b>97,790</b>	+9,789	+11.1

### Assets

Total assets at fiscal year-end decreased ¥3,437 million from the previous fiscal year-end to ¥196,946 million. Current assets declined ¥1,174 million to ¥129,178 million due to decreases in cash and time deposits and notes and accounts receivable. Fixed assets declined ¥2,262 million from the end of the previous fiscal year to ¥67,767 million.

### Liabilities

Total liabilities declined ¥13,227 million to ¥99,155 million. Current liabilities declined ¥12,671 million to ¥95,880 million due to a decrease in notes and accounts payable. Fixed liabilities decreased ¥555 million to ¥3,275 million owing to a decline in deferred tax liabilities non-current.

### Net Assets

Total net assets rose ¥9,789 million, to ¥97,790 million, owing to such factors as an increase in retained earnings. As a result, the equity ratio rose 5.7 percentage points to 49.2%.

The interest coverage ratio was 183.65 times; the interest-bearing debt ratio was 4.89%; return on equity (ROE) was 15.61%; and return on assets (ROA) was 13.78%.

	2007	2008
Interest coverage ratio (times)	217.30	<b>183.65</b>
Interest-bearing debt ratio (%)	5.02	<b>4.89</b>
ROE (%)	23.55	<b>15.61</b>
ROA (%)	15.51	<b>13.78</b>

Interest coverage ratio = Business profit / (Interest expenses + Interest payable on bonds)

ROA = Business profit / Total assets (average during the fiscal year)

Business profit = Operating income + Interest and dividend income + Equity in net income (loss) of unconsolidated subsidiaries and affiliates

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## Cash flows

	Millions of yen	
	2007	2008
Cash flows from operating activities	¥16,654	<b>¥13,347</b>
Cash flows from investing activities	-4,555	<b>-6,960</b>
Cash flows from financing activities	-4,271	<b>-4,591</b>
Cash and cash equivalents at end of year	25,374	<b>27,169</b>

Cash and cash equivalents at end of year totaled ¥27,169 million, an increase of ¥1,794 million (7.1%) from the end of the previous fiscal year. Factors relating to each cash flow category were as follows.

### Cash Flows from Operating Activities

Net cash provided by operating activities decreased ¥3,307 million (19.9%) to ¥13,347 million. This was due mainly to a decrease in income before income taxes and minority interests.

### Cash Flows from Investing Activities

Net cash used in investing activities increased ¥2,405 million (52.8%) to ¥6,960 million. This was due mainly to an increase in payments for the purchase of investments in securities.

### Cash Flows from Financing Activities

Net cash used in financing activities increased ¥319 million (7.5%) to ¥4,591 million. This is chiefly attributable to an increase in cash dividends paid.

As a result, free cash flows, the sum of cash flows from operating activities and cash flows from investing activities, decreased ¥5,713 million to ¥6,386 million.

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## Forecast

In fiscal 2009, in view of the expected ongoing harsh economic environment, the Company forecasts a 4.3% decrease in consolidated net sales to ¥447,000 million, a 31.7% decline in operating income to ¥18,500 million, a 31.2% decrease in recurring profit to ¥19,000 million and a 35.6% fall in net income to ¥9,260 million.

By segment, we forecast a 10.6% decline in net sales to ¥238,300 million in the System Integration business, a 4.0% increase to ¥206,710 million in the Service and Support business and a 3.8% rise to ¥1,990 million in the Other business.

## Consolidated Balance Sheets

OTSUKA CORPORATION and Consolidated Subsidiaries  
As of December 31, 2007 and 2008

Thousands of  
U.S. dollars  
(Note 3)

	Millions of yen		2008
	2007	2008	
<b>ASSETS</b>			
<b>Current assets</b>			
Cash, time deposits and other cash equivalents (Notes 10 and 15)	¥ 24,785	¥ 21,544	\$ 236,726
Accounts and notes receivable:			
Trade	75,773	71,056	780,754
Unconsolidated subsidiaries and affiliates	43	157	1,732
Other	5,130	6,737	74,031
	80,947	77,951	856,518
Less: Allowance for doubtful accounts	(247)	(271)	(2,982)
	80,699	77,680	853,535
Short-term investments (Notes 4 and 10)	—	4,996	54,903
Inventories (Note 6)	16,923	16,526	181,588
Deferred tax assets (Note 9)	2,586	2,341	25,722
Other current assets (Note 10)	5,357	6,089	66,908
<b>Total current assets</b>	<b>130,353</b>	<b>129,178</b>	<b>1,419,385</b>
<b>Investments and advances</b>			
Investments in securities (Note 4)	4,435	3,048	33,493
Investments in unconsolidated subsidiaries and affiliates	2,138	3,307	36,343
Guarantee deposits	2,824	3,285	36,102
Deferred tax assets non-current (Note 9)	1,613	1,360	14,943
Other investments	5,041	4,910	53,952
Less: Allowance for doubtful accounts	(824)	(932)	(10,245)
	15,228	14,979	164,591
<b>Property and equipment (Note 14)</b>			
Land	16,965	16,727	183,796
Buildings and structures	65,318	62,244	683,935
Other	13,203	13,708	150,627
	95,487	92,680	1,018,359
Less: Accumulated depreciation	(45,523)	(44,978)	(494,213)
<b>Net property and equipment</b>	<b>49,963</b>	<b>47,702</b>	<b>524,145</b>
<b>Intangibles and deferred charges</b>			
Software	4,659	4,922	54,082
Other	179	163	1,800
	4,838	5,085	55,883
<b>Total assets</b>	<b>¥200,383</b>	<b>¥196,946</b>	<b>\$2,164,006</b>

The accompanying notes are an integral part of these statements.

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2007	2008	2008
<b>LIABILITIES AND NET ASSETS</b>			
<b>Current liabilities</b>			
Short-term bank loans (Note 7)	¥ 7,300	¥ 9,500	\$ 104,384
Current maturities of long-term debts (Note 7)	2,621	40	439
Accounts and notes payable: (Note 15)			
Trade	59,425	53,629	589,275
Unconsolidated subsidiaries and affiliates	522	678	7,455
Other	15,178	13,400	147,246
	75,126	67,709	743,978
Income taxes payable (Note 9)	8,429	5,297	58,207
Other current liabilities	15,074	13,333	146,502
<b>Total current liabilities</b>	<b>108,551</b>	<b>95,880</b>	<b>1,053,511</b>
<b>Long-term liabilities</b>			
Long-term debt (Note 7)	130	90	988
Reserve for retirement benefits (Note 8)	1,820	2,044	22,461
Deferred tax liabilities non-current (Note 9)	1,442	671	7,374
Deferred tax liabilities on revaluation of land	216	216	2,383
Other long-term liabilities	221	253	2,785
<b>Total fixed liabilities</b>	<b>3,831</b>	<b>3,275</b>	<b>35,993</b>
<b>Net assets</b>			
<b>Shareholders' equity (Note 13)</b>			
Common stock:			
Authorized: 112,860,000 shares			
Outstanding: 31,667,020 shares as of December 31, 2007 and 2008	10,374	10,374	113,996
Capital surplus	16,254	16,254	178,603
Retained earnings	75,389	85,652	941,133
Treasury stock			
64,954 shares as of December 31, 2007 and			
65,342 shares as of December 31, 2008	(120)	(122)	(1,350)
<b>Total shareholders' equity</b>	<b>101,899</b>	<b>112,159</b>	<b>1,232,384</b>
<b>Valuation and translation adjustments</b>			
Unrealized gains on available-for-sale securities	982	429	4,714
Revaluation differences on land (Note 14)	(15,574)	(15,574)	(171,130)
Foreign currency translation adjustments	(47)	(137)	(1,510)
<b>Total valuation and translation adjustments</b>	<b>(14,639)</b>	<b>(15,282)</b>	<b>(167,926)</b>
<b>Minority interests in consolidated subsidiaries</b>			
	741	913	10,042
<b>Total net assets</b>	<b>88,000</b>	<b>97,790</b>	<b>1,074,500</b>
<b>Total liabilities and net assets</b>	<b>¥200,383</b>	<b>¥196,946</b>	<b>\$2,164,006</b>

The accompanying notes are an integral part of these statements.

# Consolidated Statements of Income

OTSUKA CORPORATION and Consolidated Subsidiaries  
For the years ended December 31, 2007 and 2008

Thousands of  
U.S. dollars  
(Note 3)

	Millions of yen		2008
	2007	2008	
<b>Net sales</b> (Note 17)	¥469,481	<b>¥467,154</b>	<b>\$5,133,002</b>
<b>Cost of sales</b> (Notes 16 and 17)	360,435	<b>359,754</b>	<b>3,952,912</b>
Gross profit	109,046	<b>107,399</b>	<b>1,180,089</b>
<b>Selling, general and administrative expenses</b> (Notes 16 and 17)	78,994	<b>80,310</b>	<b>882,432</b>
Operating income	30,051	<b>27,089</b>	<b>297,657</b>
<b>Other income (expenses)</b>			
Interest and dividend income	137	<b>173</b>	<b>1,908</b>
Interest expenses	(138)	<b>(148)</b>	<b>(1,629)</b>
Gain on sales of stock of subsidiaries and affiliates	72	—	—
Reversal of allowance for doubtful accounts	—	<b>22</b>	<b>252</b>
Provision for allowance for doubtful accounts	(142)	<b>(50)</b>	<b>(552)</b>
Dilution gain (loss) from change in equity interest	23	<b>(17)</b>	<b>(190)</b>
Equity in net income of unconsolidated subsidiaries and affiliates	43	<b>18</b>	<b>206</b>
Gain on sales of fixed assets	28	<b>7</b>	<b>85</b>
Loss on disposal of fixed assets	(425)	<b>(1,108)</b>	<b>(12,182)</b>
Impairment losses	(446)	<b>(275)</b>	<b>(3,031)</b>
Loss on devaluation of investments in securities	(93)	<b>(284)</b>	<b>(3,123)</b>
Loss on devaluation of investments in subsidiaries and affiliates	(238)	—	—
Gain on transition of retirement benefit plan	4,298	—	—
Other, net	425	<b>506</b>	<b>5,565</b>
	3,545	<b>(1,155)</b>	<b>(12,692)</b>
Income before income taxes and minority interests	33,597	<b>25,934</b>	<b>284,964</b>
<b>Income taxes</b> (Note 9)			
Current	13,239	<b>11,212</b>	<b>123,199</b>
Deferred	1,253	<b>117</b>	<b>1,291</b>
	14,492	<b>11,329</b>	<b>124,491</b>
<b>Minority interests</b>	247	<b>233</b>	<b>2,563</b>
Net income	¥ 18,856	<b>¥ 14,371</b>	<b>\$ 157,910</b>
		yen	U.S. dollars (Note 3)
<b>Net income and dividends per share</b> (Note 2(12))			
Basic net income	¥596.69	<b>¥454.76</b>	<b>\$5.00</b>
Diluted net income	596.56	<b>454.53</b>	<b>4.99</b>
Cash dividends	130.00	<b>130.00</b>	<b>1.43</b>

The accompanying notes are an integral part of these statements.

## Consolidated Statements of Changes in Net Assets

OTSUKA CORPORATION and Consolidated Subsidiaries  
For the years ended December 31, 2007 and 2008

Millions of yen

	Number of shares issued	Shareholders' equity				Total shareholders' equity
		Common stock	Capital surplus	Retained earnings	Treasury stock	
<b>Balance at December 31, 2006</b>	31,667,020	¥10,374	¥16,254	¥60,120	¥(117)	¥ 86,632
Dividends				(3,634)		(3,634)
Net income				18,856		18,856
Reversal of revaluation differences on land				74		74
Purchase of treasury stock					(2)	(2)
Other				(27)		(27)
Items other than changes in shareholders' equity						
<b>Balance at December 31, 2007</b>	31,667,020	10,374	16,254	75,389	(120)	101,899
Dividends				(4,108)		(4,108)
Net income				14,371		14,371
Purchase of treasury stock					(2)	(2)
Items other than changes in shareholders' equity						
<b>Balance at December 31, 2008</b>	31,667,020	¥10,374	¥16,254	¥85,652	¥(122)	¥112,159

Millions of yen

	Valuation and translation adjustments					Minority interest in consolidated subsidiaries	Total net assets
	Unrealized gains on available-for- sale securities	Deferred losses on hedges	Revaluation differences on land	Foreign currency translation adjustments	Total valuation and translation adjustments		
<b>Balance at December 31, 2006</b>	¥1,779	¥(0)	¥(15,500)	¥(63)	¥(13,784)	¥566	¥73,414
Dividends							(3,634)
Net income							18,856
Reversal of revaluation differences on land							74
Purchase of treasury stock							(2)
Other							(27)
Items other than changes in shareholders' equity	(797)	0	(74)	16	(854)	175	(679)
<b>Balance at December 31, 2007</b>	982	—	(15,574)	(47)	(14,639)	741	88,000
Dividends							(4,108)
Net income							14,371
Purchase of treasury stock							(2)
Items other than changes in shareholders' equity	(553)	—	—	(90)	(643)	172	(470)
<b>Balance at December 31, 2008</b>	¥ 429	—	¥(15,574)	¥(137)	¥(15,282)	¥913	¥97,790

The accompanying notes are an integral part of these statements.

OTSUKA CORPORATION and Consolidated Subsidiaries  
For the years ended December 31, 2007 and 2008

Thousands of U.S. dollars (Note 3)

	Number of shares issued	Shareholders' equity				Total shareholders' equity
		Common stock	Capital surplus	Retained earnings	Treasury stock	
<b>Balance at December 31, 2007</b>	31,667,020	\$113,996	\$178,603	\$828,364	\$(1,318)	\$1,119,646
Dividends				(45,140)		(45,140)
Net income				157,910		157,910
Purchase of treasury stock					(31)	(31)
Items other than changes in shareholders' equity						
<b>Balance at December 31, 2008</b>	31,667,020	\$113,996	\$178,603	\$941,133	\$(1,350)	\$1,232,384

Thousands of U.S. dollars (Note 3)

	Valuation and translation adjustments				Minority interest in consolidated subsidiaries	Total net assets
	Unrealized gains on available-for- sale securities	Revaluation differences on land	Foreign currency translation adjustments	Total valuation and translation adjustments		
<b>Balance at December 31, 2007</b>	\$10,797	\$(171,130)	\$ (520)	\$(160,854)	\$ 8,143	\$ 966,935
Dividends						(45,140)
Net income						157,910
Purchase of treasury stock						(31)
Items other than changes in shareholders' equity	(6,082)	—	(989)	(7,071)	1,899	(5,172)
<b>Balance at December 31, 2008</b>	\$ 4,714	\$(171,130)	\$(1,510)	\$(167,926)	\$10,042	\$1,074,500

The accompanying notes are an integral part of these statements.

## Consolidated Statements of Cash Flows

OTSUKA CORPORATION and Consolidated Subsidiaries  
For the years ended December 31, 2007 and 2008

Thousands of  
U.S. dollars  
(Note 3)

	Millions of yen		2008
	2007	2008	
<b>Cash flows from operating activities:</b>			
Income before income taxes and minority interests	¥33,597	¥25,934	\$284,964
Depreciation and amortization	5,388	6,012	66,062
Amortization of (negative) goodwill	(4)	—	—
Equity in net income of unconsolidated subsidiaries and affiliates	(43)	(18)	(206)
Increase (decrease) in reserve for retirement benefits	(6,331)	486	5,346
Increase in allowance for doubtful accounts	60	131	1,443
Interest and dividend income	(137)	(173)	(1,908)
Interest expenses	138	148	1,629
Gain on sales of fixed assets	(28)	(7)	(85)
Loss on disposal of fixed assets	425	961	10,567
Impairment losses	446	275	3,031
Loss on devaluation of investments in securities	93	284	3,123
Gain on sales of stock of subsidiaries	(72)	—	—
Loss on devaluation of investments in subsidiaries and affiliates	238	—	—
Dilution loss (gain) from change in equity interest	(23)	17	190
Decrease (increase) in accounts and notes receivable	(6,324)	3,511	38,580
Decrease (increase) in inventories	(465)	397	4,367
Increase (decrease) in accounts and notes payable	21	(7,298)	(80,197)
Other	(32)	(2,888)	(31,741)
Subtotal	26,946	27,773	305,170
Interest and dividend income received	157	202	2,222
Interest expenses paid	(137)	(148)	(1,636)
Income taxes paid	(10,311)	(14,479)	(159,100)
Net cash provided by operating activities	16,654	13,347	146,655
<b>Cash flows from investing activities:</b>			
Payments for purchase of property and equipment	(2,528)	(2,812)	(30,904)
Proceeds from sales of property and equipment	546	292	3,213
Payments for software developed	(2,567)	(2,702)	(29,691)
Payments for purchase of investments in securities	(279)	(1,293)	(14,210)
Proceeds from sales of investments in securities	—	112	1,230
Proceeds from sales of stock of consolidated subsidiaries' stock	470	—	—
Payments for long-term loans receivable	(428)	(355)	(3,906)
Proceeds from long-term loans receivable	16	92	1,014
Other	214	(294)	(3,230)
Net cash used in investing activities	(4,555)	(6,960)	(76,486)
<b>Cash flows from financing activities:</b>			
Increase (decrease) in short-term bank loans, net	(350)	2,200	24,173
Proceeds from long-term debts	200	—	—
Repayments for long-term debts	(652)	(2,621)	(28,802)
Proceeds from issuance of new shares	192	—	—
Cash dividends paid	(3,632)	(4,107)	(45,128)
Other	(28)	(63)	(695)
Net cash used in financing activities	(4,271)	(4,591)	(50,452)
<b>Effect of exchange rate changes on cash and cash equivalents</b>	(25)	—	—
<b>Net increase in cash and cash equivalents</b>	7,802	1,794	19,717
<b>Cash and cash equivalents at beginning of year</b>	18,305	25,374	278,814
<b>Decrease in cash and cash equivalents due to exclusion of subsidiaries from scope of consolidation</b>	(732)	—	—
<b>Cash and cash equivalents at end of year (Note 10)</b>	¥25,374	¥27,169	\$298,531

The accompanying notes are an integral part of these statements.

# Notes to Consolidated Financial Statements

OTSUKA CORPORATION and 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 the 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 Companies Act and the Financial Instruments and Exchange Law of Japan.

Certain items presented in the consolidated financial statements have been reclassified for the convenience of readers outside Japan.

## 2. Summary of Significant Accounting Policies

### (1) Scope of consolidation

The Company had 13 subsidiaries (majority-owned companies) and 12 subsidiaries as at December 31, 2007 and 2008, respectively. The consolidated financial statements include the accounts of the Company and 8 subsidiaries for the years ended December 31, 2007 and 2008.

The 8 subsidiaries which were consolidated in the year ended December 31, 2008 are listed below:

	A ratio of voting rights held by the Company
OSK Co., LTD.	100.0%
Netplan Co., Ltd.	100.0%
Alpha Techno Co., LTD.	100.0%
Alpha System Co., LTD.	100.0%
Alpha Net Co., LTD.	100.0%
Otsuka Auto Service Co., LTD.	100.0%
Network Corporation	68.3%
Otsuka Business Service Co., LTD.	65.0%

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

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 5 unconsolidated subsidiaries and 4 unconsolidated subsidiaries as at December 31, 2007 and 2008, respectively, consisted of insignificant amounts in terms of total assets, net sales, net income and retained earnings, and have, therefore, been excluded from consolidation.

### (2) Investments in unconsolidated subsidiaries and affiliates

The Company had 5 unconsolidated subsidiaries and 9 affiliates at December 31, 2007 and 4 unconsolidated subsidiaries and 9 affiliates at December 31, 2008.

The Company had 2 investments in affiliate and 3 investments in affiliate for the equity method at December 31, 2007 and 2008, respectively. 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.

The 3 investment in affiliate by the equity method at December 31, 2008, are listed below:

	A ratio of voting rights held by the Company
SIOS Technology, Inc.	46.1%
Otsuka Information Technology Corp.	39.8%
LION OFFICE PRODUCTS CORP.	40.4%

(Fiscal year 2008)

LION OFFICE PRODUCTS CORP. became an affiliate company of the Company and accounted for by the equity method after its capital increase through third party allotment on May 28, 2008.

### **(3) 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.

### **(4) Inventories**

Inventories are valued by the 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

### **(5) Financial instruments**

#### **(a) Securities**

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

- **Held-to-maturity debt securities**

Held-to-maturity debt securities are stated using amortized cost method on a straight-line basis.

- **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, determined by the moving-average method, because the effect of application of the equity method would be immaterial.

- **Available-for-sale securities**

Securities with market quotations 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 net assets at a net-of-tax amount, while cost of sale is determined by the moving-average method.)

Securities without market quotations are stated at cost, determined by the moving-average method.

Regarding investments in limited partnerships and similar investments, an amount equivalent to the Company's partnership investment gain or loss under the equity method, with such a gain or loss being based on the latest available financial statements of the corresponding limited partnerships, was recognized in the consolidated financial statements.

#### **(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, and forward exchange contracts. The related hedged items are trade bank loans and accounts payable.

The Companies have a policy to utilize 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.

#### **(6) Property and equipment**

Depreciation is computed using the declining-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.

Estimated useful lives of assets are principally as follows:

- Building and structures — 15 to 50 years
- Other — 4 to 6 years

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

(Fiscal year 2008)

Due to the revision to corporate tax legislation, the Company and its subsidiaries adopted the depreciation method based on the revised Corporate Tax Law for tangible fixed assets acquired on or before March 31, 2007. With this method, the difference between the amounts equivalent to 5% of the acquisition costs and the residual value are depreciated evenly over five years effectively from the year following the fiscal year when the residual value reached the amounts equivalent to 5% of the acquisition costs, and recorded as depreciation expenses.

The effect of this change on the financial result is immaterial.

#### **(7) 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.

#### **(8) Software and other intangible assets**

The amortization of costs of software developed for external sales is computed at an amount based on the ratio of actual sales during the year to total estimated sales for the estimated salable period. 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 mainly 5 years.

Other intangible assets with finite useful lives are amortized using the straight-line method over the estimated useful lives.

#### **(9) Accounting for income taxes**

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

#### **(10) Allowance for doubtful accounts**

An allowance for doubtful accounts 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.

#### **(11) 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, 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.

(b) Retirement benefits for directors

The Company and six 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.

#### (12) 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.

Diluted net income per common share assumes full exercise of outstanding stock options which have a dilutive effect.

#### (13) 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.

#### (14) Rounding of amounts

Rounding down sums of less than a million yen.

### 3. U.S. Dollar Amounts

Amounts in U.S. dollars are included solely for the convenience of readers outside Japan. The rate of ¥91.01=US\$1, the rate of exchange on December 31, 2008, 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, 2007 and 2008 investments in securities were as follows:

#### (1) Available-for-sale securities with fair value

	Millions of yen						Thousands of U.S. dollars		
	2007			2008			2008		
	Acquisition cost	Carrying value	Unrealized gain (loss)	Acquisition cost	Carrying value	Unrealized gain (loss)	Acquisition cost	Carrying value	Unrealized gain (loss)
<b>Securities whose carrying value exceed their acquisition costs</b>									
Stocks	¥1,075	¥2,790	¥1,714	¥ 962	¥1,753	¥791	\$10,573	\$19,268	\$8,694
Bonds	—	—	—	—	—	—	—	—	—
Other securities	92	119	26	—	—	—	—	—	—
	¥1,167	¥2,909	¥1,741	¥ 962	¥1,753	¥791	\$10,573	\$19,268	\$8,694
<b>Securities whose carrying value does not exceed their acquisition costs</b>									
Stocks	¥ 468	¥ 383	¥ (84)	¥ 428	¥ 377	¥(51)	\$ 4,711	\$ 4,144	\$ (567)
Bonds	—	—	—	—	—	—	—	—	—
Other securities	—	—	—	92	61	(30)	1,013	677	(336)
	¥ 468	¥ 383	¥ (84)	¥ 521	¥ 438	¥(82)	\$ 5,725	\$ 4,821	\$ (903)
<b>Total</b>	<b>¥1,635</b>	<b>¥3,293</b>	<b>¥1,657</b>	<b>¥1,483</b>	<b>¥2,192</b>	<b>¥709</b>	<b>\$16,298</b>	<b>\$24,089</b>	<b>\$7,791</b>

**(2) Available-for-sale securities sold in 2007 and 2008 (for the years ended December 31, 2007 and 2008)**

			Millions of yen			Thousands of U.S. dollars		
			2007	2008		2008		
Sales proceeds	Aggregate gains	Aggregate losses	Sales proceeds	Aggregate gains	Aggregate losses	Sales proceeds	Aggregate gains	Aggregate losses
—	—	—	¥112	¥12	—	\$1,230	\$131	—

**(3) Carrying value of major securities whose fair value is not available**

		Millions of yen		Thousands of U.S. dollars	
		2007	2008		2008
		Carrying value on consolidated balance sheets	Carrying value on consolidated balance sheets		Carrying value on consolidated balance sheets
<b>Held-to-maturity debt securities</b>					
Negotiable certificates of deposit		—	¥3,000		\$32,963
Commercial paper		—	1,996		21,940
<b>Available-for-sale securities</b>					
Unlisted stocks		866	655		7,204
Investment limited liability partnerships		276	200		2,199

**(4) The carrying values of debt securities by contractual maturities for securities classified as available-for-sale and held-to-maturity were as follows:**

			Millions of yen		Thousands of U.S. dollars	
			2007		2008	
			Within one year	More than one year	Within one year	More than one year
<b>Held-to-maturity debt securities</b>						
Negotiable certificates of deposit			—	—	¥3,000	—
Commercial paper			—	—	1,996	—
<b>Total</b>			—	—	¥4,996	—
					\$54,903	—

## 5. Derivative Information

The Companies utilize derivative transactions for the purpose of hedging their exposure to fluctuation in foreign exchange rates on payables denominated in foreign currencies and interest rates on interest-bearing debt, however, do not enter into transactions involving derivatives for speculative purposes.

The relevant derivative transactions used for hedging are summarizing as follows:

Foreign exchange risk associated with liabilities denominated in foreign currencies: forward foreign exchange contracts

Interest rate risk associated with sourcing funds and investing: interest rate swaps

There remains the risk of foreign currency exchange fluctuations on currency transactions and the risk of interest rate fluctuations on interest rate transactions. As the Companies enter into derivative transactions only with financial institutions which have a sound credit profile, we believe that a credit risk is insignificant.

All risk hedge operations and management are carried out pursuant to the Companies' rules which stipulate management policies of derivative transactions, limitation of a hedging position and so forth by treasury department with an appropriate approval.

At December 31, 2007 and 2008, derivatives were as follows:

Currency-related transactions

	Millions of yen			
	2007			
	Contractual value or notional principal amount		Fair value	Valuation gain (loss)
Total	Over one year			
Forward foreign exchange contracts				
Purchased U.S.dollar	—	—	—	—

	Millions of yen			
	2008			
	Contractual value or notional principal amount		Fair value	Valuation gain (loss)
Total	Over one year			
Forward foreign exchange contracts				
Purchased U.S.dollar	¥126	—	¥127	¥0

	Thousands of U.S. dollars			
	2008			
	Contractual value or notional principal amount		Fair value	Valuation gain (loss)
Total	Over one year			
Forward foreign exchange contracts				
Purchased U.S.dollar	\$1,394	—	\$1,398	\$4

## 6. Inventories

Inventories at December 31, 2007 and 2008 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Merchandise and maintenance parts	¥16,072	¥15,526	\$170,600
Work-in-process	737	892	9,806
Supplies	114	107	1,181
	¥16,923	¥16,526	\$181,588

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

The annual average interest rates applicable to short-term bank loans at December 31, 2007 and 2008 were 1.45% and 1.32%, respectively.

Long-term debt at December 31, 2007 and 2008 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Long-term loans from banks with annual interest rates:			
1.63%	¥2,751	¥130	\$1,428
	2,751	130	1,428
Less : Current maturities of long-term debts	(2,621)	(40)	(439)
	¥ 130	¥ 90	\$ 988

Aggregate annual maturities of long-term debt subsequent to December 31, 2008 are as follows:

Year ending December 31	Millions of yen	Thousands of U.S. dollars
2009	¥ 40	\$ 439
2010	40	439
2011	40	439
2012	10	109
	¥130	\$1,428

## 8. Reserve for Retirement Benefits

### (1) Retirement benefit plan

The Company and certain its subsidiaries operated a defined contribution 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, 2007 and 2008 is summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Projected benefit obligations	¥ (29,317)	¥(31,095)	\$(341,668)
Plan assets	39,741	26,742	293,836
	10,423	(4,353)	(47,831)
Unrecognized prior service cost	(5,698)	(5,007)	(55,023)
Unrecognized actuarial gain or loss	(3,351)	10,248	112,609
	1,374	887	9,755
Prepaid pension cost	2,690	2,401	26,390
Reserve for retirement benefits	¥ (1,316)	¥(1,514)	\$(16,635)

The balance of the reserve for retirement benefits in the accompanying consolidated balance sheets at December 31, 2007 and 2008 included retirement benefits for directors in the amounts of 504 million yen and 530 million yen (5,825 thousand U.S. dollars), respectively.

**(3) Pension expense related to the retirement benefits for the years ended December 31, 2007 and 2008 were as follows:**

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Service cost	¥ 2,731	<b>¥2,352</b>	<b>\$25,846</b>
Interest cost	525	<b>431</b>	<b>4,742</b>
Expected return on plan assets	(1,240)	<b>(1,192)</b>	<b>(13,100)</b>
Amortization of the unrecognized prior service cost	(690)	<b>(690)</b>	<b>(7,589)</b>
Amortization of the unrecognized actuarial gain or loss	11	<b>(187)</b>	<b>(2,058)</b>
Payments for defined contribution pension plan	377	<b>772</b>	<b>8,489</b>
Additional benefits for employees' early retirement	188	<b>151</b>	<b>1,666</b>
Net periodic pension cost	¥ 1,903	<b>¥1,638</b>	<b>\$17,998</b>
Gain on transition of retirement benefit plan	¥(4,298)	—	—

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

**(4) Computation basis of pension liabilities**

As of December 31, 2007 and 2008

	2007	2008
Discount rate	1.5%	<b>1.5%</b>
Expected rate of return on plan assets	3.0%	<b>3.0%</b>
Periodic allocation principle	Standard of fixed-amount	<b>Standard of fixed-amount</b>
for projected benefit obligation	-for-period	<b>-for-period</b>
Amortization of unrecognized prior service cost	12 years	<b>12 years</b>
Amortization of unrecognized actuarial gain or loss	12 years from the fiscal year following occurrence	<b>12 years from the fiscal year following occurrence</b>

## 9. Income Taxes

A reconciliation between the normal statutory tax rates and the effective tax rates reflected in the accompanying consolidated statements of income for the years ended December 31, 2007 and 2008 was as follows:

	2007	2008
Statutory tax rate	40.7%	<b>40.7%</b>
Expenses not deductible for tax purposes	0.6%	<b>0.7%</b>
Per capita inhabitant tax	0.4%	<b>0.5%</b>
Valuation allowance	1.7%	<b>2.4%</b>
Deduction for tax incentive to help strengthen information infrastructure for business	(0.4%)	<b>(0.1%)</b>
Other	0.1%	<b>(0.5%)</b>
Effective tax rate	43.1%	<b>43.7%</b>

At December 31, 2007 and 2008, significant components of the deferred tax assets and liabilities were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
<b>Deferred tax assets:</b>			
Allowance for doubtful accounts	¥ 299	¥ 322	\$3,545
Enterprise taxes	753	519	5,704
Accrued bonuses	1,111	1,018	11,187
Retirement benefits for employees	537	617	6,786
Retirement benefits for directors	205	216	2,377
Impairment losses	781	742	8,163
Software cost	1,240	1,357	14,915
Eliminated unrealized profits	420	411	4,520
Other	1,050	1,185	13,029
<b>Total deferred tax assets</b>	<b>6,401</b>	<b>6,391</b>	<b>70,230</b>
Less: Valuation allowance	(823)	(1,443)	(15,859)
<b>Net deferred tax assets</b>	<b>5,578</b>	<b>4,948</b>	<b>54,370</b>
<b>Deferred tax liabilities:</b>			
Reserve for computer program	1,035	639	7,023
Prepaid pension cost	1,097	979	10,763
Unrealized gains on available-for-sale securities	674	288	3,167
Other	19	21	233
<b>Total deferred tax liabilities</b>	<b>2,826</b>	<b>1,928</b>	<b>21,187</b>
<b>Net deferred tax assets</b>	<b>¥2,751</b>	<b>¥3,019</b>	<b>\$33,182</b>

## 10. Supplementary Cash Flow Information

Cash and cash equivalents consisted of:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Cash, time deposits and other cash equivalents	¥24,785	¥21,544	\$236,726
Time deposits with deposit terms of more than three months	(105)	(55)	(604)
Short-term investments with maturity or redemption dates within three months of acquisition date	—	4,996	54,903
Trust beneficiary interests included in other current assets with investment terms with three months or less	694	683	7,506
<b>Cash and cash equivalents at end of year</b>	<b>¥25,374</b>	<b>¥27,169</b>	<b>\$298,531</b>

## 11. Subsequent Events

### (1) Appropriation

The following appropriation of the Company's retained earnings in respect of the year ended December 31, 2008 was as proposed by the Board of Directors and approved by the shareholders at the annual general meeting held on March 27, 2009:

Appropriation	Millions of yen	Thousands of U.S. dollars
Cash dividends (¥130.00 per share)	¥4,108	\$45,140

## 12. Lease Transactions

The *proforma* information of acquisition costs, accumulated depreciation and net book values of leased assets at December 31, 2007 and 2008 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Acquisition cost	¥6,152	<b>¥4,617</b>	<b>\$50,736</b>
Accumulated depreciation	(3,543)	<b>(2,602)</b>	<b>(28,600)</b>
Net book value	¥2,608	<b>¥2,014</b>	<b>\$22,136</b>

Future minimum lease payments under finance leases at December 31, 2007 and 2008 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Due within one year	¥ 998	<b>¥ 795</b>	<b>\$ 8,744</b>
Due after one year	1,652	<b>1,260</b>	<b>13,846</b>
	¥2,650	<b>¥2,056</b>	<b>\$22,591</b>

Lease rental expenses, depreciation and interest expenses for the years ended December 31, 2007 and 2008 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Lease rental expenses	¥1,311	<b>¥1,060</b>	<b>\$11,653</b>
Depreciation	1,254	<b>1,009</b>	<b>11,095</b>
Interest expenses	59	<b>48</b>	<b>529</b>

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, 2007 and 2008 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Due within one year	¥ 761	<b>¥ 663</b>	<b>\$ 7,292</b>
Due after one year	2,088	<b>1,574</b>	<b>17,300</b>
	¥2,850	<b>¥2,238</b>	<b>\$24,593</b>

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### 13. Shareholders' Equity

The Companies Act of Japan provides that an amount equal to 10% of the amount to be distributed as distributions of capital surplus (other than the capital reserve) and retained earnings (other than the legal reserve) be transferred to the capital reserve and the legal reserve, respectively, until the sum of the capital reserve and the legal reserve equals 25% of the common stock account. Such distributions can be made at any time by resolution of the shareholders, or by the Board of Directors if certain conditions are met, but neither the capital reserve nor the legal reserve is available for distributions.

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### 14. Land Revaluation

Pursuant to the Law Concerning 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 "Revaluation difference on land" net assets 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 Concerning Land Revaluation, after making reasonable adjustments. Revaluation is permitted for one time only. The excess of the book value after revaluation over the fair value are 1,212 million yen and 672 million yen (7,391 thousand U.S. dollars) at December 31, 2007 and 2008, respectively.

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### 15. Pledged Assets

At December 31, 2007 and 2008, assets pledged as collateral for accounts and notes payable were as follows:

	Millions of yen		Thousands of
	2007	2008	U.S. dollars
Time deposits	¥5	¥5	2008
	¥5	¥5	\$54

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### 16. 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, 2007 and 2008 amounted to 829 million yen and 757 million yen (8,324 thousand U.S. dollars), respectively.

## 17. Segment Information

The business segment information of the Company and its consolidated subsidiaries for the years ended December 31, 2007 and 2008 is summarized as follows:

### (1) Business segment information

	Millions of yen					
	System Integration	Service & Support	Other	Total	Elimination or corporate	Consolidated total
2007						
Net sales to:						
Third parties	¥279,753	¥187,358	¥2,370	¥469,481	¥ —	¥469,481
Inter-segment sales/transfers	96	284	2,358	2,738	(2,738)	—
	279,850	187,642	4,728	472,220	(2,738)	469,481
Operating expenses	255,445	174,873	4,587	434,906	4,523	439,430
Operating income	¥ 24,404	¥ 12,769	¥ 140	¥ 37,314	¥ (7,262)	¥ 30,051
Assets, depreciation, impairment losses and capital expenditure:						
Assets	¥ 88,233	¥ 74,147	¥2,036	¥164,417	¥35,966	¥200,383
Depreciation and amortization	2,529	2,098	24	4,651	737	5,388
Impairment losses	4	5	304	314	131	446
Capital expenditure	2,215	1,712	14	3,942	1,153	5,095

	Millions of yen					
	System Integration	Service & Support	Other	Total	Elimination or corporate	Consolidated total
2008						
Net sales to:						
Third parties	¥266,476	¥198,761	¥1,916	¥467,154	¥ —	¥467,154
Inter-segment sales/transfers	191	296	2,142	2,630	(2,630)	—
	266,668	199,057	4,058	469,785	(2,630)	467,154
Operating expenses	243,679	187,517	3,911	435,108	4,956	440,064
Operating income	¥ 22,989	¥ 11,539	¥ 146	¥ 34,676	¥ (7,586)	¥ 27,089
Assets, depreciation, impairment losses and capital expenditure:						
Assets	¥ 82,639	¥ 75,758	¥1,618	¥160,017	¥36,928	¥196,946
Depreciation and amortization	2,898	2,215	22	5,136	875	6,012
Impairment losses	14	291	—	305	(30)	275
Capital expenditure	2,915	1,790	8	4,715	819	5,535

	Thousands of U.S. dollars					
	System Integration	Service & Support	Other	Total	Elimination or corporate	Consolidated total
2008						
Net sales to:						
Third parties	\$2,927,996	\$2,183,950	\$21,055	\$5,133,002	\$ —	\$5,133,002
Inter-segment sales/transfers	2,106	3,257	23,540	28,904	(28,904)	—
	2,930,102	2,187,208	44,595	5,161,907	(28,904)	5,133,002
Operating expenses	2,677,498	2,060,410	42,980	4,780,888	54,456	4,835,345
Operating income	\$ 252,604	\$ 126,798	\$ 1,614	\$ 381,018	\$ (83,360)	\$ 297,657
Assets, depreciation, impairment losses and capital expenditure:						
Assets	\$ 908,029	\$ 832,424	\$17,786	\$1,758,239	\$405,766	\$2,164,006
Depreciation and amortization	31,848	24,342	249	56,441	9,621	66,062
Impairment losses	163	3,198	—	3,362	(330)	3,031
Capital expenditure	32,040	19,675	95	51,811	9,009	60,820

Notes ;

1. Business segments are defined in consideration of the operations of the companies.
2. Significant operations of each segment are as summarized below;

Segment	Major product and services
System Integration business	Research, analysis, design, and introduction for comprehensive information system Transport and installation Network construction Introduction for packaged software Development of consigned software Other related services
Service and Support business	Supplies for comprehensive information system Telephone support Maintenance Consigned system operation Data recovery IT education Guidance for operation of packaged software Hotel business
Other business	Construction Repair, sale of automobiles Insurance Printing

3. Significant components of "Eliminations or corporate" are as follows;

	Millions of yen		Thousands of U.S. dollars
	2007	2008	2008
Non-allocable operating expenses	¥ 7,326	¥ 7,654	\$ 84,110
Corporate assets	37,262	38,304	420,885

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.

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 for overseas sales is not disclosed pursuant to regulations on consolidated financial statements in Japan, since aggregate of overseas sales of the Company and its domestic consolidated subsidiaries and overseas consolidated subsidiaries, were less than 10% of consolidated net sales.**

### Report of Independent Auditors

The Board of Directors

OTSUKA CORPORATION

We have audited the accompanying consolidated balance sheets of OTSUKA CORPORATION and consolidated subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of income, changes in net assets, and cash flows for the year then ended, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of OTSUKA CORPORATION and consolidated subsidiaries at December 31, 2008 and 2007, and the consolidated results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in Japan.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended December 31, 2008 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3.

*Ernst & Young Shin Nihon LLC*

March 27, 2009

## Principal Group Companies (As of December 31, 2008)

The OTSUKA Group (OTSUKA CORPORATION and its subsidiaries) consists of 12 subsidiaries, including 8 consolidated subsidiaries as well as 12 affiliated companies, including 3 affiliates for the equity method that carry out the System Integration business, Service and Support business and Other business. The 8 consolidated subsidiaries are listed below.

Company Name	Established	Capital (¥ million)	A ratio of voting rights	Scope of Business
<b>■ System Integration business</b>				
OSK Co., LTD.	1984	300	100.0%	• Development and sale of packaged software
Netplan Co., Ltd.	1964	499	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
Networld Corporation	1990	585	68.3%	• Sales and technical support for network related equipment
<b>■ Service and Support business</b>				
Alpha Techno Co., LTD.	1996	50	100.0%	• Emergency repair of PCs and peripheral equipment, and data recovery service
Alpha Net Co., LTD.	1997	400	100.0%	• Comprehensive service and support for network systems
<b>■ Other business</b>				
Otsuka Auto Service Co., LTD.	1987	50	100.0%	• Maintenance, body work and sale 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, 2008)

<b>Name</b>	OTSUKA CORPORATION
<b>Founded</b>	July 17, 1961 (registered as joint-stock company on December 13, 1961)
<b>Paid-in Capital</b>	¥10,374,851,000
<b>Number of Employees</b>	6,736 (with consolidated subsidiaries: 8,202)
<b>Business</b>	<p><b>System Integration Business :</b></p> <p>Sales of computers, copiers, communication equipment and software, and software development of consigned software, other activities</p> <p><b>Service and Support Business :</b></p> <p>Supplies, maintenance, and educational support, other activities</p>
<b>Main Banks</b>	<p>The Bank of Yokohama, Ltd.</p> <p>The Bank of Tokyo-Mitsubishi UFJ, Ltd.</p> <p>Mizuho Bank, Ltd.</p>

### Base (As of December 31, 2008)

<b>Head Office</b>	2-18-4 Iidabashi, Chiyoda-ku, Tokyo, 102-8573 TEL 03-3264-7111		
<b>Branch Offices</b>	<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>		
<b>Local Area Sales Groups</b>	Chuo Sales Group 1 Johoku Sales Group Kanagawa Sales Group Osaka Southern Sales Group	Chuo Sales Group 2 Tama Sales Group Northern Kanto Sales Group	Josai Sales Group Keiyo Sales Group Osaka Northern Sales Group
<b>Regional Offices</b>	Sapporo Branch Nagoya Branch Kobe Branch	Sendai Branch Mikawa Branch Hiroshima Branch	Utsunomiya Branch Kyoto Branch Kyushu Branch

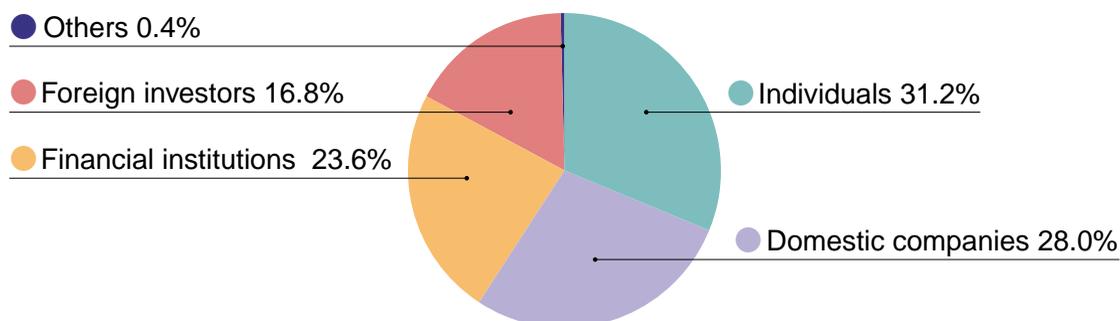
## Stock Information (As of December 31, 2008)

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	4,917

### Major Shareholders

Name	Investment in OTSUKA CORPORATION		Investment in Major Shareholders by OTSUKA CORPORATION	
	Number of Shares held	Equity Ownership (%)	Number of Shares held	Equity Ownership (%)
Otsuka Sobi Co., Ltd.	8,537,530	26.96	—	—
Yuji Otsuka	2,197,780	6.94	—	—
Minoru Otsuka	1,525,490	4.81	—	—
Japan Trustee Services Bank, Ltd. (Trust Account)	1,450,100	4.57	—	—
The Master Trust Bank of Japan, Ltd. (Trust Account)	1,435,800	4.53	—	—
Japan Trustee Services Bank, Ltd. (Trust Account 4G)	1,408,300	4.44	—	—
Atsushi Otsuka	1,075,850	3.39	—	—
OTSUKA CORPORATION Employee Stock-Sharing Plan	1,015,420	3.20	—	—
Terue Otsuka	645,500	2.03	—	—
The Chase Manhattan Bank, N.A. London Secs Lending Omnibus Account	552,084	1.74	—	—

### Breakdown of Shareholders (Based on total shares)



The background is a vibrant yellow with a central bright point from which numerous thin white lines radiate outwards, creating a sunburst effect. Scattered throughout the scene are several 3D-rendered spheres of varying sizes, all in shades of yellow and gold, giving the impression of a dynamic, energetic space.

OTSUKA CORPORATION WEBSITE

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

***Otsuka Corporation***

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