

3. Financial Condition

Assets, Liabilities and Shareholders' Equity

(Billion Yen)

	As of March 31, 2004	Change from March 31, 2003
Total assets	3,865.5	-359.7
(Cash and cash equivalents and short-term investments)	(416.9)	(132.9)
Interest bearing loans	1,277.1	-486.6
Total shareholders' equity	827.1	124.7

Total assets at the end of fiscal 2003 were 3,865.5 billion yen (US\$36,468 million), a reduction of 359.7 billion yen from the end of the previous fiscal year. The reduction in assets is a result of the switch to equity-method accounting for our flash memory operations and leasing affiliate, as well as the sale of marketable securities and other measures that we have pursued to improve asset efficiency.

We reduced total current assets by 56.0 billion yen from the end of the last fiscal year. Cash and cash equivalents and short-term investments increased by 132.9 billion yen. We had a 74.8 billion yen decline in inventories, and other current assets declined by 84.2 billion yen, primarily as a result of a decrease in lease receivables associated with the shift to the equity method of accounting for the leasing operation.

Total fixed assets decreased by 303.7 billion yen from the end of the prior fiscal year. Property, plant, and equipment less accumulated depreciation decreased by 187.5 billion yen, due in large part to the shift to the equity method of accounting for the flash memory operation and selectivity in making new capital investments. Investments and other assets decreased by 74.5 billion yen as a result of such factors as the sale of FANUC shares and the effect of the shift to the equity method of accounting for the leasing operation.

Total liabilities were 2,847.9 billion yen (US\$26,867 million), a reduction of 460.4 billion yen compared to the end of the prior fiscal year. The reduction of 486.6 billion yen in interest bearing loans was accomplished as a result of improved profitability in business operations, as well as proceeds from the sale of marketable securities and by the shift to equity-method accounting for the leasing operation.

Total shareholders' equity increased by 124.7 billion yen, to 827.1 billion yen (US\$7,804 million). As a result, the shareholders' equity ratio increased to 21.4%, surpassing the 20% mark for the first time in three years. This increase was attributable to increased profits in our business operations as well as a change to market value accounting for holdings in FANUC from the third quarter.

Summary of Cash Flows

(Billion Yen)

	FY 2003	Change from FY 2003
Cash flows from operating activities	304.0	186.2
Cash flows from investing activities	67.3	131.8
Free cash flow	371.4	318.0

Net cash provided by operating activities during the fiscal year was 304.0 billion yen (US\$2,868 million). The earnings recovery in our business operations pushed operating cash flows back above the 300 billion yen level, an improvement of 186.2 billion yen compared to the prior fiscal year.

Net cash provided by investing activities was 67.3 yen (US\$636 million). In addition to a decrease in the outflow of funds from investing activities due to greater selectivity in capital expenditures, there was inflow of funds from the sale of shareholdings as well as from sales of fixed assets.

Adding together the cash flows from operating activities and the cash flows from investing activities, free cash flow strongly rebounded, amounting to 371.4 billion yen (US\$3,504 million), a portion of which was used to redeem corporate bonds and repay borrowings. Net cash provided by financing activities was negative 239.9 billion yen (US\$2,263 million).

As a result, cash and cash equivalents stood at 413.8 billion yen (US\$3,904 million) at the end of the period, 131.4 billion yen more than at year-end in fiscal 2002.

Financial Index

All of our key financial indices showed major improvement in fiscal 2003, and a number of them recorded even better results than in fiscal 2000, just before the bursting of the IT bubble.

With respect to profitability, operating margins rose to 3.2%, moving closer to the 4.4% level of fiscal 2000. Although shareholders' equity was about 400 billion yen lower than in fiscal 2000, we achieved a major improvement in our shareholders' equity ratio, raising it to 21.4% and approaching the 23.4% level recorded in fiscal 2000. There were also considerable improvements compared to fiscal 2000 in the areas of total assets and interest bearing liabilities. Total assets were reduced by 25% compared with the peak level in fiscal 2000, and efficiency increased significantly as the total assets turnover ratio improved from 1.07 times in fiscal 2000 to 1.18 times in fiscal 2003. Furthermore, the ending balance of interest bearing loans was reduced by more than 350 billion yen to 1,277.1 billion yen. And net interest bearing liabilities, defined as interest bearing liabilities minus cash deposits, dropped by nearly 500 billion yen from fiscal 2000 to fiscal 2003. Likewise, the D/E ratio, when calculated on the basis of net interest bearing liabilities, moved from 1.11 times in fiscal 2000 to 1.04 times in fiscal 2003, contributing to the stability of our balance sheets.

On the other hand, our net worth ratio at market value was 34.4%, just half that of the level in fiscal 2000, reflecting the fact that our stock price remained relatively undervalued. In fiscal 2004, we will continue to strengthen our earnings, further solidify our financial condition, and strive to raise our market valuation.

(Billion Yen)

	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Net sales	5,255.1	5,484.4	5,006.9	4,617.5	4,766.8
Operating margin	2.9%	4.4%	-1.5%	2.2%	3.2%
Total assets	5,019.7	5,200.0	4,595.8	4,225.3	3,865.5
Total assets turnover ratio	(1.05 times)	(1.07 times)	(1.02 times)	(1.05 times)	(1.18 times)
Shareholders' equity	1,176.5	1,214.3	853.7	702.3	827.1
Shareholders' equity ratio	(23.4%)	(23.4%)	(18.6%)	(16.6%)	(21.4%)
Shareholders' equity ratio at market value	123.2%	63.5%	43.8%	15.2%	34.4%
Debt repayment period	3.6 years	2.7 years	5.7 years	15.0 years	4.2 years
Interest coverage ratio	9.6	12.2	7.1	3.9	13.0

(Billion Yen)

Interest bearing loans	1,725.0	1,636.2	1,760.6	1,763.7	1,277.1
Ending balance of net interest bearing loans	1,451.0	1,347.2	1,460.0	1,500.5	861.2
D/E ratio	1.47	1.35	2.06	2.51	1.54

(Billion Yen)

Cash flows from operating activities	477.0	596.4	306.5	117.7	304.0
Free cash flow	128.7	129.6	-102.8	53.3	371.4

(Note 1)

- Total assets turnover ratio: $\text{net sales} / \{(\text{ending balance of total assets in current period} + \text{ending balance of total assets in previous period}) / 2\}$
- Shareholders' equity ratio: $\text{balance of shareholders' equity} / \text{balance of total assets}$
- Shareholders' equity ratio at market value: $\text{total market capitalization} / \text{total assets}$
- Debt repayment period: $\text{balance of interest bearing loans} / \text{cash flows from operating activities}$
- Interest coverage ratio: $\text{cash flows from operating activities} / \text{interest paid}$
- Ending balance of net interest bearing loans: $\text{ending balance of interest bearing loans} - \text{ending balance of cash and cash equivalents}$
- D / E ratio: $\text{balance of interest bearing loans} / \text{balance of shareholders' equity}$

(Note 2) The above are all calculated based on consolidated financial data.