Management's Discussion and Analysis of Operations

The following section, Management's Discussion and Analysis of Operations, provides an overview of the consolidated financial statements of Fujitsu Limited (the "Company") and its consolidated subsidiaries (together, the "Group") for the year ended March 31, 2005 (fiscal 2004). Forward-looking statements in this section are based on management's understanding and best judgment as of March 31, 2005.

1. Analysis of Results

Business Environment

With regard to the business environment during fiscal 2004, overseas, the US and China experienced a temporary slowdown in growth as a result of surging oil prices and rising interest rates, but both these countries as well as Europe were able to maintain economic growth, and factors tempering growth appear to be easing. In Japan, there was a shift from the robust conditions that had prevailed in the digital consumer electronics sector until the beginning of the period, and the market for electronic components rapidly deteriorated, leading to a temporary flattening out of overall economic growth. Despite this, there appear to be prospects for a mild recovery in fiscal 2005.

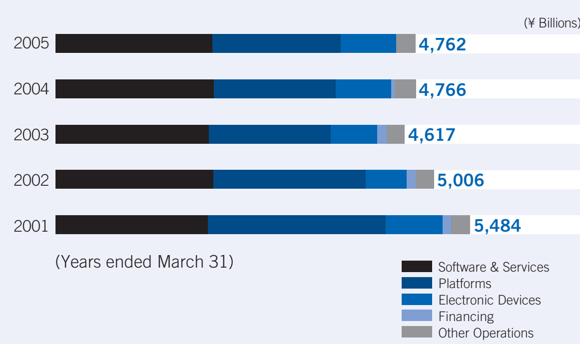
Looking at trends in IT investment, while the prospects for IT spending overseas appear to be bright, led by an aggressive spending posture among global corporations, in Japan the outlook varies according to industry, company size, or region, and there is a continuing lack of intensity overall. On the other hand, spending on open architecture IT infrastructure systems is enjoying strong growth in both qualitative and quantitative terms, and there is rapidly increasing demand for greater stability and efficiency in such systems. In addition, with more attention being paid to security issues as a result of the enactment of the Personal Information Protection Act in Japan this year, there is greater demand than ever for the capabilities that IT can deliver in supporting internal controls and other measures to enhance security. Consequently, an increase in IT spending on public infrastructure systems as well as by individual corporations can be expected.

In the world of ubiquitous networking, made possible by sophisticated IT infrastructure comprised of high-performance, high-reliability servers, networks and software seamlessly integrated in an open environment, it will be possible to securely and conveniently deliver advanced services in such areas as shopping, banking, and healthcare. As a leading provider of server and networking technology and services essential to the ubiquitous networking era, Fujitsu seeks to provide comprehensive solutions that bring together high-performance, high-quality products and services—such as biometric authentication technology for enhanced security—to meet the specific needs of individual customers.

Net Sales

Consolidated net sales for fiscal 2004 were ¥4,762.7 billion ($44,512 million), a decrease of 0.1% compared to the preceding fiscal year. On a continuing operations basis, excluding the impact of restructuring, this represented an increase of 2.8%. Deteriorating market conditions reduced sales of products such as plasma display panels (PDPs) and liquid crystal displays (LCDs), and in Japan, a sluggish recovery in IT spending restrained sales of servers and solutions/system integration services. Overseas, sales of outsourcing services, UNIX servers, optical transmission systems, PCs and compact hard disk drives (HDDs) improved.

Net Sales by Business Segment
(excluding intersegment)



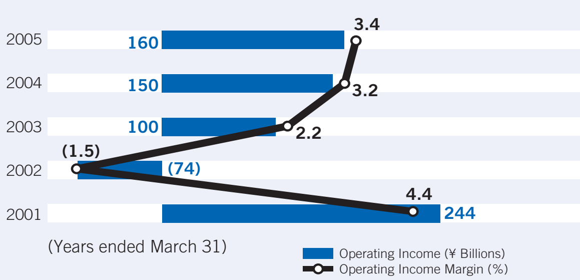
Cost of Sales, Selling, General & Administrative Expenses, and Operating Income

In fiscal 2004, the cost of sales rose ¥51.6 billion to ¥3,512.5 billion ($32,828 million), while selling, general and administrative (SG&A) expenses declined ¥65.5 billion to ¥1,090.0 billion ($10,187 million).

The cost of sales ratio deteriorated by 1.2 percentage points from the prior fiscal year to 73.8%, while the ratio of SG&A expenses to net sales improved by 1.4 percentage points to 22.8% as a result of increased efficiency, benefits from restructuring carried out primarily at overseas operations and the reclassification of certain subsidiaries as equity method affiliates. As a result of the foregoing, the overall operating income margin rose by 0.2 percentage points.

Operating income was ¥160.1 billion ($1,497 million), up ¥9.8 billion over the previous fiscal year. Although operating income was adversely impacted by lower prices and losses on projects with deteriorating profitability in the Software & Services segment, in the Platforms and Electronic Devices segments, despite intense price competition, operating income grew as a result of increased sales, progress on cost-cutting and expense controls.

Operating Income and Operating Income Margin



Other Income (Expenses) and Net Income

Other income, net of other expenses, totaled ¥63.3 billion ($592 million). Net interest, comprising interest and dividend income and interest charges, resulted in a loss of ¥9.6 billion ($90 million), an improvement of ¥7.0 billion mainly owing to a decrease in interest-bearing loans. Equity in earnings of affiliates, net was ¥3.6 billion ($34 million), an increase of ¥4.5 billion from a loss posted last year. Amortization of unrecognized obligation for retirement benefits was ¥39.2 billion ($367 million), an improvement of ¥17.6 billion due to an increase in stock prices last year and the transfer of the substitutional portion of employees' pension funds.

Besides the previously mentioned items, other income (expenses), during fiscal 2004 included gains from the sales of marketable securities to bolster our financial position, as well as on the transfer of the PDP business. Details are as follows:

- **Gain on sales of marketable securities**
  . . . . ¥133.2 billion ($1,246 million)

Sales of part of our holdings in Fanuc Ltd. and Advantest Corporation on February 22 and 23, 2005 (¥129.2 billion) were recorded as gain on sales of marketable securities.

- **Gain on business transfer**
  . . . . ¥36.5 billion ($341 million)

A formal agreement was reached on March 25, 2005 for the transfer of our PDP business to joint venture partner Hitachi, Ltd. We recognized proceeds from this and other business transfers as gain on business transfer.

- **Restructuring charges**
  . . . . ¥20.0 billion ($188 million)

Restructuring charges were recorded as expenses relating to reductions and relocation of personnel and disposal of assets primarily at domestic manufacturing subsidiaries.

- **Real estate valuation losses**
  . . . . ¥15.2 billion ($143 million)

Valuation losses on idle property holdings were reported.

We recognized ¥185.5 billion ($1,734 million) as income taxes, which combines current and deferred income taxes, against ¥223.5 billion ($2,089 million) of income before income taxes and minority interests. The income taxes included a valuation allowance of ¥93.5 billion ($874 million) for deferred tax assets, in addition to normal tax expenses.

Having significant tax loss carryforwards from the restructuring of operations since fiscal 2001, we calculated deferred tax assets at fiscal year-end based on projected future taxable income. At that time, in light of the delayed recovery of taxable income primarily from the Company's business operations, we recorded a valuation allowance to cover the amount in excess of what we were likely to recover, as based on estimates of the next fiscal year's taxable income.

After deducting minority interests of ¥6.0 billion ($57 million), net income for the year was ¥31.9 billion ($298 million), a decrease of ¥17.7 billion from the prior fiscal year.

2. Segment Information

Net sales below refer to sales to unaffiliated customers.

Business Segment Information

Although operating income in the Software & Services segment declined sharply in fiscal 2004, the opposite was true for the Platforms segment, where income was substantially higher. The Electronic Devices segment also saw income growth.

Software & Services

Consolidated net sales were ¥2,070.4 billion ($19,350 million), roughly on par with fiscal 2003 when excluding the impact of that fiscal year's restructuring of overseas subsidiaries. Sales in Japan decreased, primarily due to the slow recovery in IT investment, sluggish sales in solutions/systems integration services, and a reduction in earnings from public infrastructure systems deals. Overseas, buoyed by successive large-scale government-sector outsourcing wins by Fujitsu Services in the UK, orders and sales steadily increased, with sales rising 9.8% on a continuing operations basis.

Consolidated operating income in this segment declined by ¥25.7 billion to ¥113.0 billion ($1,057 million). Increased earnings from large-scale government-sector outsourcing deals by Fujitsu Services in the UK and the benefits of last year's restructuring of Fujitsu Consulting in the US led to improved results at each of these subsidiaries. In the domestic solutions/systems integration business, however, development costs significantly increased for projects with deteriorating profitability, resulting in a substantial drop in operating income.

Along with an increase in losses related to loss-generating projects completed during fiscal 2004 that far surpassed previous-year estimates, we also booked unexpected additional losses for projects scheduled to be completed in fiscal 2005 and beyond. In an effort to maintain delivery schedules and quality on large-scale loss-generating projects, development resources were diverted to these projects throughout the period. The result was a decline in overall efficiency in our solutions/systems integration business.

As of the end of March 2005, the balance of the reserve for losses on loss-generating projects that will be completed in fiscal 2005 or beyond was ¥28.0 billion ($262 million). Of the loss-generating projects uncovered to date, approximately 75% on a value basis were completed by the end of fiscal 2004, and of the projects expected to be completed in fiscal 2005, the majority are expected to involve systems that begin operation by the third quarter of fiscal 2005. Moreover, the major portion of losses sustained to date have been on projects that were contracted and on which development work began prior to the end of the first half of fiscal 2003. For projects initiated since the second half of fiscal 2003, at which time we implemented comprehensive countermeasures starting from the initial project discussion phase, the incidence of losses has dramatically declined.

Reviewing the concrete measures implemented to date to improve project risk management procedures, in February 2004 we established an organization to review project business discussions at every stage in order to prevent the occurrence of loss-generating projects. Since that time we have expanded our organizational resources in this area, strengthening our project risk management organization and reforming our contractual procedures. In April 2005, we established a new Systems Integration Assurance Unit with broader authority that reports directly to the president in order to further enhance our procedures to prevent the occurrence of problematic projects. We have also implemented a real-time project management tracking system and, since the beginning of fiscal 2005, have been applying the percentage of completion method to all software development contracts in order to maximize project visibility.

In June 2004, we realigned our solutions business organization in Japan by unifying our sales and systems engineering groups along customer lines. Along with reforming our organization and approach to more quickly respond to our customers' changing business environments, this has clarified organizational responsibility for ensuring project profitability from the order stage. We also restructured and consolidated our systems engineering companies in the Tohoku, Shikoku, and Chugoku regions. As a result, we expect considerable improvement in the profitability of systems integration projects going forward.

In addition, in order to augment full IT system lifecycle management (LCM) support for customers, in October 2004 we made Fujitsu Support and Service Inc. a wholly owned subsidiary of Fujitsu Limited through an exchange of shares. In January 2005, we consolidated into a single location nearly 2,500 employees of both companies who had previously been dispersed in multiple centers throughout the Tokyo metropolitan area, and we consolidated redundant service centers in regional locations throughout Japan.

Continual cost reductions are essential in order to meet customer expectations regarding pricing. Accordingly, we intend to expand the utilization of our SDAS comprehensive system development framework to all new deals, and thoroughly improve efficiency by reducing development times and other measures. Moreover, we intend to intensify the use of custom-made development tools like our TRIOLE templates, which provide pre-verified system construction patterns for open environments and greatly improve overall system reliability.

Platforms

Consolidated net sales in the Platforms segment grew 6.0% over the previous fiscal year to ¥1,705.1 billion ($15,936 million). Sales of UNIX servers overseas were strong, particularly in Europe and North America, and sales of transmission systems, primarily to European and North American telecommunications carriers, showed double-digit growth. Although sales of PCs in Japan were sluggish, primarily as a result of intense pricing competition in the retail sector, overseas sales of high-function, high-quality notebook computers registered especially large gains. Sales of our HDDs (for use in notebook computers and servers), which enjoy a reputation in the marketplace for high quality and excellent reliability, also showed significant growth, especially overseas.

Operating income for the sector nearly doubled from the previous year, increasing by ¥25.7 billion to ¥55.0 billion ($514 million). Continued progress was made in lowering costs through improvements in manufacturing processes as well as reducing development costs and increasing efficiencies for such products as optical transmission systems, IP networks and servers. Amid declining prices and increasing volumes in PCs, we made further efforts to increase efficiencies in our manufacturing and delivery infrastructure and to lower procurement costs for components. However, with the deployment of financial terminals to accommodate new Japanese banknotes having run its course, profitability declined in the Server-related sub-segment, and although sales of new mobile phone handsets increased with the shift to third-generation (3G) communications under way in Japan, equipping the new handsets with sophisticated functionality delayed cost reductions and adversely impacted profitability in this area.

In June 2004, we began global sales of new UNIX servers equipped with 64-bit processors employing our leading-edge 90nm semiconductor technology. In April 2005 we announced the global launch of PRIMEQUEST, our new mission-critical IA server with mainframe-class performance and reliability. Providing the economy of an open architecture server together with the high reliability of a mainframe computer, PRIMEQUEST breaks new ground as the world's most powerful open architecture server in the mission-critical space.

Based on a strategy of active collaboration with global partners in order to help strengthen our business, in fiscal 2004 we worked with IBM to establish standards for autonomic system technology, with Cisco Systems in routers and switches, with Intel and Microsoft in the IA server field, and with Sun Microsystems in the area of UNIX servers.

In the hard disk drive business, we merged the operations of our drive-head assembly division in the Philippines with TDK's subsidiary in the same country, and the new entity began operation in December 2004. This move helps to ensure an adequate supply of drive heads to meet future surges in demand.

In light of the Personal Information Protection Act that came into effect in Japan in April 2005 and recent increases in counterfeit credit card-related crimes, there are growing calls for technology solutions to help protect information security. Our pioneering palm vein recognition technology has been adopted by many financial institutions for use in their ATMs, and a number of these systems are already in operation.

Electronic Devices

Consolidated net sales in this segment were ¥733.8 billion ($6,859 million), an increase of 4.6% over the previous year on a continuing operations basis excluding the impact of restructuring. Although price competition in PDPs and LCDs intensified as a result of deterioration in the market supply/demand balance, increased orders for leading-edge products and strong sales by our components subsidiaries contributed to the overall increase in sales.

Operating income was ¥32.5 billion ($305 million), an increase over last year of ¥5.0 billion. Continuing progress in improving manufacturing efficiency and increased revenue from components subsidiaries offset the impact of lower sales of PDPs, LCDs and other products, contributing to the overall increase in operating income.

In February 2005, pilot testing was completed at our new Mie Plant facility for the mass production of 300mm wafers utilizing our leading-edge 90nm and 65nm process technology, and operations officially commenced in April. With market demand for leading-edge technology continually increasing, the plant is steadily progressing toward the start of volume production planned for September 2005.

In March 2005, we reached formal agreement with Hitachi, Ltd. regarding the transfer of our PDP operations. Accordingly, we transferred to Hitachi, Ltd. a portion of the stock we held in Fujitsu Hitachi Plasma Display Ltd., as well as certain intellectual property relating to PDPs. In addition, in April 2005 we signed an agreement with Sharp Corporation for the transfer of our LCD business.

Through the transfer of these flat panel display businesses, we will be better able to concentrate resources on LSI devices to more effectively grow that business.

Other Operations

In June 2004, we sold our logistics subsidiary to a Japan-based subsidiary of Exel plc of the UK. By capitalizing on ties with Exel, we are bolstering our global logistics framework and achieving more advanced SCM in a drive to deliver products faster and more reliably than ever to Fujitsu customers.

Net Sales and Operating Income by Business Segment

(including intersegment)

(¥ Billions)

Years ended March 31	2004	**2005**	Increase (Decrease) Rate (%)
Net sales			
Software & Services	¥2,146	**¥2,108**	(1.7)
Platforms	1,832	**1,861**	1.6
Electronic Devices	804	**794**	(1.2)
Financing	54	**—**	—
Other Operations	418	**352**	(15.8)
Intersegment elimination	(489)	**(354)**	
Consolidated net sales	¥4,766	**¥4,762**	(0.1)

Years ended March 31	2004	**2005**	Increase (Decrease)
Operating income (loss)			
Software & Services	¥138	**¥113**	¥(25)
Platforms	29	**55**	25
Electronic Devices	27	**32**	5
Financing	2	**—**	(2)
Other Operations	13	**14**	0
Unallocated operating costs and expenses/ intersegment elimination	(60)	**(54)**	6
Consolidated operating income	¥150	**¥160**	¥ 9

Geographic Segment Information

Japan

Net sales were ¥3,560.9 billion ($33,280 million), a decline of 1.2% year on year. Excluding the impact of business realignment in the previous fiscal year, which resulted in the reclassification of our Flash memory, leasing, and other businesses as equity method affiliates, net sales rose 1.5% on a continuing operations basis. Sales were also higher for system-on-chip devices used in base stations for 3G mobile communications systems and digital home appliances.

Operating income was ¥187.8 billion ($1,756 million), ¥15.8 billion lower than the previous year, mainly due to a drop in income caused by deteriorating performance in Software & Services and PDPs.

Europe

Net sales were ¥585.1 billion ($5,469 million), up 7.4% year on year and 12.1% higher on a continuing operations basis. This result stemmed from increased sales from large-scale government-sector outsourcing contracts in the UK, and from business targeting telecommunications carriers.

Operating income was ¥11.7 billion ($109 million), nearly double the previous year's figure. This reflected the benefits of higher sales in Software & Services and communications equipment.

The Americas

Net sales were ¥281.9 billion ($2,635 million), a year-on-year increase of 10.8%, and 15.5% higher on a continuing operations basis.

Operating income was ¥4.3 billion ($41 million), reversing the previous year's operating loss of ¥13.1 billion. Earnings increased on the back of benefits from the previous year's restructuring initiatives, improved results from optical transmission systems, and healthy performance from HDDs.

Others

Net sales declined 7.6% year on year, to ¥334.7 billion ($3,128 million), and 6.5% on a continuing operations basis. This was largely due to a deteriorating LCD market. Operating income was ¥12.1 billion ($113 million), down ¥1.3 billion.

Net Sales and Operating Income by Geographic Segment

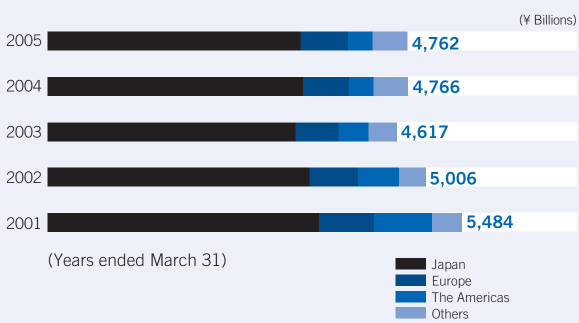
(including intersegment)

(¥ Billions)

Years ended March 31	2004	**2005**	Increase (Decrease) Rate (%)
Net sales			
Japan	¥4,071	**¥4,024**	(1.2)
Europe	563	**596**	6.0
The Americas	274	**298**	8.8
Others	579	**602**	4.1
Intersegment elimination	(721)	**(760)**	
Consolidated net sales	¥4,766	**¥4,762**	(0.1)

Years ended March 31	2004	**2005**	Increase (Decrease)
Operating income (loss)			
Japan	¥203	**¥187**	¥(15)
Europe	6	**11**	5
The Americas	(13)	**4**	17
Others	13	**12**	(1)
Unallocated operating costs and expenses/ intersegment elimination	(60)	**(55)**	4
Consolidated operating income	¥150	**¥160**	¥ 9

■ For reference: Net Sales by Customers' Geographic Location



3. Capital Resources and Liquidity

Improvement in Financial Strength

As a result of the deterioration of performance following the collapse of the IT bubble and the large charges stemming from restructuring initiatives, there had been significant deterioration in the Group's financial condition. However, since fiscal 2003, we have made progress in improving the soundness of our financial position. We were able to meet our goal of reducing interest-bearing loans to ¥1,100 billion or below by the end of fiscal 2004, ending the fiscal year with a balance of ¥1,082.7 billion ($10,120 million) as a result of cash flow generated from business operations as well as investment cash flow collected from sales of asset holdings. As a result, our D/E ratio reached 1.26, drawing closer to our medium-term goal of 1.0. Net interest-bearing loans, which subtract cash and time deposits, were greatly reduced to ¥628.0 billion ($5,870 million), and the net D/E ratio reached 0.73. In terms of management indices expressing financial stability and efficient use of assets, in a number of areas we have exceeded the values for the recent peak year of fiscal 2000.

We have also made efforts to deal with financial risks. In the same way that we did in the previous fiscal year, in fiscal 2004 we recognized upfront losses for problematic projects as soon as they were determined, including for work not yet implemented. In addition, we recorded valuation losses on idle property that we had no plans to use. Moreover, with respect to deferred tax assets, we recorded a valuation allowance to cover the amount in excess of what we are likely to recover in the future.

Assets, Liabilities and Shareholders' Equity

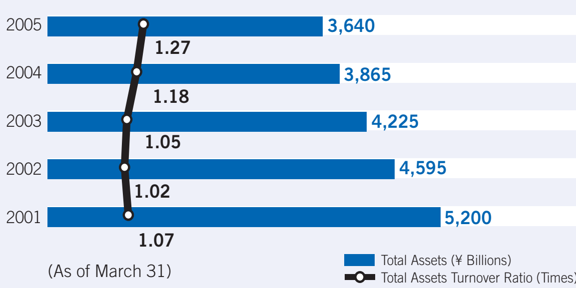
Total assets at the end of fiscal 2004 were ¥3,640.1 billion ($34,021 million), a reduction of ¥225.3 billion from the end of the previous fiscal year. Total current assets were ¥1,981.5 billion ($18,519 million), a reduction of ¥34.0 billion from the end of the last fiscal year. Inventories were reduced, mainly due to increased efforts in manufacturing innovation.

Total fixed assets decreased by ¥191.3 billion from the end of the prior fiscal year, to ¥1,658.6 billion ($15,502 million). Property, plant, and equipment less accumulated depreciation decreased by ¥75.1 billion, due to such factors as the shift to the equity method of accounting for our compound semiconductor business and the transfer of our PDP business. Investments and long-term loans were reduced by ¥120.5 billion as a result of sales of marketable securities and the posting of a valuation allowance for deferred tax assets.

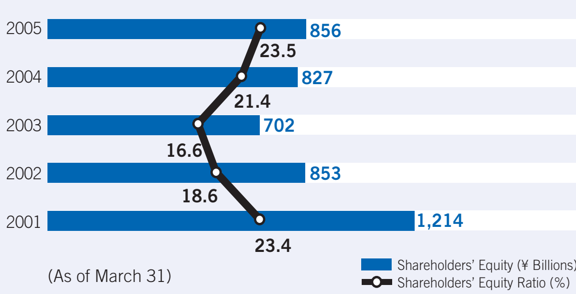
Total liabilities, which include current and long-term liabilities, were ¥2,619.0 billion ($24,477 million), a reduction of ¥228.9 billion compared to the end of the prior fiscal year. Reflecting primarily corporate bond redemptions and repayment of borrowings, interest-bearing loans were reduced by ¥194.3 billion. Along with this, we improved our D/E ratio by 0.28 to 1.26.

Total shareholders' equity increased by ¥29.8 billion, to ¥856.9 billion ($8,009 million). In addition to recording a net profit for the fiscal year, capital surplus increased in conjunction with making Fujitsu Support and Service a wholly owned subsidiary via an exchange of shares. The shareholders' equity ratio increased by 2.1 percentage points to 23.5%.

■ Total Assets/Total Assets Turnover Ratio



■ Shareholders' Equity/Shareholders' Equity Ratio



Summary of Cash Flows

Net cash provided by operating activities during the fiscal year was ¥277.2 billion ($2,591 million), roughly in line with the approximately ¥300 billion recorded in fiscal 2003. Internal reserve increased due to a significant increase in profit excluding some special items whereas working capital decreased due to such factors as the payment of accounts payable in our domestic solutions/systems integration business.

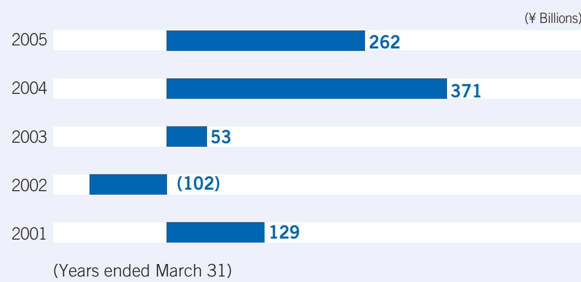
Net cash used in investing activities was ¥15.1 billion ($141 million). Outflows for capital expenditures roughly balanced out inflows from sales of marketable securities.

Free cash flow, the sum of operating and investing cash flows, was a positive ¥262.1 billion ($2,450 million) and was used to redeem corporate bonds and repay borrowings.

Net cash used in financing activities was ¥212.0 billion ($1,982 million). Excluding items such as proceeds from the sales of marketable securities, free cash flow from our business operations was positive ¥93.7 billion ($876 million), an increase in cash inflows of ¥4.6 billion over the previous fiscal year.

Cash and cash equivalents stood at ¥454.5 billion ($4,248 million) at the end of the period, ¥40.6 billion more than at year-end in fiscal 2003.

■ Free Cash Flow



4. Capital Expenditure

In fiscal 2004, capital expenditure, which was targeted at the most promising growth sectors and held within the same range as depreciation expenses, totaled ¥181.4 billion ($1,695 million). By business segment, capital expenditure was ¥49.4 billion ($462 million) in Software & Services, ¥36.6 billion ($342 million) in Platforms, ¥76.1 billion ($711 million) in Electronic Devices, and ¥19.1 billion ($179 million) for general corporate and other areas.

Capital Expenditure

(¥ Billions)

Years ended March 31	2004	2005	Increase (Decrease) Rate (%)
Software & Services	¥ 54	**¥ 49**	(8.5)
Platforms	32	**36**	12.9
Electronic Devices	59	**76**	28.4
Corporate and others*	13	**19**	37.3
Total	¥159	**¥181**	13.5
Japan	135	**142**	5.2
Overseas	24	**39**	59.7

* Non-allocable capital expenditure for shared R&D and parent company management division

5. Consolidated Subsidiaries

At the end of fiscal 2004, the Company had 403 consolidated subsidiaries, 123 in Japan and 280 overseas, representing a decrease of 52 from last year's total of 455. The decrease included the transfer of our PDP operations and the shift of our compound semiconductor subsidiary to the equity method of accounting, as well as reductions relating to global business restructuring and the realignment of our systems engineering subsidiaries in Japan's Chugoku and Shikoku regions.

The number of affiliated companies accounted for by the equity method as of the fiscal year-end totaled 34, a net increase of two. This number included Eudyna Devices Inc., Eudyna Devices Europe Ltd. and two other new equity method affiliates, while Advantest Corporation and one other company are no longer treated as equity method affiliates.

6. Critical Accounting Policies and Estimates

Accounting Principles and Practices

The accompanying consolidated financial statements of the Group have been prepared in accordance with accounting principles and practices generally accepted in Japan and the regulations under the Securities and Exchange Law of Japan. The accounting principles and practices adopted by the consolidated subsidiaries outside Japan conform to those of their respective countries.

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the amount of the assets, liabilities, contingent assets and contingent liabilities reported at the end of the fiscal year as well as the amount of revenue and expenses recognized during that term. Actual results may differ from these estimates.

The Group is discussing the requirements for the adoption of International Financial Reporting Standards. When these standards are adopted, it is possible that differences may arise from financial statements prepared under Japanese standards.

Revenue Recognition

Revenue from sales of IT systems and products, including software development contracts, is recognized upon acceptance by the customers, whereas revenue from sales of personal computers, other equipment and electronic devices is recognized when the products are shipped.

We stringently assess the potential revenue recoverable on projects for which estimated costs have exceeded estimated revenue, and recognize as losses the amounts assessed as non-recoverable. If the estimated costs relating to such contracts increase further in the future, additional losses may be recognized.

In fiscal 2005, we plan to introduce the percentage of completion method to recognize revenue and to improve the visibility of project management for software development contracts.

Property, Plant and Equipment

Property, plant and equipment are carried at cost. Depreciation is computed principally by the declining-balance method at rates based on the estimated useful lives of the respective assets, which vary according to their general classification, type of construction and function. In the future, some equipment and facilities may become obsolete as a result of technical innovation or other factors, and some equipment and facilities may no longer be required as the result of withdrawal from certain businesses, in which case their actual useful lives may become less than their originally estimated useful lives. Losses may occur as a result.

We have not adopted in advance the impairment accounting standard that will become mandatory in fiscal 2005 in Japan. Accordingly, following application of the standard, impairment losses may have to be recognized in cases in which there is a decline in the anticipated amount of future cash flows as a result of deterioration in the projected results of a business unit, or a decline in the fair market value of property, plant and equipment, leading to a corresponding decline in the amounts judged to be recoverable.

Intangible Assets

Computer software for sale is amortized based on projected unit sales volume during the period for which the projections are made. The projected unit sales volume is estimated based on a feasible sales plan, but losses may occur if anticipated unit sales fall short of the original sales plan.

Computer software for internal use is amortized by the straight-line method over its estimated useful life. Losses may occur if the actual useful life falls short of the initially estimated useful life.

Goodwill

Goodwill arising from the acquisition of a business is amortized by the straight-line method over the period corresponding to the premium of the acquired business. Losses may be recognized when the business is withdrawn or sold by the Group, or when the profitability of the acquired business decreases during the period the Group expected the return.

Marketable Securities

Held-to-maturity investments, which are the debt securities which the Group has the positive intent and ability to hold to maturity, are stated at amortized cost, adjusted for the amortization of premium or discount to maturity. Available-for-sale securities, which are "equity securities" or "debt securities not classified as held-to-maturity," are carried at fair market value as of the balance sheet date of the fiscal year if a market price is available. If no market price is available, they are carried at cost based on the moving average method. Fluctuations in the market value of available-for-sale securities for which market prices are available cause fluctuations in the carrying value of marketable securities, resulting in increases or decreases in shareholders' equity. Impairment losses are recognized on available-for-sale securities when the market value or the net worth falls significantly and is proved to be unrecoverable. If a significant decline in market value occurs and is proved to be unrecoverable in the future, additional impairment losses may need to be recognized.

Deferred Tax Assets

In fiscal 2001 and 2002, the Group posted large losses as a result of a deterioration in operating performance and related business restructuring charges. With respect to the timing difference on tax loss carryforwards and others, an estimate has been made of the amount of the deferred tax assets within the extent of which the Group judges to be recoverable over the next five years. By recording a valuation allowance for the amount exceeding the projected recoverable amount, an appropriate level of deferred tax assets is recorded. Future increases or decreases in the valuation allowance may be made if projected taxable income decreases or increases as a result of trends in future results. The deferred tax asset is recognized based on the statutory tax rate. Future revisions in the tax rate would result in increases or decreases of the deferred tax asset.

Retirement Benefits

Retirement benefit costs and obligations are determined based on certain actuarial assumptions. These assumptions include the discount rate, rates of retirement, death rates, and the expected rate of return on the plan assets. The discount rate for the Company and its domestic subsidiaries is estimated based on the market rate of return in Japan for long-term corporate bonds of a certain rating. The expected rate of return is estimated based on the weighted average of the expected rates of return for each type of asset in which the pension funds are invested. When actual results differ from the assumptions or when the assumptions are changed, retirement benefit costs and obligations can be affected. In the event an actuarial loss arises, the actuarial loss is amortized using a straight-line method over employees' average remaining service period.

Retirement benefit costs and obligations are recognized in conformity with the accounting principles and standards generally accepted in the respective countries where incurred. Any future revisions to these accounting standards could impact the recognized retirement benefit costs and obligations as well as shareholders' equity.

Provision for Loss on Repurchase of Computers

Certain computers manufactured by the Group are sold to Japan Electronic Computer Co., Ltd. (JECC) and other leasing companies for leasing to the ultimate users under contracts that require the repurchase of the computers if they are returned by the users after a certain period. Based on past experience, an estimated amount for the loss arising from such repurchases is provided at the point of sale and is recorded as a provision. If there are future changes in the usage trends of the ultimate users, there may need to be additions or reductions to the provision.