

# Japan Vilene Company, Ltd. and Consolidated Subsidiaries

## Notes to Consolidated Financial Statements Years Ended March 31, 2004 and 2003

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### 1. BASIS OF PRESENTING CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements of Japan Vilene Company, Ltd. (the "Company") and its consolidated subsidiaries have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with accounting principles generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the Company's consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications and rearrangements have been made in the 2003 financial statements to conform to classifications and presentations used in 2004.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which the Company is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥106 to \$1, the approximate rate of exchange at March 31, 2004. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Consolidation**—The accompanying consolidated financial statements as of March 31, 2004 include the accounts of the Company and its significant subsidiaries (together the "Companies"). Consolidation of the remaining subsidiaries would not have a material effect on the accompanying consolidated financial statements.

Under the control or influence concept, those companies in which the Company, directly or indirectly, is able to exercise control over operations are fully consolidated, and those companies over which the Companies have the ability to exercise significant influence are accounted for by the equity method.

Investments in seven associated companies are accounted for by the equity method. Investments in the remaining unconsolidated subsidiaries and associated companies are stated at cost.

The accounts of foreign consolidated subsidiaries are included on the basis of their fiscal year end of December 31. All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profits included in assets resulting from transactions within the Companies are eliminated.

**Cash and Cash Equivalents**—Cash equivalents are short-term investments that are readily convertible into cash and exposed to insignificant risk of changes in value. Cash equivalents include time deposits and certificate of deposits, all of which mature or become due within three months of the date of acquisition.

**Inventories**—Inventories of the Company are stated at average cost. Inventories of consolidated subsidiaries are stated at the latest purchase cost or at the lower of cost (first-in, first-out) or market.

**Investment Securities**—Marketable and investment securities are classified and accounted for, as available-for-sale securities, which are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported as a separate component of shareholders' equity.

Non-marketable available-for-sale securities are stated at cost determined by the moving-average method. For other than temporary declines in fair value, investment securities are reduced to net realizable value by a charge to income.

**Property, Plant and Equipment**—Property, plant and equipment are stated at cost. Significant renewals and additions are capitalized; maintenance and repairs are charged to income as incurred.

Depreciation of property, plant and equipment is principally computed by the declining-balance method except for buildings. The Company uses the straight-line method for depreciation of buildings. The domestic consolidated subsidiaries use the straight-line method for depreciation of buildings acquired after March 31, 1998. The declining-balance method was used for buildings acquired prior to April 1, 1998. Depreciation of property, plant and equipment of foreign consolidated subsidiaries is principally computed by the straight-line method.

The ranges of the estimated useful lives of the assets used for the computation of depreciation are as follows:

Buildings and structures	3 to 50 years
Machinery and equipment	2 to 15 years
Vehicles	2 to 10 years
Tools, furniture and fixtures	2 to 20 years

**Leases**—All leases of the Companies are accounted for as operating leases. Under the Japanese accounting standard for leases, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the lessee's financial statements.

**Income Taxes**—The provision for income taxes is computed based on the pretax income included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

The Company and certain domestic subsidiaries file a tax return under the consolidated corporate-tax system from the fiscal year ended March 31, 2003, which allows companies to base tax payments on the combined profits or losses of the parent company and its wholly owned domestic subsidiaries. Under the consolidated corporate-tax system, a surcharge tax of 2% of taxable income is levied in addition to the national corporate income tax rate for the fiscal years ended March 31, 2004 and 2003.

**Pension and Retirement Benefits Plans**—Effective April 1, 2000, the Company and domestic consolidated subsidiaries adopted a new accounting standard for employees' retirement benefits and accounted for the liability for retirement benefits based on projected benefit obligations and plan assets at the balance sheet date.

The provision for retirement benefits to directors and corporate auditors is made at the amount which would be paid in accordance with company bylaws if they retired at each balance sheet date. Such plan is not funded.

***Appropriations of Retained Earnings***—Appropriations of retained earnings are reflected in the financial statements for the following year upon shareholders' approval. Payments of bonuses to directors and corporate auditors as approved by the shareholders are accounted for as appropriations of retained earnings.

***Translation of Foreign Currency Transactions***—All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the current exchange rate at the balance sheet date. The foreign exchange gains and losses from translation are recognized in the consolidated statements of income to the extent that they are not hedged by forward exchange contracts. Forward exchange contracts are separately accounted for in accordance with the accounting standard for financial instruments.

***Translation of Foreign Currency Financial Statements***—The balance sheet accounts of the foreign consolidated subsidiaries are translated into Japanese yen at the current exchange rate at the balance sheet date except for shareholders' equity, which is translated at the historical rates. Differences arising from such translation were shown as "Foreign currency translation adjustments" in a separate component of shareholders' equity. Revenue and expense accounts of foreign consolidated subsidiaries and associated companies are also translated into Japanese yen at the current exchange rate at the balance sheet date.

***Derivatives and Hedging Activities***—The Company uses derivative financial instruments to manage its exposures to fluctuations in foreign exchange and interest rates. Foreign exchange forward contracts, interest rate swap contracts are utilized by the Company to reduce foreign currency exchange and interest rate risks. The Company does not enter into derivatives for trading or speculative purposes.

Derivative financial instruments and foreign currency transactions are classified and accounted for as follows: (1) all derivatives are recognized as either assets or liabilities and measured at fair value, and gains or losses on derivative transactions are recognized in the statement of income and (2) for derivatives used for hedging purposes, if derivatives qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, gains or losses on derivatives are deferred until maturity of the hedged transactions.

The foreign currency forward contracts employed to hedge foreign exchange exposures for export sales and import purchases are measured at fair value and the unrealized gains or losses are recognized in income. Forward contracts designated as hedging forecasted (or committed) transactions are also measured at the fair value but the unrealized gains or losses are deferred until the underlying transactions are completed.

The interest rate swap contracts which qualify for hedge accounting and meet specific matching criteria are not remeasured at market value but the differential paid or received under the swap agreements is recognized and included in interest expense or income.

***Per Share Information***—Basic net income per share is computed by dividing net income available to common shareholders, by the weighted-average number of common shares outstanding for the period, retroactively adjusted for stock splits.

Diluted net income per share reflects the potential dilution that could occur if securities were exercised or converted into common stock. Diluted net income per share of common stock assumes full conversion of the outstanding convertible bonds at the beginning of the year with an applicable adjustment for related interest expense, net of tax, and full exercise of outstanding warrants.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends of the Company applicable to the respective years including dividends to be paid after the end of the year.

**New Accounting Pronouncements**—In August 2002, the Business Accounting Council issued a Statement of Opinion, "Accounting for Impairment of Fixed Assets," and in October 2003 the Accounting Standards Board of Japan ("ASB") issued ASB Guidance No. 6, "Guidance for Accounting Standard for Impairment of Fixed Assets." These new pronouncements are effective for fiscal years beginning on or after April 1, 2005 with early adoption permitted for fiscal years ending on or after March 31, 2004.

The new accounting standard requires an entity to review its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

The Company is currently in the process of assessing the effect of adoption of these pronouncements.

### 3. INVESTMENT SECURITIES

Investment securities at March 31, 2004 and 2003, consisted of the following:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Non-current—Investment securities:			
Marketable equity securities	¥ 675	¥ 867	\$ 6,368
Trust fund investments		62	
Investments in unconsolidated subsidiaries and associated companies	4,631	4,616	43,689
Other	<u>239</u>	<u>238</u>	<u>2,254</u>
Total	<u>¥5,545</u>	<u>¥5,783</u>	<u>\$52,311</u>

Marketable equity securities included an investment in Dainippon Ink and Chemicals, Incorporated in the amount of ¥382 million in 2003, which represented 0.25% of its outstanding shares for 2003. Dainippon Ink and Chemicals, Incorporated owned 22.80% of the Company's outstanding shares in 2004 and 2003.

Information regarding the securities classified as available-for-sale at March 31, 2004 and 2003, was as follows:

	Millions of Japanese Yen			
	2004			
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Securities classified as available-for-sale equity securities	<u>¥491</u>	<u>¥184</u>	<u>¥1</u>	<u>¥674</u>
Total	<u>¥491</u>	<u>¥184</u>	<u>¥1</u>	<u>¥674</u>

	Thousands of U.S. Dollars			
	2004			
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Securities classified as available-for-sale equity securities	<u>\$4,632</u>	<u>\$1,735</u>	<u>\$9</u>	<u>\$6,358</u>
Total	<u>\$4,632</u>	<u>\$1,735</u>	<u>\$9</u>	<u>\$6,358</u>

	Millions of Japanese Yen			
	2003			
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Securities classified as available-for-sale:				
Equity securities	<u>¥861</u>	<u>¥44</u>	<u>¥38</u>	<u>¥867</u>
Trust fund investments	<u>62</u>	<u>—</u>	<u>—</u>	<u>62</u>
Total	<u>¥923</u>	<u>¥44</u>	<u>¥38</u>	<u>¥929</u>

Other investment securities whose fair value was not readily determinable as of March 31, 2004 and 2003, were as follows:

	Carrying Amount		
	Millions of Japanese Yen	Thousands of U.S. Dollars	
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Other investment securities:			
Associated companies	<u>¥4,422</u>	<u>¥4,448</u>	<u>\$41,717</u>
Other	<u>449</u>	<u>406</u>	<u>4,236</u>
Total	<u>¥4,871</u>	<u>¥4,854</u>	<u>\$45,953</u>

Proceeds from sales of available-for-sale securities for the years ended March 31, 2004 and 2003, were ¥444 million (\$4,189 thousand) and ¥2 million, respectively. Gross realized gains on these sales, computed on the moving average cost basis, were ¥114 million (\$1,075 thousand) for the year ended March 31, 2004. For 2003, no such gains were recorded.

#### 4. INVENTORIES

Inventories at March 31, 2004 and 2003, consisted of the following:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Merchandise	¥1,005	¥ 935	\$ 9,481
Finished goods	2,719	2,752	25,651
Work in process	436	530	4,113
Raw materials and supplies	<u>1,159</u>	<u>1,171</u>	<u>10,934</u>
Total	<u>¥5,319</u>	<u>¥5,388</u>	<u>\$50,179</u>

#### 5. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at March 31, 2004 and 2003, consisted of the following:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Land	¥ 4,273	¥ 4,713	\$ 40,311
Buildings and structures	19,792	19,777	186,717
Machinery and equipment	32,813	33,270	309,557
Vehicles	383	397	3,613
Tools, furniture and fixtures	5,233	5,305	49,368
Construction in progress	<u>173</u>	<u>257</u>	<u>1,632</u>
Total	<u>¥62,667</u>	<u>¥63,719</u>	<u>\$591,198</u>

Depreciation expense amounted to ¥2,010 million (\$18,962 thousand) and ¥2,308 million for the years ended March 31, 2004 and 2003, respectively.

#### 6. LEASES

The Companies lease certain office equipment and vehicles under long-term noncancelable lease agreements.

Total rental expenses for the years ended March 31, 2004 and 2003, were ¥209 million (\$1,972 thousand) and ¥281 million, respectively, including ¥122 million (\$1,151 thousand) and ¥167 million of lease payments under finance leases.

Pro forma information of leased property such as acquisition cost, accumulated depreciation and obligations under finance leases that do not transfer ownership of the leased property to the Companies on an "as if capitalized" basis as of March 31, 2004 and 2003, was as follows:

	Millions of Japanese Yen				Thousands of U.S. Dollars			
	<u>2004</u>				<u>2004</u>			
	Buildings and Structures	Machinery and Equipment	Tools, Furniture and Fixtures	Total	Buildings and Structures	Machinery and Equipment	Tools, Furniture and Fixtures	Total
Acquisition cost	¥17	¥57	¥400	¥474	\$ 160	\$ 538	\$3,774	\$4,472
Accumulated depreciation	<u>14</u>	<u>29</u>	<u>282</u>	<u>325</u>	<u>132</u>	<u>274</u>	<u>2,660</u>	<u>3,066</u>
Net leased property	<u>¥ 3</u>	<u>¥28</u>	<u>¥118</u>	<u>¥149</u>	<u>\$ 28</u>	<u>\$264</u>	<u>\$1,114</u>	<u>\$1,406</u>

	Millions of Japanese Yen			
	2003			
	Buildings and Structures	Machinery and Equipment	Tools, Furniture and Fixtures	Total
Acquisition cost	¥16	¥61	¥599	¥676
Accumulated depreciation	<u>10</u>	<u>28</u>	<u>371</u>	<u>409</u>
Net leased property	<u>¥ 6</u>	<u>¥33</u>	<u>¥228</u>	<u>¥267</u>

Future lease payments, including imputed interest, under finance leases that do not transfer ownership of the leased property and long-term noncancelable operating leases as of March 31, 2004 and 2003, were as follows:

	Millions of Japanese Yen				Thousands of U.S. Dollars	
	2004		2003		2004	
	Finance Lease	Operating Lease	Finance Lease	Operating Lease	Finance Lease	Operating Lease
Due within one year	¥ 81	¥ 71	¥122	¥ 98	\$ 764	\$ 670
Due after one year	<u>68</u>	<u>260</u>	<u>145</u>	<u>370</u>	<u>642</u>	<u>2,453</u>
Total	<u>¥149</u>	<u>¥331</u>	<u>¥267</u>	<u>¥468</u>	<u>\$1,406</u>	<u>\$3,123</u>

Depreciation expense which was not reflected in the consolidated statements of income, computed by the straight-line method, was ¥122 million (\$1,151 thousand) and ¥167 million for the years ended March 31, 2004 and 2003, respectively.

## 7. SHORT-TERM BANK LOANS AND LONG-TERM DEBT

Short-term bank loans represented borrowings under bank overdraft agreements and notes, bearing interest at rates ranging from 0.5% to 2.3% and from 0.5% to 2.6% per annum at March 31, 2004 and 2003, respectively.

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

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
2.1% unsecured convertible bonds, due 2003		¥1,905	
0.6% to 2.7% loans due through 2009:			
Collateralized	¥ 460	540	\$ 4,340
Unsecured	<u>2,267</u>	<u>2,858</u>	<u>21,386</u>
Total	<u>2,727</u>	<u>5,303</u>	<u>25,726</u>
Less current maturities	<u>(118)</u>	<u>(2,545)</u>	<u>(1,113)</u>
Total	<u>¥2,609</u>	<u>¥2,758</u>	<u>\$24,613</u>

The 2.1% unsecured convertible bonds are convertible by the holder into common stock of the Company on any date prior to maturity at a conversion price of ¥1,502 per share. The bonds are redeemable, at the option of the Company, in whole or in part, on any date prior to maturity, at prices which range from 100% to 101% of the principal amount thereof.

The per share conversion price for the above bonds is subject to adjustments in certain instances, including stock splits.

As of March 31, 2003, the 2.1% unsecured convertible bonds were convertible into a total of 1,268,308 common shares.

Maturities of long-term debt at March 31, 2004, were as follows:

<u>Year Ending March 31</u>	<u>Millions of Japanese Yen</u>	<u>Thousands of U.S. Dollars</u>
2005	¥ 118	\$ 1,113
2006	117	1,104
2007	273	2,575
2008	2,080	19,623
2009	80	755
2010 and thereafter	<u>59</u>	<u>556</u>
Total	<u>¥2,727</u>	<u>\$25,726</u>

The carrying amounts of assets pledged as collateral for long-term bank loans of ¥460 million (\$4,340 thousand) at March 31, 2004, were as follows:

	<u>Millions of Japanese Yen</u>	<u>Thousands of U.S. Dollars</u>
Land	¥ 242	\$ 2,283
Buildings and structures	3,875	36,557
Machinery and equipment	2,313	21,821
Vehicles	7	65
Tools, furniture and fixtures	<u>320</u>	<u>3,019</u>
Total	<u>¥6,757</u>	<u>\$63,745</u>

As is customary in Japan, loan agreements provide, under certain circumstances, that the Company shall provide additional collateral or guarantees for the present and future indebtedness immediately upon the banks' or other lenders' request. Basic agreements with banks also provide that the banks have the right to offset cash deposited with them against loans, or any other indebtedness outstanding, in the case of default or other similar events.

## 8. INCOME TAXES

Income taxes for the years ended March 31, 2004 and 2003, consisted of the following:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Current:			
Domestic	¥ 288	¥391	\$ 2,717
Foreign	<u>25</u>	<u>(5)</u>	<u>236</u>
Total	<u>313</u>	<u>386</u>	<u>2,953</u>
Deferred:			
Domestic	876	81	8,264
Foreign	<u>(33)</u>	<u>(2)</u>	<u>(311)</u>
Total	<u>843</u>	<u>79</u>	<u>7,953</u>
Total	<u>¥1,156</u>	<u>¥465</u>	<u>\$10,906</u>

The Company and domestic consolidated subsidiaries are subject to a number of taxes based on income which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 42% for 2004 and 2003. Foreign consolidated subsidiaries are subject to income taxes of the countries in which they operate.

The tax effects of significant temporary differences and loss carryforwards which resulted in deferred tax assets and liabilities at March 31, 2004 and 2003, were as follows:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Deferred tax assets:			
Accrued bonuses	¥ 310	¥ 272	\$ 2,925
Liability for retirement benefits	1,669	1,961	15,745
Loss on write-down of investment securities	189	381	1,783
Loss on revaluation of land	77	254	726
Loss on write-down of other investments	75	130	708
Tax loss carryforwards	379	574	3,575
Unrealized loss on available-for-sale securities		6	
Other	453	449	4,274
Less valuation allowance	<u>(302)</u>	<u>(285)</u>	<u>(2,849)</u>
Total deferred tax assets	<u>2,850</u>	<u>3,742</u>	<u>26,887</u>
Deferred tax liabilities:			
Unrealized gain on land transacted within the Companies	(310)	(310)	(2,925)
Unrealized gain on available-for-sale securities	(52)		(491)
Other	<u>(141)</u>	<u>(143)</u>	<u>(1,329)</u>
Total deferred tax liabilities	<u>(503)</u>	<u>(453)</u>	<u>(4,745)</u>
Net deferred tax assets	<u>¥2,347</u>	<u>¥3,289</u>	<u>\$22,142</u>

A reconciliation between the normal effective statutory tax rate and the actual effective tax rates reflected in the accompanying consolidated statements of income for the years ended March 31, 2004 and 2003, is as follows:

	<u>2004</u>	<u>2003</u>
Normal effective statutory tax rate	42.0%	42.0%
Expense not deductible for tax purposes	1.8	3.7
Valuation allowance	0.6	(11.9)
Equity in earnings of associated companies	(5.3)	(11.3)
Effect of tax rate reduction		6.0
Inhabitant tax—per capita	0.7	1.4
Credit for foreign taxes	(3.6)	
Other—net	<u>(0.2)</u>	<u>0.3</u>
Actual effective tax rate	<u>36.0%</u>	<u>30.2%</u>

On March 31, 2003, a tax reform law concerning enterprise tax was enacted in Japan which changed the normal effective statutory tax rate from 42.0% to 40.6%, effective for years beginning on or after April 1, 2004. The deferred tax assets and liabilities which will be realized on or after April 1, 2004 are measured at the effective tax rate of 40.6% as at March 31, 2004 and 2003.

#### 9. LIABILITY FOR RETIREMENT BENEFITS

Under the funded pension plan of the Company which covers substantially all employees, eligible employees are entitled to either life annuities starting at the age of 60, or lump-sum payments upon termination of employment. Under the unfunded retirement benefit plans of the Company and domestic consolidated subsidiaries, eligible employees receive lump-sum payments upon termination of employment. The retirement benefits for directors and corporate auditors are paid subject to the approval of the shareholders.

Liability for retirement benefits at March 31, 2004 and 2003, consisted of the following:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Employees' retirement benefit plans	¥4,092	¥4,856	\$38,604
Directors' and corporate auditors' plan	<u>223</u>	<u>230</u>	<u>2,104</u>
Total	<u>¥4,315</u>	<u>¥5,086</u>	<u>\$40,708</u>

The liability (asset) for employees' retirement benefits at March 31, 2004 and 2003, consisted of the following:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Projected benefit obligations	¥15,077	¥22,127	\$ 142,236
Fair value of plan assets	(8,645)	(10,859)	(81,557)
Unrecognized prior service cost		189	
Unrecognized actuarial loss	<u>(2,340)</u>	<u>(6,601)</u>	<u>(22,075)</u>
Net liability	<u>¥ 4,092</u>	<u>¥ 4,856</u>	<u>\$ 38,604</u>

The components of net periodic benefit costs for the years ended March 31, 2004 and 2003, were as follows:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Service cost	¥ 703	¥690	\$ 6,632
Interest cost	438	608	4,132
Expected return on plan assets	(294)	(472)	(2,774)
Actuarial cost	515	172	4,858
Prior service cost	(21)	(62)	(198)
Gain on transfer of the substitutional portion of the governmental pension program	<u>(1,146)</u>	—	<u>(10,811)</u>
Net periodic benefit costs	<u>¥ 195</u>	<u>¥936</u>	<u>\$ 1,839</u>

The Company and certain domestic subsidiaries have two types of pension plans for employees: a non-contributory and a contributory funded defined benefit pension plan. The contributory funded defined benefit pension plan, established under the Japanese Welfare Pension Insurance Law, covers a substitutional portion of the governmental pension program managed by the Company on behalf of the government and a corporate portion established at the discretion of the Company. In accordance with the Defined Benefit Pension Plan Law enacted in April 2002, the Company applied for an exemption from obligation to pay benefits for future employee services related to the substitutional portion, which would result in the transfer of the pension obligations and related assets to the government upon approval. The Company obtained approval for exemption from the future obligation by the Ministry of Health, Labour and Welfare on August 13, 2003 and recognized a gain on exemption from the future pension obligation of the governmental program in the amount of ¥1,146 million (\$10,811 thousand) for the year ended March 31, 2004. The substitutional portion of the plan assets which will be transferred to the government in the subsequent year is measured to be approximately ¥4,725 million (\$44,575 thousand) as at March 31, 2004.

Assumptions used for the years ended March 31, 2004 and 2003, are set forth as follows:

	<u>2004</u>	<u>2003</u>
Discount rate	2.7%	2.7%
Expected rate of return on plan assets	4.0%	4.0%
Recognition period of actuarial gain or loss	10 years	10 years
Amortization period of prior service cost	5 years	5 years

## 10. SHAREHOLDERS' EQUITY

Japanese companies are subject to the Japanese Commercial Code (the "Code") to which certain amendments became effective from October 1, 2001.

The Code was revised whereby common stock par value was eliminated resulting in all shares being recorded with no par value and at least 50% of the issue price of new shares is required to be recorded as common stock and the remaining net proceeds as additional paid-in capital, which is included in capital surplus. The Code permits Japanese companies, upon approval of the Board of Directors, to issue shares to existing shareholders without consideration as a stock split. Such issuance of shares generally does not give rise to changes within the shareholders' accounts.

The revised Code also provides that an amount at least equal to 10% of the aggregate amount of cash dividends and certain other appropriations of retained earnings associated with cash outlays applicable to each period shall be appropriated as a legal reserve (a component of retained earnings) until such reserve and additional paid-in capital equals 25% of the balance of common stock. The amount of total additional paid-in capital and legal reserve that exceeds 25% of the common stock may be available for dividends by resolution of the shareholders. In addition, the Code permits the transfer of a portion of additional paid-in capital and legal reserve to the common stock by resolution of the Board of Directors.

The revised Code eliminated restrictions on the repurchase and use of treasury stock allowing Japanese companies to repurchase treasury stock by a resolution of the shareholders at the general shareholders meeting and dispose of such treasury stock by resolution of the Board of Directors. The repurchased amount of treasury stock cannot exceed the amount available for future dividends plus the amount of common stock, additional paid-in capital or legal reserve to be reduced in the case where such reduction was resolved at the general shareholders meeting.

The amount of retained earnings available for dividends under the Code was ¥7,532 million (\$71,057 thousand) as of March 31, 2004, based on the amount recorded in the parent company's general books of account. In addition to the provision that requires an appropriation for a legal reserve in connection with the cash payment, the Code imposes certain limitations on the amount of retained earnings available for dividends.

Dividends are approved by the shareholders at a meeting held subsequent to the fiscal year to which the dividends are applicable. Semiannual interim dividends may also be paid upon resolution of the Board of Directors, subject to certain limitations imposed by the Code.

The Company has a stock option plan. The stock option plan which was approved at the general shareholders meeting held on June 28, 2001 provides for granting options to directors and key employees to purchase up to 635,000 shares of the Company's common stock in the period from July 1, 2003 to June 30, 2006. The options were granted at an exercise price of 105% of the fair market value of the Company's common stock at the date one-month previous to the option grant date.

## 11. COMMITMENTS AND CONTINGENT LIABILITIES

The amount of capital commitments outstanding at March 31, 2004, for purchases of property, plant and equipment for the purpose of renewal or expansion of production and research facilities was ¥37 million (\$349 thousand).

Contingent liabilities at March 31, 2004, are summarized as follows:

	<u>Millions of Japanese Yen</u>	<u>Thousands of U.S. Dollars</u>
Guarantees and items of a similar nature of related parties' indebtedness	¥1,174	\$11,075
Trade notes endorsed	<u>88</u>	<u>830</u>
Total	<u>¥1,262</u>	<u>\$11,905</u>

## 12. NET INCOME PER SHARE

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the years ended March 31, 2004 and 2003, is as follows:

<u>Year Ended March 31, 2004</u>	<u>Millions of Japanese Yen</u> <u>Net Income</u>	<u>Thousands of Shares</u> <u>Weighted-average Shares</u>	<u>Yen</u>	<u>U.S. Dollars</u> <u>EPS</u>
Basic EPS—Net income available to common shareholders	¥2,010	64,492	<u>¥31.18</u>	<u>\$0.29</u>
Effect of dilutive securities:				
Stock option		68		
Convertible bonds	<u>12</u>	<u>634</u>		
Diluted EPS—Net income for computation	<u>¥2,022</u>	<u>65,194</u>	<u>¥31.02</u>	<u>\$0.29</u>
<u>Year Ended March 31, 2003</u>				
Basic EPS—Net income available to common shareholders	<u>¥1,034</u>	<u>64,482</u>	<u>¥16.05</u>	

Diluted net income per share is not disclosed because it is anti-dilutive.

## 13. RELATED PARTY TRANSACTIONS

Transactions of the Company with associated companies for the years ended March 31, 2004 and 2003, were as follows:

	<u>Millions of Japanese Yen</u>		<u>Thousands of U.S. Dollars</u>
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Sales	¥1,143	¥1,305	\$10,783
Purchases	1,470	1,219	13,868
Dividend income	2	2	19
Other income	171	130	1,613

The balances due to or from these associated companies at March 31, 2004 and 2003, were as follows:

	Millions of Japanese Yen		Thousands of U.S. Dollars
	<u>2004</u>	<u>2003</u>	<u>2004</u>
Trade notes receivable	¥ 4	¥ 3	\$ 38
Trade accounts receivable	339	369	3,198
Trade accounts payable	193	131	1,821

#### 14. RESEARCH AND DEVELOPMENT COSTS

Research and development costs charged to income were ¥1,796 million (\$16,943 thousand) and ¥1,875 million for the years ended March 31, 2004 and 2003, respectively.

#### 15. DERIVATIVES

The Company enters into foreign exchange forward contracts to hedge foreign exchange risk associated with certain assets and liabilities. The Company also enters into interest rate swap contracts as a means of managing its interest rate exposure on certain liabilities. All derivative transactions are entered into in order to hedge interest and foreign currency exposures associated with its business. Accordingly, interest and currency risks associated with these derivatives are basically offset by opposite movements in the value of hedged assets and liabilities. Because the counterparties to these derivatives are limited to major international financial institutions, the Company does not anticipate any losses arising from credit risk. Derivative transactions entered into by the Company have been made in accordance with internal policies which regulate the authorization and credit limit amount.

The Company had the following derivatives contracts outstanding at March 31, 2004 and 2003:

	Millions of Japanese Yen				Thousands of U.S. Dollars	
	<u>2004</u>		<u>2003</u>		<u>2004</u>	
	<u>Contract or Notional Amount</u>	<u>Fair Value</u>	<u>Contract or Notional Amount</u>	<u>Fair Value</u>	<u>Contract or Notional Amount</u>	<u>Fair Value</u>
Forward exchange contracts—Selling U.S.\$			¥ 44	¥42		
Interest rate swaps— Fixed rate payment, floating rate receipt			2,000	(22)		

Interest rate swap contracts, which qualify for hedge accounting for the years ended March 31, 2004 and 2003, are excluded from the disclosure of market value information.

The contract or notional amounts of derivatives which are shown in the above table do not represent the amounts exchanged by the parties and do not measure the Company's exposure to credit or market risks.

16. SEGMENT INFORMATION

(1) Operations by Industry Segment

Information has not been provided because the Companies operated principally in the "non-woven fabrics" industry in 2004 and 2003.

(2) Operations by Geographical Segment

Operations of the Companies by geographical segment for the years ended March 31, 2004 and 2003, were as follows:

	Millions of Japanese Yen				Thousands of U.S. Dollars			
	2004				2004			
	<u>Japan</u>	<u>North America</u>	<u>Eliminations</u>	<u>Consolidated</u>	<u>Japan</u>	<u>North America</u>	<u>Eliminations</u>	<u>Consolidated</u>
Sales:								
Sales to customers	¥43,086	¥5,545		¥48,631	\$406,472	\$52,311		\$458,783
Intersegment sales	<u>66</u>	<u>351</u>	<u>¥(417)</u>	<u>          </u>	<u>622</u>	<u>3,312</u>	<u>\$(3,934)</u>	<u>          </u>
Total sales	43,152	5,896	(417)	48,631	407,094	55,623	(3,934)	458,783
Operating cost and expenses	<u>41,723</u>	<u>5,521</u>	<u>(430)</u>	<u>46,814</u>	<u>393,613</u>	<u>52,085</u>	<u>(4,057)</u>	<u>441,641</u>
Operating income	<u>¥ 1,429</u>	<u>¥ 375</u>	<u>¥ 13</u>	<u>¥ 1,817</u>	<u>\$ 13,481</u>	<u>\$ 3,538</u>	<u>\$ 123</u>	<u>\$ 17,142</u>
Assets	<u>¥48,144</u>	<u>¥3,333</u>	<u>¥ (37)</u>	<u>¥51,440</u>	<u>\$454,189</u>	<u>\$31,443</u>	<u>\$ (349)</u>	<u>\$485,283</u>
	Millions of Japanese Yen							
	2003							
	<u>Japan</u>	<u>North America</u>	<u>Eliminations</u>	<u>Consolidated</u>				
Sales:								
Sales to customers	¥41,753	¥6,295		¥48,048				
Intersegment sales	<u>257</u>	<u>416</u>	<u>¥(673)</u>	<u>          </u>				
Total sales	42,010	6,711	(673)	48,048				
Operating cost and expenses	<u>40,496</u>	<u>6,376</u>	<u>(687)</u>	<u>46,185</u>				
Operating income	<u>¥ 1,514</u>	<u>¥ 335</u>	<u>¥ 14</u>	<u>¥ 1,863</u>				
Assets	<u>¥53,102</u>	<u>¥3,448</u>	<u>¥(322)</u>	<u>¥56,228</u>				

**(3) Sales to Foreign Customers**

Sales to foreign customers of the Companies for the years ended March 31, 2004 and 2003, were as follows:

	<u>Millions of Japanese Yen</u>				<u>Thousands of U.S. Dollars</u>			
	<u>2004</u>				<u>2004</u>			
	<u>Asia</u>	<u>North America</u>	<u>Other</u>	<u>Total</u>	<u>Asia</u>	<u>North America</u>	<u>Other</u>	<u>Total</u>
Sales to foreign customers	¥3,666	¥5,861	¥595	¥10,122	\$34,585	\$55,292	\$5,613	\$ 95,490
Consolidated sales				48,631				458,783
Ratio of sales to foreign customers to consolidated sales				20.8%				20.8%

  

	<u>Millions of Japanese Yen</u>			
	<u>2003</u>			
	<u>Asia</u>	<u>North America</u>	<u>Other</u>	<u>Total</u>
Sales to foreign customers	¥2,707	¥6,572	¥519	¥ 9,798
Consolidated sales				48,048
Ratio of sales to foreign customers to consolidated sales				20.4%

**17. SUBSEQUENT EVENT**

At the general shareholders meeting held on June 29, 2004, the Company's shareholders approved the following appropriations of retained earnings:

	<u>Millions of Japanese Yen</u>	<u>Thousands of U.S. Dollars</u>
Cash dividends, ¥6.0 (\$0.06) per share	¥388	\$3,660
Bonuses to directors	<u>21</u>	<u>198</u>
Total	<u>¥409</u>	<u>\$3,858</u>

\* \* \* \* \*