

## Consolidated Financial Results

### for the First Nine Months of the Fiscal Year Ending 31st March 2004

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 Stock code: 4770  
 Stock market listing: TSE Mothers Market  
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## 1. Financial Highlights

### (1) Financial Results for the First Nine Months of the Fiscal Year Ending March 2004 (From April 1, 2003 to December 31, 2003)

(Amounts rounded down to million yen)

Term	FY 2002 1st - 3rd Qtr.	FY 2003 1st - 3rd Qtr.	% Change	FY 2002 Full year
Net sales	1,231	1,181	(4.1)	1,888
Operating income	(90)	(177)	-	(26)
Ordinary income	(88)	(187)	-	(27)
Net income (for the period)	(834)	81	-	(392)
Total assets	2,854	3,088	8.2	3,210
Shareholders' equity	2,274	2,709	19.1	2,690

### (2) Sales Breakdown

(Amounts rounded down to million yen)

Products			FY 2002 1st - 3rd Qtr.		FY 2003 1st - 3rd Qtr.		% Change	FY 2002 Full year	
Source	Group	¥ millions	%	¥ millions	%	¥ millions		%	
Manufactured products	1	Communications	275	22.4	252	21.3	(8.3)	405	21.4
	2	Internet protocol	421	34.2	386	32.7	(8.3)	526	27.9
	3	Real-time OS	163	13.2	51	4.4	(68.2)	249	13.2
	4	System Integration	305	24.8	413	35.0	35.5	579	30.7
Subtotal			1,165	94.6	1,104	93.4	(5.2)	1,760	93.2
Purchased products	5	Others	66	5.4	77	6.6	16.4	127	6.8
Total			1,231	100.0	1,181	100.0	(4.1)	1,888	100.0

#### Notes:

- Communications, the first product category in the above table, was divided into two categories in previous fiscal years: Multi-purpose communication boards and ISDN boards. The Company combined these items to form the new communications category in the current fiscal year.
- Real-time OS, the third product category in the above table, was divided into two categories in previous fiscal years: Windows and real-time OS. The Company combined these items to form the new real-time OS category in the current fiscal year.
- There have been no revisions to products contained in each category due to the above changes.

## **2. Results of Operations and Financial Position**

### **(1) Results of Operations**

During the first three quarters of the fiscal year, the operating environment continued to recover even as the Japanese economy remained generally negative due to concerns about unemployment and persistent deflationary forces. As a result, manufacturers of electrical machinery, automobiles and parts, semiconductors and other products, which represent the Company's primary source of sales, continued to be cautious about making significant investments.

In this environment, the Company's operating results have been improving since the middle of the fiscal year. Driving growth is demand for Internet products, chiefly equipment for IP telephony and VoIP (images and voice), and multimedia products (H.323 and SIP).

VoIP products hold much promise as they are currently at the point of moving from the development stage to commercialization. However, orders for these products are not yet increasing. The primary reason is that customers are still reviewing their system development processes. Because of this, demand for finished VoIP products has yet to emerge. Manufacturers have therefore adopted a cautious stance regarding R&D, causing many delays in the provision of system integration and customization services.

Regarding communication boards, the Company received large orders for boards in conjunction with the replacement of POS equipment and other devices. Nevertheless, demand is likely to decline because communication boards are on the downward end of their life cycle.

Real-time OS (RTOS) are undergoing a shift in their positioning in the Company's product lineup. One reason is that these systems are not sold as stand-alone products. Another is that open-source (free) software like ITRON and embedded Linux are becoming the main choice for RTOS requirements. Due to this situation, applications for the ELX family, the Company's original OS, are becoming increasingly limited.

In the market for embedded systems, the outlook is favorable as society stands on the doorstep of the 'Ubiquitous information age' in which everyone has networked home appliances and information appliances. The Company along with all its peers and customers are thus entering a major period of transition in their products and services. In response, the Company is concentrating on upgrading its product lineup, chiefly in the TCP/IP category, to bring about a big shift away from legacy systems.

As is noted later in this report, a major event occurred during the third quarter, the nine-month period that ended December 31, 2003. On December 25, 2003, the Company sold its wholly owned subsidiary Elmic Systems USA, Inc., which is based in San Francisco, California, to Ardro Engineering, Inc., which is based on Cincinnati, Ohio.

### **Results by product category**

Certain product categories have been combined beginning with the current fiscal year.

### **Communications Boards**

Multi-purpose communications boards and ISDN boards account for most sales in this category. Multi-purpose communications boards are incorporated in control units used in semiconductor manufacturing equipment and other production equipment. Although factory utilization rates are climbing, weak capital expenditures among manufacturer held sales of these boards below expectations. However, sales in communication-related products are being underpinned by strong growth in capital spending for LCD production facilities. In ISDN boards, sales are exceeding initial projections for the year because of sales to manufacturers of POS equipment for service stations during the first half of the fiscal year. Due to these factors, sales in this category during the first three quarters decreased 8.3% year on year.

### **Internet Protocol**

The market for TCP/IPv4 in Japan has matured, meaning that the focus of activity has shifted from the development (investments in) of IT-related products to marketing activities. The provision at no cost of KASAGO IPv6 has caused users to once again recognize the superiority of the Company's KASAGO TCP/IP (IPv4). As a result, system integration sales, as well as royalties, involving the commercialization of this protocol continue to

grow. Regarding IPv6, which the Company aims to establish as a core element of the Ubiquitous information society, an increasing number of prospective users are conducting R&D programs to evaluate this protocol for possible use in their next-generation products. This is leading to growth in tie-ups with semiconductor companies. While there are many projects under way at the R&D level, manufacturers of finished products are moving toward commercialization of new models slowly because of Japan's lackluster economy. A weak performance at Elmic Systems USA, Inc. further held back sales in this category. The result was a year-on-year decrease of 8.3% in sales.

### **Real-Time OS**

High expectations regarding TEngine, the next generation of ITRON, are making the direction of this market unclear. The result is lower investments in products and a market trends that generally match the Company's outlook at the beginning of the fiscal year.

Among RTOS products, orders for Windows-related versions are falling because of high expectations concerning Linux and TEngine for embedded systems. This development is in line with the Company's initial forecast. Accordingly, sales in the first three quarters fell 68.2% year on year.

### **System Integration (Customized services to match specific user needs)**

Substantial investments in LCD production facilities lifted orders for system integration projects using the Company's products above expectations. As demand for LCDs is likely to continue to outstrip supply, system integration orders for involving LCD production equipment will probably remain strong. In addition, capital expenditures in the LCD/TFT sector are increasing outside Japan, indicating that sales in this category will grow in the following fiscal year, too. Due to these factors, sales during the first three quarters were up 35.5% year on year.

### **Others**

In this category, the Company began sales of the iNHERITOR industrial PC during the fiscal year. As the product is still undergoing tests by customers, it is only beginning to contribute to sales. As a result, category sales increased 16.4% year on year.

### **Sale of Elmic Systems USA, Inc.**

On December 25, 2003, the Company sold wholly owned subsidiary Elmic Systems USA, Inc. to Ardor Engineering, Inc. A public announcement was made on the same day.

Elmic Systems USA, Inc. was established in August 2000 for the purpose of developing IPv6 and holding all rights to software related to this Internet protocol. If possible, this subsidiary was to have offset its expenses through sales in the United States. Unfortunately, Elmic Systems USA, Inc. was dealt a severe blow by the sharp downturn of the U.S. economy, and particularly the IT industry, in the wake of the 9.11 terrorist attacks. Operating results were disappointing, making this subsidiary an increasing financial burden on the Company. In the previous fiscal year, impairment losses at Elmic Systems USA, Inc. forced the Company to record a valuation loss on stock held in subsidiaries.

Despite these difficulties, work on developing IPv6 is largely on track. In October 2001, sales of the kernel section began in Japan and the United States. Development is also proceeding on major options and functions to enlarge the product lineup. As the Company believes that Elmic Systems USA, Inc. is quite capable of completing the remaining software development work on its own, the conclusion was reached to sell this subsidiary.

The sale of Elmic Systems USA, Inc. resulted in a gain of ¥258 million. After netting out the subsidiary's book value of ¥941 million and unamortized goodwill of ¥689 million on the consolidated financial statements, this gain becomes ¥252 million. Consequently, ¥6 million was added to the capitalized software development expenses of Elmic Systems USA, Inc.

The Company will continue to maintain a sound relationship with Ardor Engineering, Inc. with regard to marketing, the outsourcing of development tasks and other areas. The Company's U.S. sales are beginning to recover.

Due to this sale and other factors, consolidated net sales for the first three quarters of the fiscal year decreased

4.1% year on year to ¥1,181 million, there was an ordinary loss of ¥187 million and, including the gain on the sale of Elmic Systems USA, Inc. stock, net income was ¥81 million.

## **(2) Financial Position**

### Cash flows

During the third quarter, cash and cash equivalents increased ¥2 million to ¥1,280 million as of December 31, 2003. This was mainly attributable to a net income before income taxes and minority interest of ¥83 million, 111.5% more than one year earlier. In addition, the decrease in trade account receivables was up 53.3% to ¥222 million and the trade account payables were up 188.8% to ¥67 million.

Cash flows by category in the nine-month period were as follows were as follows.

### **(Operating activities)**

Net cash used in operating activities was ¥41 million compared with net cash used of ¥22 million in the nine-month period of the previous fiscal year. In addition to the net income before income taxes and minority interest of ¥83 million, cash provided by the decrease in trade account receivables was down to ¥222 million and there was a decrease of ¥258 million as the gain from sale of stock in a subsidiary was transferred as accrued revenue.

### **(Investing activities)**

Net cash provided by investing activities was ¥43 million. In the previous fiscal year's nine-month period, investing activities provided net cash ¥187 million. The major components were payments of ¥68 million for the acquisition of intangible assets, payments of ¥10 million for the acquisition of investment securities and proceeds of ¥138 million from the sale of investment securities.

### **(Financing activities)**

Net cash used in financing activities was ¥4 million, 98.2% less than one year earlier. This was mainly due to payments of ¥3 thousand for the repayment of finance leases.

### 3. Outlook for Fiscal Year Ending March 31, 2004

In the previous fiscal year, the lending at no cost of IPv6 (including IPv4) gave users an opportunity to take another look at the strengths of IPv4. The result was the decision by several users during the first half of this fiscal year to use IPv4 in their cell phones (PDC). As this is generating income in the form of royalties, it appears that a change in the Company's profit structure will begin to occur late in the current fiscal year.

Regarding content and services, primarily voice and moving images, the Company's major customers are currently in the R&D stage. KASAGO (TCP/IP), H.323, SIP and other software protocols, all of which are vital to these R&D activities, are therefore unlikely to contribute to earnings in the current fiscal year. Furthermore, development work begun in the past year with the goal of rapidly creating software for the communication functions of semiconductor manufacturing equipment has resulted in the introduction of SoftCOM. The Company expects to begin deliveries of this product at the end of the fiscal year as semiconductor industry investments increase and manufacturers switch to 300mm wafers.

The Company is determined to position itself squarely at the center of the emerging Ubiquitous information age. This will be accomplished by offering a diverse line of products and support: middleware such as communication protocol TCP/IP and VoIP; ELX, Linux, ITRON, T-Engine and other operating systems; a variety of drivers; and applications. The goal is to become an even more reliable partner for customers through the provision of a full line of software.

The Company is confident that its products can be successful. Furthermore, the forecast for the current fiscal year reflects the annual pattern in which a high percentage of deliveries take place near the end of the fiscal year. Consequently, the Company is forecasting fiscal year net sales that are much higher than sales recorded through the first nine months of the fiscal year.

Net sales are expected to decrease ¥345 million to ¥1,763 million due to lower sales in Japan and at Elmic Systems USA, Inc. Ordinary income is expected to decrease ¥143 million to a loss of ¥68 million as significant cost reductions in Japan were insufficient to offset the deteriorating performance at Elmic Systems USA, Inc. Due to the ¥258 million gain on the sale of Elmic Systems USA, Inc. (see note), the net income forecast has been revised to ¥144 million, an increase of ¥131 million.

Note: The sale of Elmic Systems USA, Inc. resulted in a gain of ¥258 million. After netting out the subsidiary's book value of ¥941 million and unamortized goodwill of ¥689 million on the consolidated financial statements, this gain becomes ¥252 million. Consequently, ¥6 million was added to the capitalized software development expenses of Elmic Systems USA, Inc.

#### Consolidated Forecast

		(¥ millions, %)		
		Net sales	Ordinary income	Net income
Forecast (A)	(as of December 25, 2003)	2,108	75	13
Forecast (B)	(as of February 13, 2004)	1,763	(68)	144
Change (B - A)		(345)	(143)	131
Change %		(16.4%)	-	1,007.7%
FY2002	(Apr. 1, 2002 – Mar. 31, 2003)	1,888	(27)	(392)

\* The forecast for the fiscal year ending March 31, 2004 is based on the judgments of management in accordance with information currently available. Actual results may differ materially from the forecast for a number of reasons. Consequently, investment decisions should not be based solely on this forecast. Factors that may affect operating results include, but are not limited to, economic trends in major markets, changes in demand and pricing for products, rapid technological advances, changes in foreign exchange rates, and revisions in regulations and accounting standards in Japan and overseas.

## 4. Consolidated Financial Statements

### (1) Consolidated Balance Sheets

Account	Period	FY2002 1st - 3rd Qtr. As of Dec. 31, 2002		FY2003 1st - 3rd Qtr. As of Dec. 31, 2003		FY2002 Selected data As of March 31, 2003		
		¥ thousands	%	¥ thousands	%	¥ thousands	%	
<b>Assets</b>								
I Current assets								
1. Cash and deposits		146,793		112,514		171,219		
2. Notes & accounts receivable - trade *3		645,627		546,687		801,048		
3. Available for sale securities		1,190,164		1,168,071		1,106,818		
4. Inventories		150,304		161,420		104,722		
5. Other current assets		128,962		127,477		116,809		
6. Reserve for doubtful receivables		(484)		(177)		(2,266)		
Total current assets		2,261,368	79.2	2,115,995	68.5	2,298,352	71.6	
II Fixed assets								
1. Property, plant and equipment *1		46,605		16,260		50,811		
2. Intangible assets								
(1) Goodwill		60,167		-		58,842		
(2) Other intangible assets		118,308	178,476	167,383	167,383	144,478	203,320	
3. Investments and other assets								
(1) Investment securities		227,501		-		195,758		
(2) Deferred tax assets – non-current		-		326,738		320,924		
(3) Other		142,105		463,329		142,734		
(4) Reserve for doubtful receivables		(1,344)	368,263	(1,400)	788,668	(1,500)	657,917	
Total fixed assets		593,345	20.8	972,312	31.5	912,049	28.4	
Total assets		2,854,713	100.0	3,088,307	100.0	3,210,401	100.0	

Account	Period	FY2002 1st - 3rd Qtr. As of Dec. 31, 2002		FY2003 1st - 3rd Qtr. As of Dec. 31, 2003		FY2002 Selected data As of March 31, 2003	
		¥ thousands		¥ thousands		¥ thousands	
			%		%		%
<b>Liabilities</b>							
I	Current liabilities						
1.	Accounts payable - trade	85,287		64,229		133,439	
2.	Income taxes payable	6,005		4,981		7,636	
3.	Reserve for accrued bonuses	28,979		27,839		50,200	
4.	Other current liabilities *2	201,835		60,481		101,096	
	Total current liabilities	322,107	11.3	157,531	5.1	292,372	9.1
II	Long-term liabilities						
1.	Reserve for employees' retirement benefits	-		-		19	
2.	Reserve for directors' retirement benefits	158,447		159,867		160,225	
3.	Other long-term liabilities	90,404		54,009		59,664	
	Total long-term liabilities	248,851	8.7	213,876	6.9	219,909	6.9
	Total liabilities	570,958	20.0	371,408	12.0	512,281	16.0
<b>Minority interest</b>							
	Minority interest	9,171	0.3	7,390	0.3	7,706	0.2
<b>Shareholders' equity</b>							
I	Common stock	1,160,041	40.7	1,160,041	37.6	1,160,041	36.1
II	Capital surplus	1,459,152	51.1	1,459,152	47.2	1,459,152	45.5
III	Retained earnings	(250,211)	(8.8)	273,680	8.9	192,041	6.0
IV	Net unrealized gain on other securities	(5,914)	(0.2)	1,819	0.0	(16,740)	(0.5)
V	Foreign currency translation adjustment	96,135	3.4	-	-	80,539	2.5
IV	Treasury stock	(184,619)	(6.5)	(185,184)	(6.0)	(184,619)	(5.8)
	Total shareholders' equity	2,274,583	79.7	2,709,509	87.7	2,690,414	83.8
	Total liabilities, minority interest and shareholders' equity	2,854,713	100.0	3,088,307	100.0	3,210,401	100.0

**(2) Consolidated Statements of Income**

Account	Period		FY2002 1st - 3rd Qtr. From April 1, 2002 to Dec. 31, 2002		FY2003 1st - 3rd Qtr. From April 1, 2003 to Dec. 31, 2003		FY2002 Selected data From April 1, 2002 to March 31, 2003		
			¥ thousands	%	¥ thousands	%	¥ thousands	%	
I Net sales *1		1,231,945	100.0		1,181,856	100.0		1,888,436	100.0
II Cost of sales		508,826	41.3		523,466	44.3		853,308	45.2
Gross profit		723,119	58.7		658,389	55.7		1,035,128	54.8
III SG&A expenses *2		814,067	66.1		835,511	70.7		1,061,207	56.2
Operating loss		90,947	(7.4)		177,121	(15.0)		26,079	(1.4)
IV Non-operating income									
1. Interest income	1,724			884			2,935		
2. Dividends income	100			1,015			100		
3. Equity in earnings of affiliates	10,926			4,419			9,215		
4. Gain on anonymous partnerships	3,784			5,271			5,217		
5. Other non-operating income	1,177	17,712	1.5	1,827	13,418	1.1	2,173	19,641	1.0
V Non-operating expenses									
1. Interest expense	349			131			414		
2. Foreign exchange loss	8,321			23,779			12,873		
3. Loss on options	6,700			-			6,700		
4. Other non-operating expenses	313	15,685	1.3	0	23,911	2.0	785	20,774	1.1
Ordinary loss		88,920	(7.2)		187,614	(15.9)		27,211	(1.4)
VI Extraordinary income									
1. Gain on reversal from doubtful receivables	-			450			-		
2. Gain on sales of investment securities	3,102			22,904			10,150		
3. Gain on sale of subsidiary stock	-	3,102	0.3	258,876	282,231	23.9	-	10,150	0.5
VII Extraordinary loss									
1. Loss on removal of fixed assets	-			98			-		
2. Loss on impairment of goodwill	618,404			-			604,785		
3. Loss on revaluation of investment securities	26,880			10,735			32,120		
4. Loss on revaluation of inventories	-	645,284	52.4	-	10,833	0.9	14,399	651,305	34.5
Net loss before income taxes and minority interest		(731,102)	(59.3)		83,782	7.1		(668,366)	(35.4)
Income taxes - current	5,347			6,035			6,979		
Income taxes - deferred	96,258	101,606	8.3	(3,575)	2,459	0.2	(283,424)	(276,445)	(14.6)
Minority interest		2,015	0.2		(315)	(0.0)		550	0.0
Net loss		(834,723)	(67.8)		81,639	6.9		(392,471)	(20.8)

**(3) Consolidated Statements of Retained Earnings**

Account	Period	FY2002 1st - 3rd Qtr. From April 1, 2002 to Dec. 31, 2002		FY2003 1st - 3rd Qtr. From April 1, 2003 to Dec. 31, 2003		FY2002 Selected data From April 1, 2002 to March 31, 2003	
		¥ thousands		¥ thousands		¥ thousands	
<b>Capital surplus</b>							
I	Capital surplus at beginning of period		1,459,152		1,459,152		1,459,152
II	Retained earnings at end of period		1,459,152		1,459,152		1,459,152
<b>Retained earnings</b>							
I	Retained earnings at beginning of period		624,316		192,041		624,316
II	Increase in retained earnings						
1.	Net income	-	-	81,639	81,639	-	-
III	Decline in retained earnings						
1.	Cash dividends	39,804		-		39,804	
2.	Net loss	834,723	874,528	-	-	392,471	432,275
IV	Retained earnings at end of period		(250,211)		273,680		192,041

**(4) Consolidated Statements of Cash Flows**

Account	Period	FY2002 1st - 3rd Qtr. From April 1, 2002 to Dec. 31, 2002	FY2003 1st - 3rd Qtr. From April 1, 2003 to Dec. 31, 2003	FY2002 Selected data From April 1, 2002 to March 31, 2003
		¥ thousands	¥ thousands	¥ thousands
I Cash flows from operating activities				
Net loss before income taxes and minority interest		(731,102)	83,782	(668,366)
Depreciation and amortization		47,583	59,507	68,848
Equity in earnings of affiliates		(10,926)	(4,419)	(9,215)
Increase (decrease) in reserve for doubtful receivables		329	(450)	2,266
Decrease in reserve for accrued bonuses		(23,683)	(22,360)	(2,462)
Increase (decrease) in reserve for employees' retirement benefits		-	(19)	19
Increase(decrease) in reserve for directors' retirement benefits		1,040	(357)	2,818
Interest and dividends income		(1,824)	(1,899)	(3,035)
Interest expense		349	131	414
Gain on anonymous partnerships		(3,784)	(5,271)	(5,217)
Foreign exchange loss		6,889	618	6,827
Loss on options		6,700	-	6,700
Gain on sales of investment securities		(3,102)	(22,904)	(10,150)
Gain on sale of subsidiary stock		-	(258,876)	-
Loss on sales of investment securities		-	98	-
Loss on impairment of goodwill		618,404	-	604,785
Loss on revaluation of investment securities		26,880	10,735	32,120
Loss on revaluation of inventories		-	-	14,399
Decrease (increase) in notes and accounts receivable - trade		144,932	222,131	(11,444)
Increase in inventories		(64,499)	(56,607)	(33,318)
Increase (decrease) in accounts payable - trade		(23,242)	(67,123)	25,067
Decrease (increase) in other assets		(32,457)	33,090	(11,673)
Increase (decrease) in other liabilities		8,056	3,193	(16)
Decrease in suspense receipt of consumption taxes		9,302	-	9,302
Increase (decrease) in suspense payment of consumption taxes		5,138	(11,692)	16,858
Subtotal		(19,015)	(38,693)	35,528
Interest and dividends received		1,824	4,399	10,560
Interest paid		(349)	(131)	(414)
Income taxes paid		(4,681)	(7,476)	(4,817)
Net cash provided by (used in) operating activities		(22,222)	(41,901)	40,857

Account	Period	FY2002 1st - 3rd Qtr. From April 1, 2002 to Dec. 31, 2002	FY2003 1st - 3rd Qtr. From April 1, 2003 to Dec. 31, 2003	FY2002 Selected data From April 1, 2002 to March 31, 2003
		¥ thousands	¥ thousands	¥ thousands
II Cash flows from investing activities				
Payments for acquisition of available for sale securities		(101,500)	-	(202,154)
Proceeds from redemption of available for sale securities		-	-	100,654
Payments for acquisition of property, plant and equipment		(16,358)	(2,531)	(24,470)
Payments for acquisition of intangible assets		(44,708)	(68,396)	(88,767)
Payments for acquisition of investment securities		(30,204)	(10,280)	(53,656)
Gain on sales of investment securities		15,327	138,784	61,267
Decrease in cash and cash equivalents due to sale of subsidiary resulting in changes in the scope of consolidation		-	(14,121)	-
Payments for short-term loans receivable		(10,000)	-	(10,000)
Proceeds from collection of short-term loans receivable		-	-	10,000
Payments for long-term loans receivable		(200)	(700)	(500)
Proceeds from collection of long-term loans		1,435	845	1,640
Proceeds from return of leasehold and security deposits		323	4,423	373
Others		(1,246)	(4,964)	(2,230)
Net cash provided by (used in) investment activities		(187,132)	43,060	(207,844)
III Cash flows from financing activities				
Payments for finance lease liabilities		(2,701)	(3,366)	(3,245)
Payments for acquisition of treasury stock		(184,264)	(564)	(184,264)
Cash dividends paid		(39,466)	(162)	(39,504)
Net cash provided by (used in) financing activities		(226,432)	(4,092)	(227,013)
IV Effect of exchange rate changes on cash and cash equivalents		(10,578)	5,483	(10,370)
V Increase (decrease) in cash and cash equivalents		(446,365)	2,549	(404,370)
VI Cash and cash equivalents at beginning of period		1,682,407	1,278,037	1,682,407
VII Cash and cash equivalents at end of period *1		1,236,042	1,280,586	1,278,037

## **Significant Accounting Policies in the Preparation of Consolidated Financial Statements**

Consolidated nine-month period ended December 31, 2003 (From April 1, 2003 to December 31, 2003)

### **1. Scope of consolidation**

(1) Consolidated subsidiary: 1

Names of consolidated subsidiary: AIRFOLC Corporation

Effective from the nine-month period ended December 31, Elmic Systems USA, Inc., a consolidated subsidiary in previous fiscal year, has been excluded from the consolidation since the Company sold its entire stock holding in the subsidiary. However, the consolidated financial statements include the accounts (statement of income and statement of cash flows) of Elmic Systems USA, Inc. for the period from January 1, 2003 to December 31, 2003.

(2) Unconsolidated subsidiary: None

### **2. Equity method accounting**

(1) Affiliates accounted for by the equity method of accounting: 1

Affiliate name: WESCOM Inc.

(2) Rock Hand Technology, an equity method affiliate, is excluded from the scope of affiliates accounted for by the equity method since it does not have material effect on consolidated net income (loss) (equity in earnings) and consolidated retained earnings (interest in earnings) for the period and is of relatively little significance in the context of consolidated financial statements.

### **3. Balance sheet date of subsidiary**

The consolidated financial statements include the accounts of the following consolidated subsidiary, of which the nine-month period ends on a different day:

AIRFOLC Corporation: Nine-month period ended November 31

In the preparation of consolidated financial statements for the period, the financial statements of the subsidiary for the respective nine-month period have been used. With respect to significant transactions, which occurred after the balance sheet date of the consolidated subsidiary, necessary adjustments have been made in the consolidated financial statements.

### **4. Accounting standards**

A. Valuation criteria and methods for significant assets:

(1) Securities

Held-to-maturity securities: Valued using the amortized cost method

Affiliate company stock: Stated at cost, cost using the moving average method

Other securities:

Securities with market quotations

Stated at fair value based on market prices on the balance sheet date

(Unrealized holding gains and losses are accounted for as a component of the shareholders' equity; cost of other securities sold is determined using the moving average method.)

Securities without market quotations

Stated at cost, cost using the moving average method

(2) Derivatives

No reportable information.

(3) Inventories

Merchandise:

Stated at cost, cost being determined by the moving average method

Products, work in process and raw materials:

Stated at cost, cost being determined by the period average method

## B. Depreciation and amortization of significant depreciable assets

### (1) Property, plant and equipment

The Company and its domestic subsidiary compute depreciation using the declining balance method, in accordance with Corporation Tax laws.

Overseas consolidated subsidiary compute depreciation using the straight-line method in accordance with the generally accepted accounting standards of the country of its domicile.

### (2) Intangible assets

The Company and its domestic subsidiary amortize capitalized costs using one of two alternate methods, which is higher, depreciation based on estimated sales volume or the straight-line method based on remaining the estimated period to expiration.

Software for internal use is amortized using the straight-line method over its estimated useful life of five years.

Overseas consolidated subsidiary amortizes in accordance with the generally accepted accounting standards of the country of its domicile.

## C. Recognition of reserves

### (1) Reserve for doubtful receivables

To prepare for credit losses on accounts receivable, the Company and its domestic subsidiary provide an allowance equal to the estimated amount of uncollectible receivables for general receivables based on the historical write-off ratio, and bad receivables based on a case-by-case determination of collectibility. Overseas consolidated subsidiary provides allowances for credit losses based on a case-by-case determination of collectibility.

### (2) Reserve for accrued bonuses

As a means of providing for bonus obligations, the Company and its domestic subsidiary designate in the reserve account an amount accrued for the nine-month period among the estimated future obligations.

### (3) Reserve for employees' retirement benefits

To provide for employees' retirement benefits, an allowance for retirement benefits is provided in the amount deemed to have accrued, determined based on the estimated retirement benefit obligations and pension assets on the balance sheet date. Since pension assets at the end of the period exceeded the estimated retirement benefit obligations ¥2,117 thousand was charged to income as a pre-paid pension expense.

### (4) Reserve for directors' retirement benefits

To provide for directors' retirement benefits, an allowance is provided pursuant to the Company's rules on directors' retirement benefits.

## D. Accounting for lease transactions

Overseas consolidated subsidiary accounts all finance lease contracts other than those that are deemed to transfer the ownership of the leased assets to lessees by the method similar to that applicable to regular trading transactions.

## E. Accounting for significant hedge transactions

No reportable information.

## F. Other significant accounting policies in the preparation of consolidated financial statements for the period

### (1) Equity method of accounting based on the anonymous partnership agreement

The Company in March 1995 entered a leveraged lease agreement (term of agreement: 12 years) with an anonymous partnership. The ¥50,000 thousand investments at the time of participation are recognized as a claim against the anonymous association. A share of the anonymous partnership's net assets (as recorded in the most recent settlement of accounts) proportional to the Company's investment in the anonymous partnership is recognized as a claim or liability against the anonymous partnership. A share anonymous partnership's net income (as recorded in the settlement of accounts for the nine-month period) applicable to the current consolidated nine-month period, proportional to the Company's investment in the anonymous partnership is recognized as a gain or loss on investment in the anonymous partnership.

### (2) Accounting treatment for consumption taxes

Consumption taxes are accounted by the tax exclusion method.

(3) Accounting for corporation, residential and enterprise taxes

Appropriation of retained earnings for the consolidated period reflects the planned withdrawal from the program reserve and special depreciation reserve.

## 5. Scope of cash and cash equivalents on consolidated statements of cash flows

For the purpose of consolidated statements of cash flows, cash and cash equivalents consists of vault cash, deposits that can be withdrawn on demand, and short-term investments, with original maturities of three months or less, that are readily convertible to known amounts of cash and present insignificant risk of change in value.

## Reclassifications

### Consolidated balance sheets for the nine-month period ended December 31, 2003

Effective from the consolidated nine-month period ended December 31, "Deferred tax assets - non-current," presented as a component of "Other" in the "Investments and other assets" account for the consolidated nine-month period ended December 31, 2002, are reclassified and presented as a separate item since the value of deferred assets exceeded 5% of total assets as of the end of the consolidated nine-month period ended December 31, 2003.

"Deferred tax assets - non-current" totaled ¥143 thousand as of the end of the nine-month period ended December 31, 2002.

Effective from the consolidated nine-month period ended December 31, "Investment securities," presented as a separate line item in the consolidated nine-month period ended December 31, 2002, has been reclassified and included in "Other" under investments and other assets since the total amount of "Investment securities" declined to less than 5% of total assets.

"Investment securities" totaled ¥101,032 thousand as of the end of the nine-month period ended December 31, 2002.

## Notes to Consolidated Financial Statements

Consolidated nine-month period ended December 31, 2003 (From April 1, 2003 to December 31, 2003)

### Notes to consolidated balance sheets

\*1. Accumulated depreciation on property, plant and equipment: ¥101,207 thousand

\*2. Accounting for consumption taxes

Consumption tax suspense payments and receipts are included in the "Other current liabilities" account in current liabilities since the amount is insignificant in the context of total current assets.

\*3. Accounting of trade notes maturing on the balance sheet date of the period. The settlement of trade notes maturing on the balance sheet date of the period is accounted on the clearance date. As the balance sheet date of the period was a bank holiday, the trade notes maturing on the balance sheet date of the period, in the following amounts were included in trade notes outstanding at the end of the period.

Notes receivable - trade: ¥10,689 thousand

### Notes to consolidated statements of income

\*1. The Company's sales are characterized by seasonal fluctuations. Since production on order is concentrated heavily in the second half, there is considerable difference in sales between the first and the second halves.

\*2. Principal components and corresponding amounts of SG&A expenses are as follows.

Wages & allowances: ¥332,152 thousand

Provision of reserve for accrued bonuses: ¥11,714 thousand

Provision of reserve for directors' retirement benefits: ¥5,334 thousand

R&D expenses: ¥64,047 thousand

\*3. Removal of tools, furniture and fixtures represents the loss on removal of fixed assets.

## Notes to consolidated statements of cash flows

\*1. Reconciliation of cash and cash equivalents of the statements of cash flows and account balances of consolidated balance sheets for the period is made as follows. (As of December 31, 2003)

Cash and deposits: ¥112,514 thousand

Short-term investments with original maturities of less than three months: ¥1,168,071 thousand

Cash and cash equivalents: ¥1,280,586 thousand

\*2. Assets and liabilities of the subsidiary excluded from the consolidation due to sale of stock holding

Assets and liabilities of Elmic Systems USA, Inc., excluded from the consolidation due to sale of stock holding, are as follows:

Current assets: ¥31,446 thousand

Fixed assets: ¥77,547 thousand

Total assets : ¥108,994 thousand

Current liabilities: ¥184,108 thousand

Total liabilities: ¥184,108 thousand

## Accounting for Leases

No reportable information.

## Securities

(As of December 31, 2003)

1. Securities with market quotations classified as "Other securities"

(¥ thousand)

Security	Acquisition cost	Carrying value	Unrealized gain/(loss)
(1) Equity securities	8,060	10,340	2,280
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	-	-	-
Total	8,060	10,340	2,280

2. Securities without market quotations

(¥ thousand)

	Carrying value
(1) Held-to-maturity debt securities	
Commercial paper	99,989
(2) Other securities	
Money management funds	965,959
Free financial funds	100,018
Medium-term government bond funds	2,103
Unlisted stock (excluding OTC stock)	11,354
Total	1,179,426

## Derivatives

Consolidated nine-month period ended December 31, 2003 (From April 1, 2003 to December 31, 2003)

No reportable information. The Group did not have any outstanding derivative positions as of the end of the consolidated nine-month period ended December 31, 2003.

## Segment Information

Consolidated nine-month period ended December 31, 2003 (From April 1, 2003 to December 31, 2003)

### 1. Segment information by operating segment

No reportable items. The Company and its consolidated subsidiary operate in a single industry commonly classified as electronics component manufacturing. These activities include manufacturing and marketing of components products related to communications and real-time operating systems.

### 2. Geographical segment information

(¥ thousand)

	Japan	N. America	Europe	Total	Elimination or Corporate	Consolidated
Net sales						
(1) Sales to external customers	1,019,737	141,715	20,404	1,181,856	-	1,181,856
(2) Inter-segment sales and transfers	-	111,537	-	111,537	(111,537)	-
Total	1,019,737	253,252	20,404	1,293,393	(111,537)	1,181,856
Operating expenses	1,035,507	352,354	52,331	1,440,193	(81,214)	1,358,978
Operating loss	15,770	99,101	31,927	146,799	(30,322)	177,121

Notes: 1. Countries and regions are grouped together according to the proximity of their geographical locations.

2. The principal countries or areas included in each region, outside Japan, are as follows.

North America: U.S.A.

Europe: France

3. Unallocatable operating expenses included in eliminations or corporate.

Amount of unallocatable operating expenses included in eliminations or corporate: ¥31,980 thousand

Significant components: Represent expenses related to the administration division

### 3. Overseas sales

(¥ thousand, %)

	N. America	Other regions	Total
I Overseas sales	89,301	72,817	162,119
II Consolidated net sales	-	-	1,181,856
III Weight of overseas sales in total consolidated net sales	7.5%	6.2%	13.7%

Notes: 1. Countries and regions are grouped together according to the proximity of their geographical locations.

2. The principal countries or areas included in each region, outside Japan, are as follows:

North America: U.S.A., Canada

Other regions: Germany, Britain, Hong Kong and India etc.

3. Overseas sales of the Company and its consolidated subsidiaries represent sales in countries and regions other than Japan.

## Per Share Information

Consolidated nine-month period ended December 31, 2003 (From April 1, 2003 to December 31, 2003)

Net assets per share: ¥562.64

Net income per share: ¥16.95

Diluted net income per share for the third quarter is not presented since the Company had no outstanding dilutive securities.

Note: The basis of calculation of net income per share and the diluted net loss per share for the period is as follows.

Net income for the period: ¥81,639 thousand

Equity in net loss not account of regular shareholders: None

Regular shareholders' equity in net income: ¥81,639 thousand

Average number of shares outstanding for the period: 4,816,000 shares

Details on potential stock not included in the calculation of diluted net earnings per share since there is no dilution: Pursuant to Article 280-19 of the Commercial Code of Japan, the Company has only one type of share acquisition right by way of stock options outstanding (Shares to be issued upon execution of share acquisition rights: Common shares, Number of shares to be issued upon execution of share acquisition rights: 164,000 shares)

## **Subsequent Events**

None.

## **5. Others**

Financial statements for the current nine-month period ended December 2003, that is consolidated balance sheet, consolidated statements of income, and consolidated statements of cash flows for the period, have been audited by the company's auditors in conformation with the "Standards for Report of the Independent Certified Public Accountants on Quarterly Financial Statements" set forth in the supplement to the "Rules Regarding Timely Disclosure of Corporate Information by Companies Issuing Listed Securities."

*\* This financial report is solely a translation of summary of "Kessan Tanshin" (in Japanese, including attachments), which has been prepared in accordance with accounting principles and practices generally accepted in Japan, for the convenience of readers who prefer an English translation.*