

Consolidated Financial Results

for the Fiscal Year Ended March 31, 2005

Company name: ELMIC SYSTEMS, INC.
 Stock code: 4770
 Stock market listing: TSE Mothers Market
 Company domicile: Kanagawa prefecture
 Head office: 4-59 Benten-Dori, Naka-ku, Yokohama 231-0007 Japan
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 Date of board meeting for approving financial results: May 19, 2005
 Accounting principle: Japanese GAAP

1. Consolidated Financial Results (From April 1, 2004 to March 31, 2005)

(1) Financial Results

(Amounts rounded down to million yen)

	Net sales		Operating income		Ordinary income	
	¥ millions	%	¥ millions	%	¥ millions	%
Fiscal year ended March 2005	1,254	(27.6)	(21)	-	2	-
Fiscal year ended March 2004	1,733	(8.2)	(77)	-	(78)	-

	Net income		Net income per share (basic)	Net income per share (diluted)
	¥ millions	%	¥	¥
Fiscal year ended March 2005	(590)	-	(122.55)	-
Fiscal year ended March 2004	142	-	29.51	-

	Return on equity	Ratio of ordinary income to total assets	Ratio of ordinary income to net sales
	%	%	%
Fiscal year ended March 2005	(24.0)	0.1	0.2
Fiscal year ended March 2004	5.2	(2.4)	(4.5)

Notes: 1. Equity in earnings of unconsolidated subsidiaries:

Fiscal year ended March 2005: ¥ 7 million

Fiscal year ended March 2004: ¥ 11 million

2. Average number of shares outstanding:

Fiscal year ended March 2005: 4,815,719 shares

Fiscal year ended March 2004: 4,816,230 shares

3. Changes in accounting principles applied: None

4. The percentages shown for net sales, operating income, ordinary income, and net income represent changes from the corresponding of the same period of the previous year.

(2) Financial Position

(Amounts rounded down to million yen)

	Total assets	Shareholders' equity	Shareholders' equity ratio	Shareholders' equity per share
	¥ millions	¥ millions	%	¥
As of March 31, 2005	2,463	2,134	86.6	443.19
As of March 31, 2004	3,221	2,773	86.1	576.02

Note: 1. Number of shares outstanding:

As of March 31, 2005:	4,815,682 shares
As of March 31, 2004:	4,815,730 shares

(3) Cash Flows Position

(Amounts rounded down to million yen)

	Net cash provided by operating activities	Net cash used in investing activities	Net cash used in financing activities	Cash and cash equivalents at end of year
	¥ millions	¥ millions	¥ millions	¥ millions
Fiscal year ended March 2005	214	(180)	(36)	1,252
Fiscal year ended March 2004	35	(60)	(4)	1,254

(4) Scope of Consolidation and the Application of Equity Method

Consolidated subsidiaries: 1

Unconsolidated subsidiaries accounted for under the equity method: None

Affiliates accounted for under the equity method: 1

(5) Changes in the Scope of Consolidation and Affiliates Accounted for Under the Equity Method

Consolidated subsidiaries:

New: None

Excluded: None

Affiliates accounted for under the equity method:

New: None

Excluded: None

2. Forecast for the Fiscal Year Ending March 2006 (From April 1, 2005 to March 31, 2006)

	Net sales	Ordinary income	Net income
	¥ millions	¥ millions	¥ millions
Full year	1,698	60	8

Reference: Estimated net income per share for the fiscal year ending March 2006: ¥1.66

Note: Forecasts regarding future performance in these materials are based judgments made in accordance with information available at the time this presentation was prepared. Forecasts therefore embody risks and uncertainties.

Please be aware that actual results may turn out different from those forecast as our company's business is affected by many factors. Please reference page 12 for details on the above forecasts.

1. Corporate Group

The Elmic Systems Group is made up of three companies: Elmic Systems, Inc. (the Company), Airfolc Corporation, (a 78%-owned subsidiary based in Kyoto, Japan) and Wescom Inc. (a 25%-owned affiliate based in Osaka, Japan).

Airfolc Corporation specializes in the development of technology, such as programs (H.323 and others) related to software for Internet-linked embedded systems for processing voice and imaging data (VoIP).

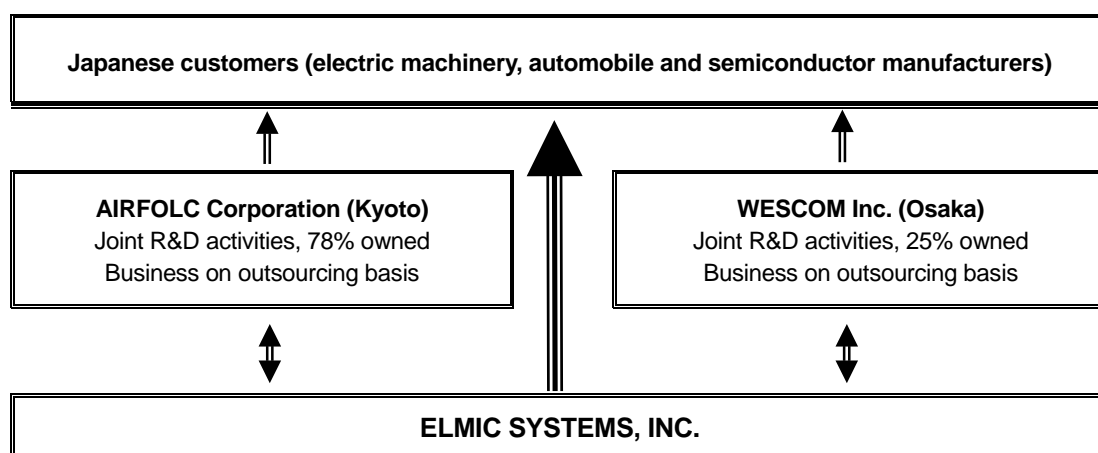
Wescom Inc. is a software house established in 1982 by Kazuya Murashima, who has served as deputy chairman of the Japan System House Association. This company is responsible for part of the Company's systems development activities, performing a broad range of software development ranging from applications for microprocessors to multi-purpose computers, stand-alone units and large-scale systems.

The Company signed a merger contract with Wescom, Inc. on March 25, 2005. The merger will result in the birth of Elmic Wescom, Inc. on July 1, 2005, assuming that approval is granted at an extraordinary shareholders meeting to be held on May 20, 2005.

Major products are as follows.

Major products		Description	Elmic Systems Group		
			ELMIC SYSTEMS	AIRFOLC	WESCOM
Manufactured products	Communications	Software and hardware for wire line and wireless communications	○		
	Internet protocol	Embedded TCP/IP modules, products for KASAGO application modules	○	○	○
	Real-time OS	The ELX exclusive RTOS, ITRON and other existing OS-related products, Windows CE resale and related products	○		
	System Integration (customization)	Products and system development using exclusive Elmic Systems key technologies, consigned products	○		○
Purchased products	Others	Products for Windows, Linux and TCP/IP and semiconductor-related products	○		

[Business Flowchart]



This chart shows only consolidated subsidiaries and equity-method affiliates.

2. Management Policies

(1) Fundamental Management Policy

The Elmic Systems Group is guided by the management philosophy of "Justice and Logic." The basic code of behavior is "Speedy, Compact, Perfect." In accordance with these precepts, the Group aims to be an organization capable of meeting the expectations of customers.

The Group is mainly involved in the provision of real-time OS (RTOS) products for embedded systems, the commercialization of software, and system integration (SI or customization) services that meet specific customer needs. Consequently, the Group depends heavily on expertise in the field of software.

Due to this dependence, the skill and experience of employees are critical to the Group's capabilities. The Group therefore places great importance on training employees so they can contribute to the operations of the Group and its customers.

(2) Fundamental Policy Regarding Distribution of Earnings

In the production of software, securing the funds required to implement medium- and long-term business plans as well as to conduct an aggressive R&D program is essential to the success.

The Company's fundamental policy is to return earnings to shareholders by paying a stable dividend while maintaining a sound operating base and financial position.

(3) Policy Regarding Reduction in Investment Unit

A reduction in the investment unit is regarded as an effective means of broadening the shareholder base and increasing trading volume in equity markets. Based on this position, the Group reduced its investment unit from 1,000 shares to 100 shares in August 2004. As a result, the number of shareholders increased from 861 on March 31, 2004 to 1,553 on March 31, 2005 and there was an increase in trading volume.

Management will continue to consider actions to increase the number of shareholders and trading volume in accordance with changes in the Company's share price, market conditions and other factors.

(4) Targeted Performance Indicators

The Elmic Systems Group is seeking to use its collective strengths, including those of consolidated subsidiaries, to maximize earnings, thereby returning to consolidated profitability at the operating level as soon as possible.

(5) Medium- and Long-Term Management Strategy

The Group is targeting the market associated with the ubiquitous information society, in which home appliances other than PCs are linked to the Internet. Unfortunately, market developments are not occurring as the Group had expected. Although manufacturers of electrical products, which are the users of the Group's products, continue to work on plans for Internet-linked products, the start of mass production will be much later than had been initially expected. Nevertheless, the industry and the market continue to prepare for the advent of the ubiquitous information society. The introduction of next-generation systems is definitely approaching, as is evident in rising sales of LCD televisions, the switch to digital terrestrial TV broadcasts and the growing use of fiber-optic networks. TCP/IP for embedded systems will be the fundamental communication software for these applications. That means IPv6 and its options will be essential as a core protocol. The Group is therefore continuing to invest in development programs aimed at commercializing IPv6 as quickly as possible.

Sales

The Elmic Systems Group is an independent organization having no affiliations with other companies. As such, the Group sells its products to numerous major producers of electrical products as well as to companies in many other industries. To serve this diverse customer base, the Group is upgrading its ability to conduct sales that seamlessly link expertise in marketing and the development of new technology. Sales target strategic customers and the introduction of new products that reflect market needs.

Development

The Group's core products are RTOS, communications software and other items that are distinguished by their technology and broad market coverage. From this base, the Group is developing new products and building systems (system integration or customization) using those products to meet customers' demands. The pace of technological progress in embedded systems is extremely rapid. It is imperative that Elmic Systems be prepared to offer the embedded products and services for next-generation equipment as well as products for the subsequent generation. For this purpose, the Group is focusing on acquiring new technology, fostering its engineers and many other necessary measures.

1) Communications Software

The Group is working with large manufacturers of electronics products to develop the next-generation wireless communication software that the IT market requires. The Group is also forming business alliances in its drive to acquire new technologies.

For producers of semiconductor manufacturing equipment, a major customer segment for Elmic Systems, the Company developed SoftCOM GEM, a system that conforms to the SEMI standard of the U.S. Plans call for strengthening marketing of this product, mainly by targeting applications involving 300mm wafers and LCD manufacturing equipment.

2) Internet Software

To solve the problem of an inadequate number of Internet addresses under the current IPv4 protocol, the Company and Treck Inc. (formerly Elmic System USA) are jointly developing IPv6, a next-generation protocol with a virtually unlimited number of addresses. The aim is to offer a broad range of products through collaboration with partners in Japan and overseas, this will include a variety of enhanced functions that are vital to the operation of embedded systems as well as options.

In addition, the Group is working on a product lineup that can meet a diverse spectrum of market demands, such as for security-related functions, incorporation in T-Engine, which is the next-generation version of ITRON, and VoIP products (H.323 and SIP).

3) Real-Time OS (RTOS)

Falling RTOS prices have largely erased the advantages of selling this software as a stand-alone product. Elmic Systems has considerable expertise in all types of RTOS, including open-source ITRON, embedded Linux, Window-CE and other OS, and the Company-developed ELX, among others. This knowledge gives the Company the technological skill to create systems that best match products being planned by client companies. The Company is also able to offer consulting and system integration services for a variety of applications.

4) System Integration

The Elmic Systems Group offers its consulting services, a particular Elmic Systems strength that links core technology and products, and system development services to enhance the total performance of systems used in embedded systems (finished products or consumer goods). With regard to embedded systems, the operation of software within a particular physical environment, such as the hardware, is critical. The experience of engineers is essential to delivering the needed performance. This experience has a great bearing on the ability

to use expertise gained over the Company's many years of operations as well as on the quality of services. For these reasons, Elmic Systems is placing priority on the education and development of its engineers.

5) Others

Elmic Systems has developed and started sales of iNHERITOR. This product was created to provide a means to continue using the software that was developed for use using the Company's ELX286 RTOS. This RTOS was incorporated in many FC98 industrial computers, a product that NEC has stopped manufacturing. Due to the benefits of sales promotion activities, demand for iNHERITOR, although limited, is increasing.

Elmic Systems aims to expand this market by using the core technologies, products and highly experienced engineering team, and resources of partner companies to develop products. As was mentioned above, the Company will merge with WESCOM Inc. on July 1, 2005. The objective is to transform the two companies into an organization that can break through the software layer to offer total solutions. This is to be accomplished by combining the sophisticated engineering team of WESCOM with the core technologies and products of Elmic Systems. The Company believes that synergies generated from the complementary technical skills of the two companies will lead to stability and growth in the operating results of Elmic Systems and WESCOM.

Management of Sales and Development Activities

Management systems are being strengthened from the standpoint of corporate governance. The Group is building a more clearly defined structure for submitting reports and directives and performing other management-related tasks covering sales, gross profit, delivery times, cost of sales, quality assurance, support services and other operating items.

(6) Key Issues

- a. Bolstering alliances
- b. Maintaining stable relationships with reliable vendors
- c. Training personnel
- d. Upgrading risk management
- e. Refining Data management systems
- f. Improving marketing capabilities

With expansion foreseen in markets where the Elmic Systems Group is active, the Group must minimize risk and maximize earnings in order to grow. The merger with WESCOM is aimed at achieving these goals. Therefore, several pressing issues involve using the benefits of the merger to generate concrete improvements.

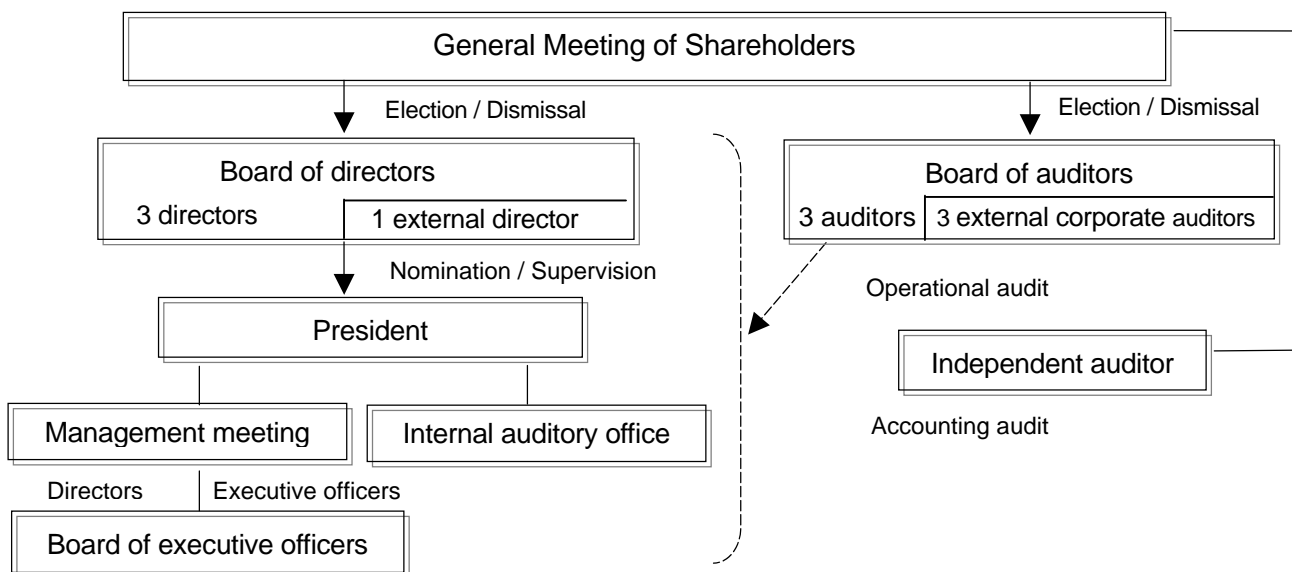
(7) Fundamental Approach to and Actions Regarding Corporate Governance

1) Fundamental approach to corporate governance

The most important goal of management is to sustain growth over the long term. This requires a decision-making system that is sound, efficient, speedy, and backed by managers who exercise strong leadership. The Company believes that such a system demands management that is transparent and devoted to the interests of shareholders. For this purpose, the Company quickly discloses financial information on its Internet site and through other channels.

2) Actions regarding corporate governance

a. Status of management oversight organization and other corporate governance systems for management decision-making, the execution of business activities and the supervision of operations



As of March 31, 2005, the Company had a corporate auditor system in which all three corporate auditors were from outside the Company. Furthermore, one of the Company's three directors was from outside the Company. None of these individuals have careers that involve the Company or any group companies.

b. Personnel, capital, business and other relationships between the Elmic Systems Group and external directors and external corporate auditors

The Company has an external director who is a president of IBT Corp. One external corporate auditor is a tax accountant and another is a president of Pacific Tsusho Co.

One external director is a director of a company that has a business relationship (a consulting contract) with the Company. One external corporate auditor is also a shareholder of the Company.

There are no other related party interests among other external directors.

c. Corporate governance actions during the past year

The Board of Directors, which makes decisions involving fundamental management policies and other important matters, held a meeting every month. In addition, the Company has an executive officer system to provide a framework for the rapid execution of decisions made by the directors. To increase the transparency of management, the Company is upgrading IR activities, including the expansion of its Internet site (adding English-language IR information, etc.)

d. Internal audits, corporate auditors and independent accountant

The accounting firm that serves as the independent accountant, the corporate auditors and the Internal Auditory Office hold regular meetings regarding annual plans, audit results and other matters, thereby facilitating better cooperation.

Internal Auditory Office

The Internal Auditing Office performs internal audits in accordance with an annual internal auditing plan and reports the results periodically to the directors. As prescribed in regulations for internal audits, the internal audits verify that all business units are conducting their operations in compliance with laws and regulations, the Articles of Incorporation and internal regulations. The objectives of these audits are to establish systems to ensure the proper execution of business activities prevent improper actions and maintain a compliance system.

Audits by corporate auditors

The Board of Auditors determines policies and plans for audits performed by the corporate auditors. The corporate auditors attend the monthly Board of Directors meetings and state their opinions. These auditors also attend other important meetings as necessary.

Independent accountant

The Company has an auditing contract with ShinNihon & Co. to serve as the independent accountant and perform financial audits. In the past fiscal year, this audit was conducted by certified public accountants Mr. Hiromu Hamayoshi, Mr. Toshio Hashimoto and Mr. Shoji Wakamatsu, all of whom are the designated employee, business execution employee. There were also a number of assistants. The Company paid the independent accountant an audit certification fee of ¥18 million. No other payments were made to the independent accountant.

(8) Item Concerning Parent Company

The Company has no parent company.

(9) Other Significant Items

Not applicable.

3. Results of Operations and Financial Position

(1) Results of Operations

1) Summary of year ended March 31, 2005

During the past fiscal year, Japan's economy benefited from improving corporate earnings and growth in capital expenditures. However, the economy was unable to stage a recovery as the employment picture remained difficult and consumer spending was flat. In addition, the unusual rise in crude oil prices appears to be causing companies to adhere to conservative management policies.

In the software industry, there was no significant growth in sales or earnings due to the persistent negative effect of restructuring that has been going on for several years. The home electronics industry benefited from demand for LCD televisions and related products due to the Athens Olympics. However, overall conditions were unfavorable because of falling prices for digital cameras and other products. The situation was similar among the companies that buy Elmic Systems products. Although these companies continue to conduct R&D involving ubiquitous-information products, full-scale mass production is not going to start in the near future.

2) Results by product category

- In communications products, there was no significant growth in sales of general-purpose communication boards and ISDN boards, both products the Company has manufactured for many years. At the same time, sales did not fall significantly either because of constant demand. However, there was no growth in new orders for ISDN boards because of the large volume of ISDN boards adopted for POS equipment at large stores in the prior fiscal year. Regarding SoftCom GEM300 software for semiconductor and LCD manufacturing equipment, the growing scale of potential orders is resulting in studies to create designs but extending the time required for processes leading to final delivery. Due to timing differences, orders were received during the fiscal year that did not contribute to sales. Overall, this segment recorded a 6.4% increase in sales to ¥376 million.
- In Internet protocol products, there were strong orders for TCP/IP for embedded systems but falling prices impacted sales of KASAGO (IPv4) products. Sales and royalties involving IPv6 products were held back by delays in the introduction and mass production of new products. Despite expectations for the advent of the ubiquitous information age, manufacturers of cell phones, information appliances and similar consumer products are postponing the development of products that have reached the planning stage. The result was a 55% drop in segment sales to ¥223 million.
- In real-time OS products, there was a decline in royalties just as for Internet protocol-related software. This was primarily attributable to a drop in sales caused by the growing use of open source operating systems. One example of this trend is raising sales of devices with embedded software for Linux. Nevertheless, the decline was generally in line with forecasts. The result was a 36.1% decrease in segment sales to ¥50 million.
- In system integration (customization) products, weakening demand for Internet (TCP/IP) software caused a large downturn in sales of system integration services for the incorporation of this software in products. Furthermore, more time is required from development to delivery because Internet software is being incorporated in next-generation products and new products. Another issue is the increasing complexity of responding to customer needs due to the large number of revisions in specifications. Due to these factors, there was a 26.4% decrease in segment sales to ¥454 million.

Total consolidated net sales decreased 27.6% to ¥1,254 million and ordinary income was ¥2 million compared with a ¥78 million losses one year earlier. After a provision for the reserve for doubtful receivables, the reversal of deferred taxes assets and other items, there was a net loss of ¥590 million compared with net income of ¥142 million one year earlier.

3) Research and development

R&D expenditures decreased ¥44 million to ¥80 million, which was 6.5% of net sales. Expenditures declined mainly because work on the TCP/IPv6 Internet-related software has passed the peak. At the end of December 2003, Elmic Systems sold Elmic Systems USA, Inc., a consolidated subsidiary that had been responsible for the major components of this software development project. The lower research and development expenditures in the past fiscal year also reflect this sale. Elmic Systems continues to outsource development work to this company, which is now called Treck, although on a smaller scale. Treck is developing options and enhancing related functions. In addition to this project, Elmic Systems will continue to invest in development activities to remain competitive as a software supplier, such as by creating more advanced versions of SoftCom GEM300 and ELX.

(2) Financial Position

Cash Flows

Cash and cash equivalents decreased ¥2 million during the current fiscal year.

There was a loss before income taxes and minority interest of ¥264 million, (compared with a ¥182 million gain one year earlier) and payments for acquisition of investment securities of ¥314 million (up 179.7% year-on-year), but there was a ¥264 million increase in trade receivables (up 221.0%), ¥236 million increase in reserve for doubtful receivables (zero one year earlier), ¥105 million in proceeds from sale of investment securities (down 23.6%). Due to these and other factors, cash and cash equivalents totaled ¥1,252 million at the end of the fiscal year.

Cash flows by category in the current fiscal year were as follows.

Operating activities

Net cash provided by operating activities was ¥214 million, 496.7% more than one year earlier.

Major uses of cash were the ¥264 million of net loss before income taxes and minority interest and cash was provided by ¥264 million of decrease in trade receivables, ¥236 million of increase in reserve for doubtful receivables, ¥76 million of depreciation and amortization (up 0.4%), and other items.

Investing activities

Net cash used in investing activities was ¥180 million, 198.9% more than one year earlier.

This was mainly the net result of ¥105 million in proceeds from sale of investment securities, payments of ¥314 million for the acquisition of investment securities, payments of ¥44 million (down 42.4%) for the acquisition of intangible assets, and other items.

Financing activities

Net cash used in financing activities was ¥36 million, 779.9% more than one year earlier.

This was due to cash dividends paid of ¥36 million, 21,347.1% more than one year earlier.

Trends in cash flow indicators were as follows.

	Year ended March 31, 2002	Year ended March 31, 2003	Year ended March 31, 2004	Year ended March 31, 2005
Shareholders' equity ratio (%)	87.5	83.8	86.1	86.6
Shareholders' equity ratio at market value (%)	54.5	28.5	88.5	101.6
Debt repayment multiple (years)	-	0.2	-	-
Interest coverage ratio	-	98.6	274.3	-

Notes: 1. The above figures are calculated as follows.

Shareholders' equity ratio: shareholders' equity divided by total assets

Shareholders' equity ratio at market value: market capitalization divided by total assets

Debt repayment multiple: interest-bearing debt divided by operating cash flows

Interest coverage ratio: operating cash flows divided by interest expenses

2. All indicators are calculated based on consolidated financial figures.
3. Market capitalization is calculated by multiplying the value of the Company's stock at the close of each period by the total number of shares issued at the end of the period.
4. Operating cash flows are calculated using the figures for operating cash flows in the consolidated statements of cash flows. Net interest-bearing debt is the sum of all liabilities on the consolidated balance sheets for which interest payments are made. Interest expenses as shown in the consolidated statements of cash flows are used to calculate the interest coverage ratio.
5. The fiscal 2001 (ended March 2002) debt repayment multiples and interest coverage ratios are not shown because operating cash flows were negative in this period.
6. The fiscal 2003 (ended March 2004) debt repayment multiple are not shown because there was no interest-bearing debt in this period.
7. The fiscal 2004 (ended March 2005) debt repayment multiple and interest coverage ratio are not shown because there was no interest-bearing debt or interest expenses in this year.

(3) Outlook for the Fiscal Year Ending March 2006

Work continues on enhancing options for TCP/IP (KASAGO) even though manufacturers of finished electrical and electronics products are not moving forward with plans for products for the ubiquitous information age. The Company is therefore confident that TCP/IP (KASAGO) is becoming an increasingly appealing product. Regarding system integration, there is a growing tendency for most sales to be recorded at the end of each fiscal year due to the longer time required until deliveries are made. The outlook is for contributions and sales and earnings from iNHERITOR as market acceptance grows for this product, which was introduced as the successor to NEC's factory PC.

While adopting a conservative outlook for market trends, the Company is dedicated to achieving concrete and consistent improvements in operating results while building a sounder financial position. At the heart of this drive will be improving internal operations by raising the efficiency of development activities and improving activities targeting customers by conducting effective marketing activities. For this purpose, the Company will invest in personnel and work on transforming its business model. As part of its equity policy, the Company Board of Directors on May 19, 2005 approved a resolution to reduce the capital surplus.

As part of the above activities, the Elmic Systems signed a merger contract on March 25, 2005 with Wescom Inc. under which the two companies will merge on July 1, 2005.

Wescom Inc. is a software house established in 1982 by Kazuya Murashima, who has served as deputy chairman of the Japan System House Association. This company performs a broad range of software development ranging from applications for microprocessors to multi-purpose computers, stand-alone units and large-scale systems.

Due to the complementary strengths of the two companies involving sales and technologies, Elmic Systems expects that the merger will yield significant synergies that will lead to growth in markets served, more powerful technologies and other advantages.

Due to the above factors, the Company is forecasting consolidated net sales of ¥1,698 million, ordinary income of ¥60 million and net income of ¥8 million in the fiscal year ending in March 2006. On a non-consolidated basis, the forecast is for net sales of ¥1,655 million, ordinary income of ¥79 million and net income of ¥27 million.

These forecasts are based on management's judgments in accordance with information that is currently available. Actual results may differ significantly due to a variety of factors.

Therefore, investors are cautioned not to make investment decisions based solely on these forecasts. Factors that can affect operating results include, but are not limited to, the economic environment in major markets, changes in demand and prices for products, rapid advances in technology, changes in exchange rates, and revisions in regulations and accounting standards in Japan and overseas.

Due to the seasonal nature of the Company's operating results, in which the majority of deliveries and sales occur during the second half of each fiscal year.

4. Other Important Information

Presented below are a list of risk factors that can affect the Company's business operations and other aspects of its activities. This information is being supplied from the standpoint of conducting an aggressive disclosure program for investors by providing information on items that are believed to be important to reaching investment decisions. This list even includes items that may not necessarily correspond to obvious risk factors. The Company is aware of these risk factors and is taking measures to respond in the event that any of these problems occurs. However, investors should carefully read this list and all information in this document, as well as gather information from other sources so that all factors can be carefully considered before reaching an investment decision.

Risks concerning business operations

Communication Risk

The Company is acquiring new technology primarily through joint development programs and other forms of alliances. In the event that one or more alliances are terminated, the Company could have difficulty acquiring new technology, an event that could have a material impact on operating results.

Internet protocol risk

KASAGO TCP/IP (IPv4) is employed by a large number of users and sales of KASAGO IPv6 have been started based on these existing users. At present, a number of Japanese companies, mostly large manufacturers of electrical equipment, are using KASAGO IPv6 at no charge to conduct evaluations and research. Elmic Systems is now in phase 2 of the development process, which mainly entails the development of IPv6 optional software packages. Any delay in the market launch of these packages could have an impact on operating results.

System integration risk

By maintaining good relationships with vendors, the Company strives to maintain access to qualified personnel, sustain the profitability of system integration operations and maintain a stable level of orders. Any difficulties concerning these relationships could have a material impact on operating results.

Fables Policy

Elmic Systems designs hardware but has no manufacturing facilities of its own. The development and manufacturing companies listed below, and the new development and manufacturing outsourcing companies, are used to maintain a flexible design and manufacturing capability. This enables the Company to avoid the risk of holding excessive inventories of components and production facilities. External development and manufacturing outsourcing factories are utilized under outsourcing contracts, and every effort is made to prevent problems concerning quality. As products developed by Elmic Systems are assets of the Company, management is conducted to permit the continuous manufacture of these products at the factories of outsourcing partners.

Reliance on External Vendors (Orders Placed)

During the past fiscal year, the Company placed a total of ¥280 million of orders with external vendors.

Major companies and orders placed are shown below.

This table does not include Airfolc Corporation, Wescom Inc.

Yen in thousands

Vendor	Product	Orders		Remarks
		Fiscal year ended Mar. 31, 2004		
			Share (%)	
Treck Inc. (Elmic Systems USA, Inc.)	Software development	39,809	14.2	
TKS Co., Ltd.	Customized software	31,608	11.2	
Toshiba Personal Computer System Corp	Customized software	30,198	10.8	
Kuzumi electron Co., Ltd.	Communication boards	27,409	9.7	
Yamaki Electric Corporation	Communication boards	26,125	9.3	
Other (39 companies)		125,751	44.8	-
Total		280,903	100.0	-

Note: The above amounts do not include consumption taxes.

Elmic Systems closely monitors the management, manufacturing supervision, quality assurance and other aspects of the operations of these companies. Furthermore, precautions are taken to diversify risk to avoid excessive reliance on any particular vendor. Nevertheless, a problem in the ability of a vendor to conduct operations could affect the Company's ability to ship products. Therefore, the inability to ship products at the required time due to a problem involving the design, manufacturing or quality assurance capabilities of a vendor could have a material impact on operating results.

Human resources

Employees involved in marketing and development activities will play an important role in the expansion of new businesses. As Elmic Systems operates in a small industry and there are a limited number of talented individuals, there is a risk that the Company may not be able to hire the necessary personnel due to intense competition. The Company is currently reviewing its personnel system in order to attract skilled individuals and motivate employees. The Company will further upgrade its target management system and compensation structure to reflect the capabilities of each employee. Any difficulty in hiring or retaining the necessary personnel could hinder the Company's ability to reach its medium- and long-term strategic goals and have a material impact on operating results.

Investments

Elmic Systems has consistently invested in its core business. At this time, management plans to aggressively conduct a broad spectrum of business activities that are based on existing products and services. As part of this drive, the Company will be establishing subsidiaries and forming alliances in Japan and overseas.

The investments required by these actions may be large compared to the size of the Company, creating greater risks involving the Company's financial position and business operations. However, it is impossible to accurately predict the impact on the Company's operations of conditions at companies in which it has invested. In some cases, the Company may not be able to recover its investments.

Significant alliances

Significant contracts signed during the current fiscal year was as follows.

The Elmic Systems Group enters into a large number of business agreements and alliances to acquire new technologies. Most of these actions involve systems that will be commercialized in the future. Any leaks of such information could be harmful these customers. Consequently, the Company enters into confidentiality contracts with all customers and external vendors in addition to contracts for the placement of orders. The following information is therefore provided only to the extent possible under these confidentiality contracts.

Alliances of the type described in (6) Key Issues are conducted under strict secrecy until the products of the alliance partners are shipped. Any leak of information concerning these activities may not only cause a termination of the alliance, but could also subject the Company to a lawsuit seek payment of damages. Consequently, the following list of alliances contains information only to the extent possible under secrecy agreements with each company.

a. FUJITSU LSI SOLUTION LIMITED

Purpose: Placement of KASAGO TCP/IP on the custom LSIs for home routers made by this company

Personnel: None

b. Hitachi ULSI Systems Co., Ltd.

Purpose: Business alliance for broadband communications for embedded systems, placement of KASAGO TCP/IP (IPv4, IPv6) on Hitachi LSIs

Personnel: None

5. Consolidated Financial Statements

(1) Consolidated Balance Sheets

Account	Period	FY2003 As of March 31, 2004		FY2004 As of March 31, 2005		YoY change
		¥ thousands	%	¥ thousands	%	¥ thousands
Assets						
I Current assets						
1. Cash and deposits		154,251		166,372		12,120
2. Notes and accounts receivable - trade		686,551		410,762		(275,788)
3. Securities		1,100,636		1,086,333		(14,303)
4. Inventories		116,614		92,753		(23,861)
5. Deferred tax assets - current		51,832		29,535		(22,297)
6. Other current assets		80,067		46,920		(33,147)
Reserve for doubtful receivables		(264)		(179)		84
Total current assets		2,189,690	68.0	1,832,498	74.4	(357,191)
II Fixed assets						
1. Property, plant and equipment						
(1) Buildings		12,577		13,845		
Accumulated Depreciation		8,775	3,802	4,600	9,245	5,442
(2) Tools, furniture and fixtures		102,836		94,427		
Accumulated Depreciation		91,145	11,691	86,222	8,204	(3,486)
Total property, plant and equipment		15,493	0.5	17,449	0.7	1,955
2. Intangible assets		160,971	5.0	112,983	4.6	(47,988)
3. Investments and other assets						
(1) Investment securities	*1	215,784		416,546		200,762
(2) Long-term loans receivable		147,680		6,475		(141,205)
(3) Deferred tax assets - non-current		294,773		756		(294,016)
(4) Claim in bankruptcy		-		241,613		241,613
(5) Other assets		198,297		73,744		(124,553)
Reserve for doubtful receivables		(1,400)		(238,429)		(237,029)
Total investments and other assets		855,136	26.5	500,708	20.3	(354,428)
Total fixed assets		1,031,602	32.0	631,141	25.6	(400,460)
Total assets		3,221,292	100.0	2,463,640	100.0	(757,652)

Account	Period	FY2003 As of March 31, 2004		FY2004 As of March 31, 2005		YoY change
		¥ thousands	%	¥ thousands	%	¥ thousands
Liabilities						
I Current liabilities						
1. Accounts payable - trade		127,041		69,072		(57,968)
2. Income taxes payable		5,971		13,592		7,621
3. Deferred tax liabilities		-		73		73
4. Reserve for accrued bonuses		45,691		31,782		(13,909)
5. Other current liabilities		48,030		35,800		(12,230)
Total current liabilities		226,735	7.1	150,321	6.1	(76,413)
II Long-term liabilities						
1. Reserve for employees' retirement benefits		-		484		484
2. Reserve for directors' retirement benefits		161,499		171,229		9,730
3. Other long-term liabilities		52,094		-		(52,094)
Total long-term liabilities		213,593	6.6	171,714	7.0	(41,879)
Total liabilities		440,329	13.7	322,036	13.1	(118,293)
Minority interest						
Minority interest		7,006	0.2	7,333	0.3	326
Shareholders' equity						
I Common stock	*2	1,160,041	36.0	1,160,041	47.1	-
II Capital surplus		1,459,152	45.3	1,459,152	(59.2)	-
III Retained earnings		334,189	10.4	(292,094)	(11.9)	(626,284)
IV Net unrealized gain (loss) on other securities		5,757	0.2	(7,607)	(0.3)	(13,365)
V Treasury stock	*3	(185,184)	(5.8)	(185,220)	(7.5)	(36)
Total shareholders' equity		2,773,956	86.1	2,134,270	86.6	(639,686)
Total liabilities, minority interest and shareholders' equity		3,221,292	100.0	2,463,640	100.0	(757,652)

(2) Consolidated Statements of Income

Account	Period	FY2003 From April 1, 2003 to March 31, 2004		FY2004 From April 1, 2004 to March 31, 2005		YoY change		
		¥ thousands	%	¥ thousands	%	¥ thousands		
I Net sales			1,733,403	100.0		1,254,501	100.0	(478,902)
II Cost of sales	*2		815,492	47.0		667,803	53.2	(147,689)
Gross profit			917,911	53.0		586,697	46.8	(331,214)
III SG&A	*1,2		995,720	57.5		608,072	48.5	(387,648)
Operating loss			77,809	(4.5)		21,374	(1.7)	56,434
IV Non-operating income								
1. Interest income		1,476			11,287			
2. Dividends income		1,015			110			
3. Equity in earnings of affiliates		11,180			7,739			
4. Gain on anonymous partnerships		7,185			4,285			
5. Other non-operating income		2,331	23,188	1.4	3,539	26,960	2.2	3,772
V Non-operating expenses								
1. Interest expense		131			-			
2. Additional taxes		-			3,054			
3. Foreign exchange losses		23,835	23,966	1.4	394	3,449	0.3	(20,517)
Ordinary income (loss)			(78,587)	(4.5)		2,136	0.2	80,724
VI Extraordinary income								
1. Gain on reversal from doubtful receivables		413			-			
2. Gain on cancellation of leveraged lease		-			49,179			
3. Gain on sales of investment securities		22,904			3,980			
4. Gain on sale of subsidiary stock		258,801	282,119	16.3	-	53,159	4.2	(228,959)
VII Extraordinary loss								
1. Loss on removal of fixed assets	*3	232			22,861			
2. Provision of reserve for doubtful receivables		-			236,944			
3. Loss on revaluation of membership		-			900			
4. Loss on revaluation of investment securities		10,735			-			
5. Loss on revaluation of inventories		-			34,601			
6. Prior year consumption taxes, etc.		10,466			-			
7. Head office relocation expenses		-	21,434	1.3	24,482	319,790	25.5	298,356
Net income (losses) before income taxes and minority interest			182,097	10.5		(264,494)	(21.1)	(446,591)
Income taxes - current		6,091			5,993			
Income taxes - deferred		34,555	40,647	2.3	319,351	325,344	25.9	284,697
Minority interest			(699)	(0.0)		326	0.0	1,026
Net income (losses)			142,148	8.2		(590,166)	(47.0)	(732,315)

(3) Consolidated Statements of Retained Earnings

Account	Period	FY2003 From April 1, 2003 to March 31, 2004		FY2004 From April 1, 2004 to March 31, 2005		YoY change
		¥ thousands		¥ thousands		¥ thousands
Capital surplus						
I	Capital surplus at beginning of period		1,459,152		1,459,152	-
II	Capital surplus at end of period		1,459,152		1,459,152	-
Retained earnings						
I	Retained earnings at beginning of period		192,041		334,189	142,148
II	Increase in retained earnings					
1.	Net income	142,148	142,148	-	-	(142,148)
III	Decline in retained earnings					
1.	Cash dividends	-	-	36,117		
2.	Net loss	-	-	590,166	626,284	626,284
IV	Retained earnings at end of period		334,189		(292,094)	(626,284)

(4) Consolidated Statements of Cash Flows

Account	Period	FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005	YoY change
		¥ thousands	¥ thousands	¥ thousands
I Cash flows from operating activities				
Net income (losses) before income taxes and minority interest		182,097	(264,494)	(446,591)
Depreciation and amortization		76,587	76,885	298
Amortization of long-term prepaid expenses		247	208	(39)
Equity in earnings of affiliates		(11,180)	(7,739)	3,440
Increase (decrease) in reserve for doubtful receivables		(363)	236,944	237,308
Decrease in reserve for accrued bonuses		(4,508)	(13,909)	(9,400)
Increase (decrease) in reserve for employees' retirement benefits		(19)	484	503
Increase in reserve for directors' retirement benefits		1,273	9,730	8,457
Interest and dividends income		(2,491)	(11,397)	(8,905)
Interest expense		131	-	(131)
Gain on anonymous partnerships		(7,185)	(4,285)	2,900
Foreign exchange gain (loss)		667	(57)	(724)
Gain on cancellation of leveraged lease		-	(49,179)	(49,179)
Gain on sales of investment securities		(22,904)	(3,980)	18,924
Loss on removal of fixed assets		232	22,861	22,628
Gain on sale of subsidiary stock		(258,801)	-	258,801
Loss on revaluation of investment securities		10,735	-	(10,735)
Loss on revaluation of golf club memberships		-	900	900
Decrease in notes and accounts receivable-trade		82,267	264,059	181,792
Increase in inventories		(11,801)	23,861	35,663
Decrease in accounts payable-trade		(4,310)	(57,968)	(53,658)
Decrease (increase) in other assets		29,043	(10,997)	(40,040)
Increase (decrease) in other liabilities		(15,955)	8,553	24,509
Decrease in suspense receipt of consumption taxes		(4,988)	(11,768)	(6,780)
Subtotal		38,772	208,712	169,940
Interest and dividends received		4,991	13,100	8,108
Interest paid		(131)	-	131
Income taxes paid		(7,688)	(7,342)	346
Net cash provided by operating activities		35,943	214,469	178,526

Account	Period	FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005	YoY change
		¥ thousands	¥ thousands	¥ thousands
II Cash flows from investing activities				
Payments for acquisition of property, plant and equipment		(3,169)	(8,669)	(5,499)
Payments for acquisition of intangible assets		(77,819)	(44,849)	32,969
Payments for acquisition of investment securities		(112,280)	(314,048)	(201,768)
Gain on sales of investment securities		138,784	105,980	(32,804)
Decline in cash and cash equivalents due to sale of consolidated subsidiary		(4,514)	-	4,514
Proceeds of cancelled equity		-	47,613	47,613
Payments for long-term loans receivable		(700)	-	700
Proceeds from collection of long-term loans		1,010	760	(250)
Proceeds from collection of long-term accounts receivable - other		-	25,794	25,794
Proceeds from return of leasehold and security deposits		4,645	24,679	20,033
payments for leasehold and security deposits		-	(16,006)	(16,006)
Others		(6,386)	(1,897)	4,489
Net cash used in investing activities		(60,429)	(180,642)	(120,213)
III Cash flows from financing activities				
Payments for finance lease liabilities		(3,366)	-	3,366
Payments for acquisition of treasury stock		(564)	(36)	527
Cash dividends paid		(168)	(36,031)	(35,863)
Net cash used in financing activities		(4,098)	(36,067)	(31,968)
IV Effect of exchange rate changes on cash and cash equivalents		5,434	57	(5,377)
V Decrease in cash and cash equivalents		(23,149)	(2,182)	20,967
VI Cash and cash equivalents at beginning of period		1,278,037	1,254,887	(23,149)
VII Cash and cash equivalents at end of period	*1	1,254,887	1,252,705	(2,182)

Significant Accounting Policies in the Preparation of Consolidated Financial Statements

<div style="text-align: right;">Period</div> <div style="text-align: left;">Item</div>	<div style="text-align: center;">FY2003</div> <div style="text-align: center;">From April 1, 2003 to March 31, 2004</div>	<div style="text-align: center;">FY2004</div> <div style="text-align: center;">From April 1, 2004 to March 31, 2005</div>
<p>1. Scope of consolidation</p>	<p>(1) Consolidated subsidiaries: 1 Names of consolidated subsidiaries: AIRFOLC Corporation Effective March 31, 2004, Elmic Systems USA, Inc, a consolidated subsidiary in prior years, has been excluded from the consolidation since the Company sold its entire equity stake in the entity on December 25, 2003. The consolidated financial statements include Elmic Systems USA, Inc.'s statements of income and statements of cash flows for the period from Jan. 1, 2003 to Dec. 31, 2003.</p> <p>(2) Unconsolidated subsidiaries: 0</p>	<p>(1) Consolidated subsidiaries: 1 Names of consolidated subsidiaries: AIRFOLC Corporation</p> <p>(2) Unconsolidated subsidiaries: 0</p>
<p>2. Equity method accounting</p>	<p>(1) Affiliates accounted for by the equity method of accounting: 1 Affiliate name: WESCOM Inc.</p> <p>(2) RockHand Technology, an equity-method affiliate in prior periods, is excluded from the scope of affiliates accounted for by the equity method, given the fact that it has a very minor effect on consolidated net income/loss (equity in earnings) and consolidated retained earnings (equity in earnings) and is relatively insignificant in the context of consolidated financial statements.</p>	<p>(1) Affiliates accounted for by the equity method of accounting: 1 Affiliate name: WESCOM Inc.</p> <p>(2) Same as on the left.</p>
<p>3. Balance sheet dates of subsidiaries</p>	<p>The consolidated financial statements include the accounts of the following consolidated subsidiaries, of which the fiscal year ends on a different day:</p> <p style="padding-left: 40px;">AIRFOLC Corporation Fiscal year-end: Feb. 28</p> <p>In the preparation of consolidated financial statements for the fiscal year, the financial statements of the subsidiary for its respective fiscal year have been used. With respect to significant transactions, which occurred after the balance sheet date of the consolidated subsidiary, necessary adjustment has been made in the consolidated financial statements.</p>	<p>The consolidated financial statements include the accounts of the following consolidated subsidiaries, of which the fiscal year ends on a different day:</p> <p style="padding-left: 40px;">AIRFOLC Corporation Fiscal year-end: Feb. 28</p> <p style="text-align: center;">Same as on the left.</p>
<p>4. Accounting standards</p>	<p>A. Valuation criteria and methods for significant assets:</p> <p>(1) Securities Held-to-maturity securities Valued using the amortized cost method</p> <p>Affiliated company stock Stated at cost, cost using the moving average method</p>	<p>A. Valuation criteria and methods for significant assets:</p> <p>(1) Securities -</p> <p>Affiliated company stock Same as on the left.</p>

Item \ Period	FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
	<p>Other securities</p> <p>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)</p> <p>Securities without market quotations: Stated at cost, cost using the moving average method</p> <p>(2) Inventories Merchandise: Stated at cost, cost being determined by the moving average method</p> <p>Products, work in process and raw materials: Stated at cost, cost being determined by the period average method</p> <p>B. Depreciation and amortization of significant depreciable assets</p> <p>(1) Property, plant and equipment The Company and its domestic subsidiaries compute depreciation using the declining balance method, in accordance with Corporation Tax laws. Overseas-consolidated subsidiaries compute depreciation using the straight-line method in accordance with the generally accepted accounting standards of the countries of their domicile.</p> <p>(2) Intangible assets The Company and its domestic subsidiaries amortize capitalized costs using two alternate methods, which is higher, depreciation based on estimated sales volume or the straight-line method based on remaining period to expiration. Software for internal use is amortized using the straight-line method over its estimated useful life of five years.</p> <p>C. Recognition of reserves</p> <p>(1) Reserve for doubtful receivables To prepare for credit losses on accounts receivable, the Company and its domestic subsidiaries 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 subsidiaries provide allowances for credit losses based on a case-by-case determination of collectibility.</p>	<p>Other securities</p> <p>Securities with market quotations Same as on the left.</p> <p>Securities without market quotations: Same as on the left.</p> <p>(2) Inventories Merchandise: Same as on the left.</p> <p>Products, work in process and raw materials: Same as on the left.</p> <p>B. Depreciation and amortization of significant depreciable assets</p> <p>(1) Property, plant and equipment Depreciation using the declining balances method, in accordance with Corporation Tax laws.</p> <p>(2) Intangible assets Software for sales is amortized based on the capitalized costs using two alternate methods, which is higher, depreciation based on estimated sales volume or the straight-line method based on remaining period to expiration. Software for internal use is amortized using the straight-line method over its estimated useful life of five years.</p> <p>C. Recognition of reserves</p> <p>(1) Reserve for doubtful receivables To prepare for credit losses on accounts receivable, an allowance is estimated equal to the 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.</p>

Period Item	FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
	<p>(2) Reserve for accrued bonuses As a means of providing for bonus obligations, the Company and its domestic subsidiaries designates in the reserve account an amount accrued for the current fiscal year among the estimated future obligations.</p> <p>(3) Reserve for employees' retirement benefits To provide for employee retirement benefits, the Company provides an allowance for retirement benefits in the amount deemed to have accrued, determined based on the estimated retirement benefit obligations and pension assets on the balance sheet date. The Company accounted ¥109 thousand as pre-paid pension expenses in the current fiscal year. The amount represents pension fund assets at fair value in excess of the retirement benefit liability.</p> <p>(4) Reserve for directors' retirement benefits To provide for directors' retirement benefits, the Company provides an allowance pursuant to the Company's rules on directors' retirement benefits.</p> <p>D. Accounting for lease transactions Overseas consolidated subsidiaries account 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.</p> <p>E. Other significant accounting policies in the preparation of consolidated financial statements for the fiscal year (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 thousands investment at the time of participation is 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 of the anonymous partnership's net income (as recorded in the settlement of accounts for the fiscal year), applicable to the current consolidated fiscal year, proportional to the Company's investment in the anonymous partnership is recognized as a gain or loss on investment in the anonymous partnership.</p>	<p>(2) Reserve for accrued bonuses As a means of providing for bonus obligations, an allowance for retirement benefits is provided in the amount deemed to have accrued for the current fiscal year among the estimated future obligations.</p> <p>(3) Reserve for employees' retirement benefits To provide for employee retirement benefits, the Company provides an allowance for retirement benefits in the amount deemed to have accrued, determined based on the estimated retirement benefit obligations and pension assets on the balance sheet date.</p> <p>(4) Reserve for directors' retirement benefits Same as on the left.</p> <p>D. -</p> <p>E. Other significant accounting policies in the preparation of consolidated financial statements for the fiscal year (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 thousands investment at the time of participation is 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 of the anonymous partnership's net income (as recorded in the settlement of accounts for the fiscal year), applicable to the current consolidated fiscal year, proportional to the Company's investment in the anonymous partnership is recognized as a gain or loss on investment in the anonymous partnership. Since the lease was cancelled at the end of the current fiscal year, the Company booked its share of residual assets (¥49,179 thousand) as "Gain on cancellation of leveraged lease" under "Extraordinary income".</p>

Item \ Period	FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
	(2) Accounting treatment for consumption taxes Consumption taxes are accounted by the tax exclusion method.	(2) Accounting treatment for consumption taxes Same as on the left.
5. Evaluation of assets and liabilities of consolidated subsidiaries	The market value method is adopted fully for the evaluation of assets and liabilities of the consolidated subsidiaries.	Same as on the left.
6. Appropriation of earnings	The consolidated statement of retained earnings is prepared based on the appropriation of earnings as finalized at the relevant consolidated entities in the consolidation fiscal year under review.	Same as on the left.
7. Scope of cash and cash equivalents on consolidated statement of cash flows	For the purpose of consolidated statement 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.	Same as on the left.

Reclassifications

FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
<p>Consolidated balance sheets</p> <p>Effective the current consolidated fiscal year, Long-term Loans Receivable, included in Others under Investments and Other Assets in prior periods, is reclassified and presented as a separate line item since Long-term Loans Receivable exceeded 1/100 of total assets in the current consolidated fiscal year.</p> <p>In the previous fiscal year, Long-term Loans Receivable totaled ¥7,275 thousand.</p> <p>Consolidated Statements of Cash Flows</p> <p style="text-align: center;">-</p>	<p>Consolidated balance sheets</p> <p style="text-align: center;">-</p> <p>Consolidated Statements of Cash Flows</p> <p>“Payments for leaseholds and security deposits,” included in “Others” under “Cash flows from investing activities” in the prior period, is reclassified and presented as a separate line item, given the increase in the materiality of impact in the context of the consolidated financial statements.</p> <p>In the prior period, “Payments for leaseholds and security deposits,” included in “Others” under “Cash flows from investing activities” amounted to ¥3,934 thousand.</p>

Supplementary Information

FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
<p>_____</p>	<p>The Company signed a merger agreement with Wescom Inc. on March 25, 2005.</p> <p>(1) Merger date July 1, 2005</p> <p>(2) Method of merger Elmic Systems will absorb and merge with Wescom. Elmic Systems will be the surviving company and Wescom will be dissolved.</p> <p>(3) Merger ratio The Company will exchange six common shares of the Company for one share of WESCOM Inc. However, the 25,000 WESCOM Inc. shares, currently held by the Company, will not be allocated.</p> <p>(4) Payment due to merger Not applicable.</p> <p>(5) Shares to be issued for the merger In connection with the merger, 450,000 common shares will be allocated to its WESCOM Inc. shareholders. The treasury stock held by the Company will be allocated instead of issuing new shares.</p> <p>(6) Dividend reckoning date The dividend reckoning date of the Company's shares allocated to WESOM Inc. shareholders will be April 1, 2005.</p>

Notes to Consolidated Financial Statements

Notes to consolidated balance sheets

Yen in thousands

FY2003 As of March 31, 2004	FY2004 As of March 31, 2005
*1. Affiliated company stock:	*1. Affiliated company stock:
Investment securities (equity securities) 87,070	Investment securities (equity securities) 91,872
*2. Number of shares outstanding	*2. Number of shares outstanding
Common stock 5,307,680 shares	Common stock 5,307,680 shares
*3. Number of treasury stock held by the consolidated subsidiaries and affiliates accounted for under the equity method	*3. Number of treasury stock held by the consolidated subsidiaries and affiliates accounted for under the equity method
Common stock 491,950 shares	Common stock 491,998 shares

Notes to consolidated statements of income

Yen in thousands

FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
*1. Principal components and amounts of SG&A expenses are as follows:	*1. Principal components and amounts of SG&A expenses are as follows:
Wages & allowances: 382,320	Wages & allowances: 170,671
Provision of reserve for accrued bonuses: 24,683	Provision of reserve for accrued bonuses: 12,913
Provision of reserve for directors' retirement allowance: 6,965	Provision of reserve for directors' retirement allowance: 9,730
R&D: 79,078	R&D: 80,978
*2. R&D expenses included in SG&A expenses are as follows:	*2. R&D expenses included in SG&A expenses are as follows:
125,899	80,978
*3. A significant component of the loss from removal of fixed assets represents a loss on removal of tools, furniture and fixtures.	*3. Losses on removal of fixed assets are as follows:
	Buildings 1,786
	Tools, furniture and fixtures 901
	Software 20,174

Notes to consolidated statements of cash flows

Yen in thousands

FY2003 From April 1,2003 to March 31, 2004	FY2004 From April 1,2004 to March 31, 2005																
<p>1. Reconciliation of cash and cash equivalents of the statements of cash flows and account balances of consolidated balance sheets for the fiscal year is made as follows:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td></td> <td style="text-align: right;">As of March 31, 2004</td> </tr> <tr> <td>Cash and deposits:</td> <td style="text-align: right;">154,251</td> </tr> <tr> <td>Short-term investments with original maturities of less than 3 months:</td> <td style="text-align: right;">1,100,636</td> </tr> <tr> <td style="border-top: 1px solid black;">Cash and cash equivalents:</td> <td style="text-align: right; border-top: 1px solid black;">1,254,887</td> </tr> </table>		As of March 31, 2004	Cash and deposits:	154,251	Short-term investments with original maturities of less than 3 months:	1,100,636	Cash and cash equivalents:	1,254,887	<p>1. Reconciliation of cash and cash equivalents of the statements of cash flows and account balances of consolidated balance sheets for the fiscal year is made as follows:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td></td> <td style="text-align: right;">As of March 31, 2004</td> </tr> <tr> <td>Cash and deposits:</td> <td style="text-align: right;">166,372</td> </tr> <tr> <td>Short-term investments with original maturities of less than 3 months:</td> <td style="text-align: right;">1,086,333</td> </tr> <tr> <td style="border-top: 1px solid black;">Cash and cash equivalents:</td> <td style="text-align: right; border-top: 1px solid black;">1,252,705</td> </tr> </table>		As of March 31, 2004	Cash and deposits:	166,372	Short-term investments with original maturities of less than 3 months:	1,086,333	Cash and cash equivalents:	1,252,705
	As of March 31, 2004																
Cash and deposits:	154,251																
Short-term investments with original maturities of less than 3 months:	1,100,636																
Cash and cash equivalents:	1,254,887																
	As of March 31, 2004																
Cash and deposits:	166,372																
Short-term investments with original maturities of less than 3 months:	1,086,333																
Cash and cash equivalents:	1,252,705																
<p>2. Significant components of assets and liabilities of consolidated subsidiary excluded from the consolidation due to sale of equity stake: Significant components of assets and liabilities of Elmic Systems USA, Inc. excluded from the consolidation due to sale of equity stake in the entity:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td>Current assets</td> <td style="text-align: right;">31,512</td> </tr> <tr> <td>Fixed assets</td> <td style="text-align: right;">77,557</td> </tr> <tr> <td style="border-top: 1px solid black; border-bottom: 3px double black;">Total assets</td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">109,070</td> </tr> <tr> <td>Current liabilities</td> <td style="text-align: right;">184,108</td> </tr> <tr> <td style="border-top: 1px solid black; border-bottom: 3px double black;">Total liabilities</td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">184,108</td> </tr> </table>	Current assets	31,512	Fixed assets	77,557	Total assets	109,070	Current liabilities	184,108	Total liabilities	184,108	<p>2. -</p>						
Current assets	31,512																
Fixed assets	77,557																
Total assets	109,070																
Current liabilities	184,108																
Total liabilities	184,108																

Accounting for Leases

Not applicable.

Securities

As of March 31, 2004

Securities classified as other securities

1. Securities with market quotations

Yen in thousands

Security	Acquisition cost	Carrying value	Unrealized gain or loss
Securities whose carrying value exceeds their acquisition cost			
(1) Equity securities	8,060	11,800	3,740
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	102,000	105,560	3,560
Subtotal	110,060	117,360	7,300
Securities whose carrying value does not exceed their acquisition cost			
(1) Equity securities	-	-	-
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	-	-	-
Subtotal	-	-	-
Total	110,060	117,360	7,300

2. Securities sold during the current fiscal year

Yen in thousands

Total amount sold	Gains on sales	Losses on sales
138,784	22,904	-

3. Securities without market quotations

Yen in thousands

	Carrying value
(1) Other securities	
Money management funds	998,513
Free financial funds	100,019
Medium-term government bond funds	2,104
Unlisted stock	11,354
Total	1,111,990

As of March 31, 2005

Securities classified as other securities

1. Securities with market quotations

Yen in thousands

Security	Acquisition cost	Carrying value	Unrealized gain or loss
Securities whose carrying value exceeds their acquisition cost			
(1) Equity securities	8,060	9,380	1,320
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	-	-	-
c. Others	-	-	-
(3) Others	-	-	-
Subtotal	8,060	9,380	1,320
Securities whose carrying value does not exceed their acquisition cost			
(1) Equity securities	-	-	-
(2) Debt securities			
a. JGBs and municipal bonds	-	-	-
b. Corporate bonds	214,048	203,940	(10,107)
c. Others	-	-	-
(3) Others	-	-	-
Subtotal	214,048	203,940	(10,107)
Total	222,108	213,320	(8,787)

2. Securities sold during the current fiscal year

Yen in thousands

Total amount sold	Gains on sales	Losses on sales
105,980	3,980	-

3. Securities without market quotations

Yen in thousands

	Carrying value
(1) Other securities	
Money management funds	880,747
Free financial funds	205,585
Investment partnership funds	100,000
Unlisted stock	11,354
Total	1,197,687

Derivatives

FY2003 (From April 1, 2003 to March 31, 2004), FY2004 (From April 1, 2004 to March 31, 2005)

No reportable information. The Group did not have any outstanding derivative positions.

Retirement benefit

1. Description of retirement benefit plans

(1) Retirement benefit plans of the Company and its consolidated subsidiaries

The Company and its consolidated subsidiaries offer defined benefit plans, i. e., a tax-qualified pension plan, and a certain mutual aid retirement benefit plan, i. e., a defined contribution pension plan, covering substantially all employees. Other affiliates do not offer retirement benefit plans.

(2) Supplementary information

A. Mutual aid retirement benefit plan: Established 1979

The Company participates in the Mutual Aid Retirement Benefit Plan established by the Yokohama Chamber of Commerce to offer retirement benefits to employees retiring voluntarily.

Pension fund assets: ¥119,983 thousands

B. Tax-qualified pension plan: Established: 1985

To provide for retirement benefits, in addition to the above, to employees with three or more years of service, the Company offers the tax-qualified pension plan.

2. Principal components of retirement benefit obligations

Yen in thousands

	FY2003 As of March 31, 2004	FY2004 As of March 31, 2005
(1) Retirement benefit obligation	(29,049)	(31,661)
(2) Plan assets at fair value	29,158	31,177
(3) Reserve for employees' retirement benefits	-	(484)
(4) Prepaid pension costs	109	-

Note: Retirement benefit obligations are calculated using the Simple method.

3. Principal components of retirement benefit expenses

Yen in thousands

	FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
(1) Service cost	1,899	2,508
(2) Contribution to mutual aid pension plan	11,825	11,534
Total	13,724	14,042

Note: Service cost is computed using the Simple method.

4. Matters concerning the accounting standards for retirement benefit obligations

FY2003 From April 1, 2003 to March 31, 2004	FY2004 From April 1, 2004 to March 31, 2005
In the calculation of retirement benefit liabilities, in recent years, the Company has been using the fair value of pension assets as of the end of the term to estimate pension assets.	Same as on the left.

Deferred tax accounting

Yen in thousand

FY2003 From April 1, 2003 to March 31, 2004		FY2004 From April 1, 2004 to March 31, 2005			
1. The significant components of deferred tax assets and liabilities		1. The significant components of deferred tax assets and liabilities			
Deferred tax assets		Deferred tax assets			
Reserve for directors' retirement benefits	65,568	Provision of doubtful accounts in excess of maximum	96,823		
Provision of depreciation and amortization in excess of maximum	10,222	Reserve for employees' retirement benefits	196		
Inventories	16,015	Reserve for directors' retirement benefits	69,519		
Investment securities	4,358	Provision of depreciation and amortization in excess of maximum	6,776		
Golf club membership	8,546	Inventories	11,692		
Reserve for accrued bonuses	17,978	Investment securities	4,358		
Deficit carried forward	289,931	Golf club membership	8,911		
Others	4,031	Reserve for accrued bonuses	12,903		
Subtotal deferred tax assets	416,653	Deficit carried forward	283,561		
Valuation allowance	(42,258)	Others	5,785		
Total deferred tax assets	374,395	Subtotal deferred tax assets	500,529		
		Valuation allowance	(470,147)		
		Total deferred tax assets	30,381		
Deferred tax liabilities		Deferred tax liabilities			
Special depreciation reserve	(2,021)	Others	(163)		
Program reserve	(22,573)	Total deferred tax liabilities	(163)		
Other unrealized losses on other securities	(2,963)	Net deferred tax assets (liabilities)	30,218		
Others	(230)				
Total deferred tax liabilities	(27,789)				
Net deferred tax assets (liabilities)	346,605				
Net deferred tax assets (liabilities) are included in the following consolidated balance sheet accounts		Net deferred tax assets (liabilities) are included in the following consolidated balance sheet accounts			
Current assets	Deferred tax assets	51,832	Current assets	Deferred tax assets	29,535
Fixed assets	Deferred tax assets	294,773	Fixed assets	Deferred tax assets	756
Current assets	Deferred tax liabilities	-	Current assets	Deferred tax liabilities	73
Long-term liabilities	Deferred tax liabilities	-	Long-term liabilities	Deferred tax liabilities	-
2. Significant sources of the difference in corporate and other tax liabilities as calculated according to the effective tax rate and tax-effect accounting		2. Significant sources of the difference in corporate and other tax liabilities as calculated according to the effective tax rate and tax-effect accounting			
Statutory tax rate	42.0%	Significant sources of difference are not presented since the Company reported net loss before income taxes in the consolidated fiscal year under review. The statutory tax rates, as of the end of the current fiscal year is 40.6%.			
Adjustments					
Entertainment and other expenses in excess of tax allowable maximum	1.5%				
Dividends receivable and other items not to be included in income indefinitely.	(0.8) %				
Per capita Inhabitant Tax	3.3%				
Valuation reserve	31.9%				
Differences in tax rates	6.2%				
Equity in earnings/loss of non-consolidated subsidiaries	(2.0) %				
Gain on sale of subsidiary stock	(59.7) %				
Other	(0.1) %				
Effective tax rate	22.3%				

Segment Information

1. Segment information by operating segment

FY2003 (April 1, 2003 - March 31, 2004), FY2004 (April 1, 2004 – March 31, 2005)

No reportable items. The Company and its major consolidated subsidiaries 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

FY2003 (April 1, 2003 - March 31, 2004)

Yen in thousands

	Japan	N. America	Europe	Total	Elimination or Corporate	Consolidated
I. Net sales and operating income/ loss						
Net sales						
(1) Sales to external customers	1,571,284	141,715	20,404	1,733,403	-	1,733,403
(2) Inter-segment sales and transfers	-	111,537	-	111,537	[111,537]	-
Total	1,571,284	253,252	20,404	1,844,940	[111,537]	1,733,403
Operating expenses	1,477,167	352,354	52,331	1,881,853	[70,639]	1,811,213
Operating income (loss)	94,117	(99,101)	(31,927)	(36,912)	[40,897]	(77,809)
II. Assets	-	-	-	-	-	-

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. Amount of unallocatable operating expenses included in eliminations or corporate is ¥42,564 thousand, and its significant components are representing expenses related to the administration division

4. Asset allocation is not presented since the Company does not have consolidated subsidiaries or major branch offices in regions and countries other than Japan after the exclusion of the overseas subsidiary at the end of the current consolidated fiscal year.

FY2004 (April 1, 2004 - March 31, 2005)

Geographical segment information is not presented since the Company had no consolidated subsidiary or significant branch offices in countries and regions other than Japan in the current period.

3. Overseas sales

FY2003 (April 1, 2003 - March 31, 2004)

Yen in thousands

	North America	Other	Total
I. Overseas sales	95,023	86,747	181,770
II. Consolidated net sales	-	-	1,733,403
III. Weight of overseas sales in total consolidated net sales	5.48	5.01	10.49

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:

(1) North America: U.S.A., Canada (2) 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.

FY2004 (April 1, 2004 - March 31, 2005)

Overseas sales information is not provided since overseas sales represented less than 10% of total consolidated sales.

Related Party Transactions

FY2003 (April 1, 2003 - March 31, 2004)

Directors, principal individual shareholder and others

Yen in thousands

Type	Company etc. name	Address	Capital or investment	Activities or occupation	Voting rights (held)	Business relationship Joint director Transactions	Transaction description	Transaction amount	Item	Account balance
Directors and relatives	Seiichi Nobehara	/	/	Company director CEO IBT Co., Ltd.	(Owned) Direct 0.1	/	Consultation and language services related to domestic business and overseas expansion Notes2	3,600	Accounts payable -other	315

- Notes:
1. Transaction amounts are exclusive of consumption taxes. Fiscal year-end account balances are inclusive of consumption taxes.
 2. Transactions are arms length.

FY2004 (April 1, 2004 - March 31, 2005)

Directors, principal individual shareholder and others

Yen in thousands

Type	Company etc. name	Address	Capital or investment	Activities or occupation	Voting rights (held)	Business relationship Joint director Transactions	Transaction description	Transaction amount	Item	Account balance
Directors and relatives	Seiichi Nobehara	/	/	Company director CEO IBT Co., Ltd.	(Owned) Direct 0.1	/	Consultation and language services related to domestic business and overseas expansion Notes2	3,600	Accounts payable -other	315

- Notes:
1. Transaction amounts are exclusive of consumption taxes. Fiscal year-end account balances are inclusive of consumption taxes.
 2. Transactions are arms length.

Amounts Per Share

Yen

	FY2003 Apr. 1, 2003 - Dec. 31, 2004	FY2004 Apr. 1, 2004 - Mar. 31, 2005
Net assets per share	567.02	443.19
Net income (loss) per share (basic)	29.51	(122.55)
Net income per share (diluted)	Net income per share (diluted) is not presented since the Company has no outstanding dilutive securities.	Net income per share (diluted) is not presented since the Company has outstanding dilutive securities, though posted net loss for the current fiscal year.

Note: The basis of calculation of net income/net loss per share (basic) for the period is as follows:

Yen in thousand

	FY2003 Apr. 1, 2003 - Mar. 31, 2004	FY2004 Apr. 1, 2003 - Mar. 31, 2005
Net loss for the period	142,148	(590,166)
Equity in net loss not account of common shareholders	-	-
Common stock in net loss	142,148	(590,166)
Average number of shares outstanding for the period	4,816,000 shares	4,815,000 shares
Details on potential stock not included in the calculation of net income per share (diluted) 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 (Number of shares to be issued upon execution of share acquisition rights: 160,000 shares)	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. Exercise period: by March 31, 2005

Subsequent events

Not applicable.

6. Production, Orders Received and Net sales

(1) Production

Yen in thousands

Product category	FY 2003		FY 2004		YoY change (%)
	From April 1, 2003 to March 31, 2004		From April 1, 2004 to March 31, 2005		
Manufactured products					
Communications		667,510		193,684	29.0
Internet protocol		461,916		185,327	40.1
Real-time OS		60,748		39,962	65.8
SI (customization)		641,281		457,718	71.4
Total		1,831,456		876,692	47.9

- Notes: 1. Amounts are calculated based on sales prices.
2. The above amounts do not include consumption taxes.

(2) Procurement

Yen in thousands

Product category	FY 2003		FY 2004		YoY change (%)
	From April 1, 2003 to March 31, 2004		From April 1, 2004 to March 31, 2005		
Others		152,935		111,114	72.7
Total		152,935		111,114	72.7

- Notes: 1. Amounts are calculated based on sales prices.
2. The above amounts do not include consumption taxes.

(3) Orders received

Yen in thousands

Product category	FY 2003		FY 2004		
	From April 1, 2003 to March 31, 2004		From April 1, 2004 to March 31, 2005		YoY change (%)
	Orders received	Order backlog	Orders received	Order backlog	
Manufactured products					
Communications	386,988	119,231	350,465	78,078	65.5
Internet protocol	512,092	78,615	202,593	80,406	102.3
Real-time OS	75,450	38,590	43,345	7,200	18.7
SI (customization)	411,287	9,110	491,645	100,999	1,108.7
Subtotal	1,385,819	245,546	1,088,050	266,684	108.6
Purchased products					
Others	151,201	11,969	154,618	17,572	130.1
Total	1,537,020	257,515	1,242,668	284,256	110.4

- Notes: 1. Amounts are calculated based on sales prices.
2. The above amounts do not include consumption taxes.

(4) Net sales

Yen in thousands

Product category	FY 2003		FY 2004		YoY change (%)
	From April 1, 2003 to March 31, 2004		From April 1, 2004 to March 31, 2005		
Manufactured products					
Communications		353,638		376,375	6.4
Internet protocol		503,213		223,961	(55.5)
Real-time OS		79,154		50,545	(36.1)
SI (customization)		618,313		454,981	(26.4)
Subtotal		1,554,320		1,105,865	(28.9)
Purchased products					
Others		179,083		148,636	(17.0)
Total		1,733,403		1,254,501	(27.6)

- Notes: 1. Amounts are calculated based on sales prices.
2. Sales by major customer are not presented since no single customer represented more than 10% of aggregate net sales in the current consolidated interim period.
3. The above amounts do not include consumption taxes.

* 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.