

# Sankyo

## 2002 ANNUAL REPORT

Year ended March 31, 2002

## MANAGEMENT POLICY & BUSINESS PERFORMANCE

### Management Policy

#### (1) Basic Management Policy

Sankyo Seiki Manufacturing Co., Ltd. aims to maintain high profitability and become a company that can achieve continual development by enhancing its competitiveness through the accumulation and development of core technologies, guided by its "Customer First" motto, and also by positioning itself as a technology-oriented company. We intend to further develop our business activities so that the Company's stock will attract an increasing number of investors.

The electronic equipment market, in which we are deeply involved, is expected to expand in all sectors over the mid to long term, owing to progress in digitization and networking, and fueled by the development of the advanced information society. To meet these challenges, we will move beyond conventional management structures to improve market efficiencies, build a value-added corporate structure, and strengthen management resources. In addition, we will efficiently use the management resources of each Group company to promote the globalization of the Group, and to maximize its value.

#### (2) Basic Profit-Sharing Policy

Based on the "six S's" (Global Satisfaction, World Satisfaction, Social Satisfaction, Management Satisfaction, Customer Satisfaction and Employee Satisfaction), we will build good relationships with our stakeholders and expand our business, while contributing to the emergence of a better society.

Dividend payments are a central element of Management Satisfaction. Though stable dividends are important to our shareholders, it is our responsibility to declare dividends in proportion to the Company's business performance. Profit-sharing with shareholders, therefore, is based on comprehensive consideration of the Company's long-term welfare.

Some retained earnings are utilized for R&D expenses and capital expenditures, to ensure future growth.

#### (3) Mid-Term Management Strategy

Significant changes are expected in the Company's business environment, as a result of intensifying price competition and falling prices in the market as a whole, the latter due to the oversupply that has resulted from sluggish demand for IT related equipment, that began in the second half of calendar 2000. In addition, components are becoming increasingly standardized as technical innovation drives the switch to digital products, and EMS, large-scale business alliances, M&A, and the growing power of Asian companies are accelerating the global reorganization of customers and competitors.

Facing these circumstances, the Company introduced hard disk drives (HDDs) incorporating its proprietary fluid-dynamic-bearing (FDB) motors. High growth in sales of these devices, which offer technical superiority based on precision manufacturing, is expected in the field of IT-related equipment and computerized home appliances. Dramatic reductions in total production costs through the use of our proprietary Desk Top Factory (DTF) system will make this a highly profitable core business.

We will expand our share of the micromotor market, and will employ our technical superiority in the manufacture of bearings to do the same in the optical disk drive (ODD) market, where sales are expected to show high growth for use in personal computers and peripheral equipment. At the same time, we will further strengthen the stability of our motor business by actively participating in the non-storage market.

In the market for optical pickup units, we will emphasize not only CD-R and CD-RW products, in which we lead the competition in terms of development, but also components for DVD players, which are expected to show stable growth. We will also strive to increase profitability by reducing costs through the acceleration of product development and overseas procurement of parts. In addition, we will endeavor to gain a foothold in the optical device field, in which dramatic growth is expected, through the in-house manufacture of optical parts.

We will transfer manufacturing operations in these three businesses

to optimal locations abroad, and implement a nimble management style that will allow us to respond to every requirement and change in the environment, and to respond to structural changes at customer firms and competitors in a timely fashion.

In another measure to increase profits, we will reinforce our sales promotions in Europe, the U.S.A. and Asia of card-reader products, which hold a high share of the market for ATM equipment in Japan. At the same time, we will continue technological and product development, including the development of new applications for our products.

The Company will work to further expand its share of the market for FA products, primarily industrial robots, taking the opportunity represented by the current growth in capital investment in the liquid crystal display field. At the same time, we will endeavor to develop environmentally friendly technologies to meet the increasing demand in that area.

We will reform the profit structure of our core businesses in Japan by positioning development and marketing as key sources of added value.

To foster next-generation domestic businesses, we will establish a system to encourage the entrepreneurial spirit of our Japanese employees, thereby promoting the development and commercialization of high-value-added domestic products, such as high-end audio products, medical equipment, and security systems.

We consider that the most important factors in surviving in the age of mega-competition are management that can foresee changes, and human resources with originality and a mind for management. To achieve these, we will further reinforce and refine the "IT management" policies that we have been promoting.

Utilizing the synergies of our policy management system, which is based on the reinforcement of management, we will further expand our performance-based promotion system, and will foster human resources across the globe by strengthening the corporate system to encourage the entrepreneur spirit.

#### (4) Issues to Be Resolved

The most important issue in the reform of the Company's profit structure is the early establishment of a market presence and profitability in the FDB motor business, which has been positioned as the Company's new core business. We will concentrate Companywide resources on strategic sales promotion activities in this field.

Next in importance is the qualitative reform of our managerial resources to cope with the new, highly competitive environment. To this end, we will move steadily forward with such ongoing structural changes as the relocation of overseas operations (especially in ASEAN countries and China), the qualitative enhancement of human resources in Japan, and the concentration of our efforts on businesses that promise future growth.

Environmental protection countermeasures are also an important issue in our international operations, and we will therefore be working with our overseas subsidiaries to find solutions in this area.

#### (5) Promoting Corporate Governance

The Company introduced an executive director system in April 2000, and has shifted from a functional headquarters organization to a business unit organization, in the process reinforcing its ability to respond to market changes.

We are making efforts to activate the Board of Directors and optimize and accelerate management decision making in order to strengthen corporate governance. To this end, we are taking measures to reinforce the monitoring of corporate accountability by the newly established Internal Audit Office and to monitor the business process through the streamlined headquarters functions, including the virtual renovation of management meetings.

### Business Performance

#### (1) Outline of the Fiscal Year under Review

During the fiscal year ended March 31, 2002, the Japanese economy

experienced the most severe conditions in recent years due not only to prolonged stagnation of personal consumption and a decline in private capital investment, but also to the business slump of IT-related companies, which had been working as the traction power of economy. Furthermore, economic uncertainty remained as domestic unemployment increased to the highest level in many years.

There were also growing concerns for a deceleration of the world economy due to the slowdown of the U.S. economy and the impact of the September 11 terrorist attacks last year. Although an upward trend was evident in the second half of the fiscal year under review, the world economy remained at a low level overall.

Sankyo operates primarily in the field of electronic equipment, with three business segments that comprise Audiovisual and Home Appliance Equipment, Communications and Peripheral Computer Equipment, and Industrial Machinery and Equipment. During the fiscal year under review, on a consolidated basis, amusement products recorded favorable sales, but it was not enough to offset the decline in electronic equipment as a whole, and parts for information peripheral equipment recorded a large decrease in sales, affected by a slump in the personal computer market resulting from the worldwide IT depression. Also, parts for industrial machinery recorded a sales drop due to the decrease of private capital investment. As a result of the above, Sankyo recorded consolidated net sales of ¥109,546 million, a decrease of 19.1% compared with the previous fiscal year.

Loss before income taxes and minority interests was ¥6,910 million, compared with income before income taxes and minority interests of ¥2,627 million in the previous fiscal year. Factors contributing to this loss included strategic investment in FDB motors—Sankyo's next-generation strategic products—in addition to a decrease in sales of our existing products due to sluggish demand for IT-related products and the restraint of private capital investment, despite rationalization efforts and the reduction of fixed costs.

Other expenses were ¥1,900 million, compared with other income of ¥363 million in the previous fiscal year, due to various measures taken by management for the drastic reform of Sankyo's profit structure in response to rapid market changes that exceeded initial projections. Accordingly, a net loss was recorded of ¥7,778 million, compared with net income of ¥1,694 million during the same period last year.

## (2) Results by Segment

### Audiovisual and Home Appliance Equipment

The market scale of video motors contracted as a result of the growth in demand for DVD players, and sales of audiovisual equipment motors and tape-deck mechanisms declined due to a trend toward lower prices and shrinking consumer interest in cassette-tape media.

Sales of switches and motor-driven actuator units for white goods were virtually unchanged from the previous fiscal year as a result of increased demand in the first half of the term under review, owing to enforcement of the Electric Home Appliance Recycling Act. Sales of stepping motors for digital still cameras leveled off, while a large increase in sales of amusement equipment was recorded.

Magnetic head sales dropped sharply, as we transferred our Audio Head Division was transferred to Techreco Co., Ltd. in May 2001.

As a result of the above, total sales of this segment decreased 8.6% to ¥46,350 million, compared with the previous fiscal year.

### Communications and Peripheral Computer Equipment

Sales of HDD motors decreased in line with termination in production of ball-bearing-type products in the first half of the term under review. Instead, at Sankyo's factory in the Philippines, mass-production was commenced of FDB motors, which the Company is positioning as its future core product. Also, we reached an agreement with the Motor Company of Matsushita Electric Industrial Co., Ltd. for production cooperation of FDB motors for HDDs, which stemmed from an overlapping product strategy in this field between Sankyo and Matsushita.

However, despite Sankyo's efforts to increase its share of FDD motors, sales declined because of a slump in market demand.

Conversely, motors for ODDs helped to expand the Company's market share and bolster sales through the introduction of new models.

A sharp decrease in optical pick-up units was recorded, impacted by the slump in the PC market and price decreases.

For office equipment units, sales of molded parts increased thanks to continued growth of the printer market.

As a result of the above, total sales of this segment dropped 29.2% to ¥41,641 million, compared with the previous fiscal year.

### Industrial Machinery and Equipment

Sales of magnetic card readers to domestic financial institutions leveled off, but were offset by sales to convenience stores and exports to Europe and America. However, segment sales decreased overall, owing to a sharp decline in applications for amusement equipment.

Demand decreased for industrial machinery mainly for that related to liquid-crystal-related devices and semiconductors, due to restraint in private capital investment resulting from the weakened economy.

Accordingly, total sales of this segment fell 16.9% to ¥16,187 million, compared with the same period last year.

### Others

Sales contracted of musical movements and parts due to the change from sales of movements to sales of parts, based on a license agreement with a foreign manufacturer and a decline in demand in the toy and gift market. However, sales of services for distribution, insurance and real estate remained level with those in the previous fiscal year.

Total sales of the segment dropped 16.4% to ¥5,368 million, compared with the same period last year.

## (3) Cash Flows

Net cash provided by operating activities amounted to ¥2,077 million, mainly owing to depreciation and amortization of ¥6,108 million and decrease in trade receivables of ¥7,671 million. Major uses of cash were loss before income taxes and minority interests of ¥6,910 million and decrease in trade payables of ¥6,645 million.

Net cash used in investing activities was ¥7,603 million, mainly due to purchases of property, plant and equipment of ¥5,422 million, and purchases of unconsolidated subsidiaries and associated companies of ¥2,354 million.

Net cash provided by financing activities was ¥1,698 million. Main sources of cash were proceeds from long-term debt of ¥3,650 million and proceeds from issuance of commercial paper of ¥1,500 million. The largest uses of cash were repayments of long-term debt of ¥3,330 million.

As a result of the above, cash and cash equivalents, end of year, were ¥19,920 million, a decrease of ¥3,393 million compared with the previous fiscal year.

## (4) Outlook

Although such positive factors as a bottoming of the U.S. economy, and further monetary measures taken by the Japanese government and the Bank of Japan are anticipated, severe conditions are still expected for the Japanese economy because an upturn is not expected in exports, employment and capital investment.

Regarding the world economy, despite expectations for a recovery of the U.S. economy, a sense of stagnation remains. Also, a rapid recovery is not anticipated in the European and Asian economies, and uncertainty persists in the management environments of many firms in these countries.

Amid this environment, Sankyo will strive to expand its share of the growing electronic equipment market by producing competitive products based on its accumulated know-how and leading-edge technologies. At the same time, we will work to increase profits through the sales of our future core FDB motor products, as well as through the continued development of domestic products with high added value.

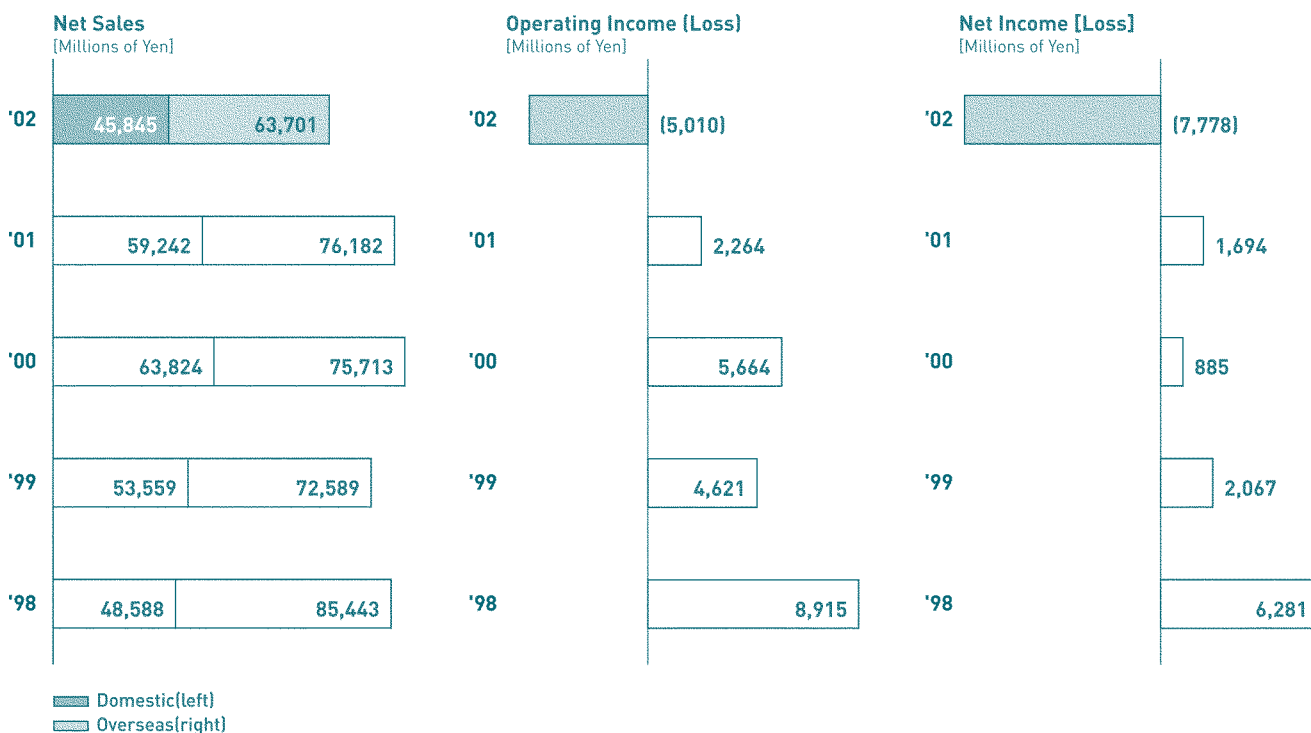
## FIVE-YEAR SUMMARY

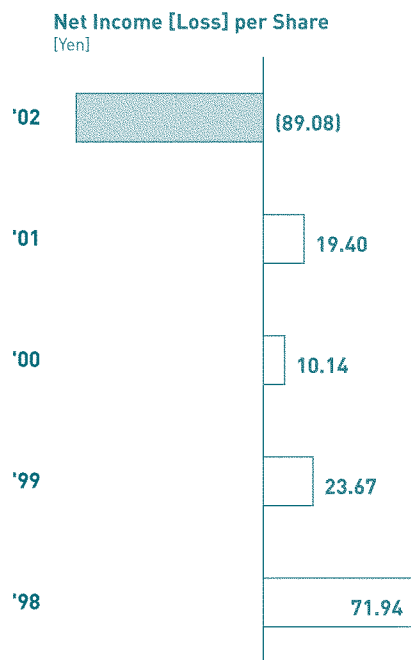
Sankyo Seiki Mfg. Co., Ltd. and Consolidated Subsidiaries

Years Ended March 31	Millions of Yen					Thousands of U.S. Dollars
	2002	2001	2000	1999	1998	2002
Net sales	<b>¥109,546</b>	¥135,424	¥139,537	¥126,148	¥134,031	<b>\$822,112</b>
Net income (loss)	<b>(7,778)</b>	1,694	885	2,067	6,281	<b>(58,370)</b>
	Yen					U.S. Dollars
Per share:						
Net income (loss)	<b>¥(89.08)</b>	¥19.40	¥10.14	¥23.67	¥71.94	<b>\$(0.67)</b>
Cash dividends		4.00	4.00	2.50	2.50	
	Millions of Yen					Thousands of U.S. Dollars
Total shareholders' equity	<b>¥ 38,592</b>	¥ 46,559	¥ 45,701	¥ 43,805	¥ 42,068	<b>\$289,623</b>
Total assets	<b>111,980</b>	123,105	122,096	107,674	114,899	<b>840,377</b>
Working capital	<b>16,541</b>	23,189	17,901	20,535	18,325	<b>124,135</b>
Long-term debt, less current portion	<b>15,143</b>	14,680	6,610	6,730	7,947	<b>113,645</b>
Capital expenditures	<b>6,125</b>	8,389	6,842	5,590	4,931	<b>45,964</b>
Depreciation and amortization	<b>6,108</b>	6,073	6,252	5,610	6,109	<b>45,839</b>

Note: U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥133=US\$1.00.

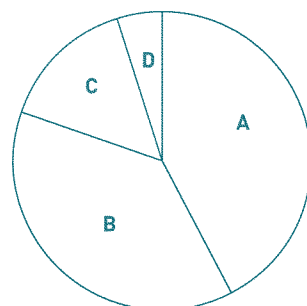
## MAJOR FINANCIAL INDICES





### Sales by Business Segment in 2002

[%]

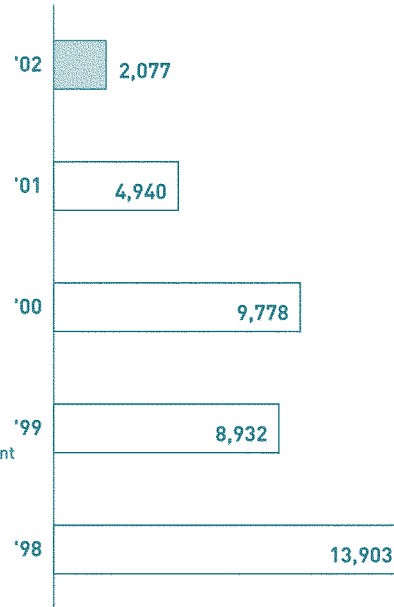


- A 42.3% Audiovisual and Home Appliance Equipment
- B 38.0% Communications and Peripheral Computer Equipment
- C 14.8% Industrial Machinery and Equipment
- D 4.9% Others [Music Boxes, etc.]

Net Sales: ¥109,546 million

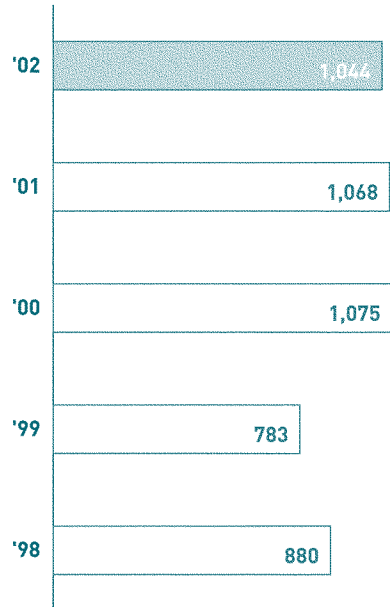
### Net Cash Provided by Operating Activities

[Millions of Yen]



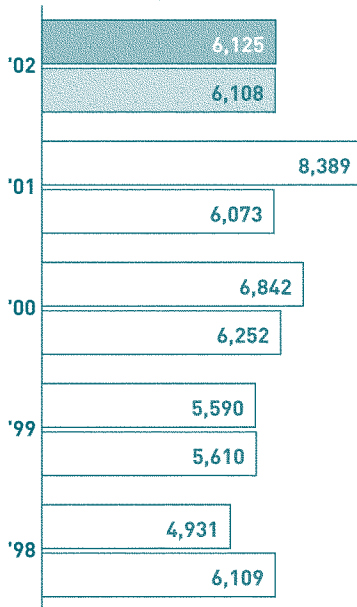
### R&D Expenses

[Millions of Yen]



### Capital Expenditures/ Depreciation & Amortization

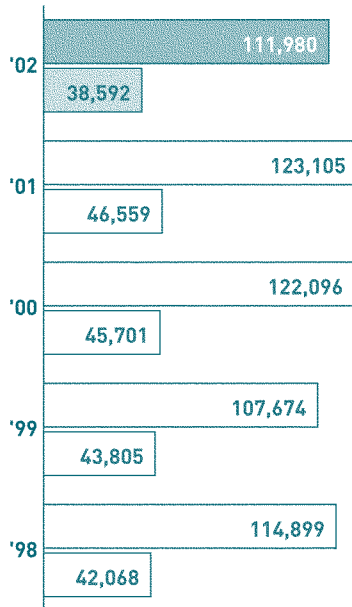
[Millions of Yen]



- Capital Expenditures
- Depreciation & Amortization

### Total Assets/Total Shareholders' Equity

[Millions of Yen]



- Total Assets
- Total Shareholders' Equity

## CONSOLIDATED BALANCE SHEETS

Sankyo Seiki Mfg. Co., Ltd. and Consolidated Subsidiaries

March 31, 2002 and 2001	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2002	2001	2002
<b>ASSETS</b>			
CURRENT ASSETS:			
Cash and cash equivalents	¥ 19,920	¥ 23,313	\$ 149,492
Short-term investments (Note 3)	2,447	1,038	18,363
Notes and accounts receivable:			
Trade notes	3,691	4,507	27,698
Trade accounts	24,233	30,556	181,865
Unconsolidated subsidiaries and associated companies	304	253	2,285
Other (Note 9)	1,777	1,932	13,334
Allowance for doubtful receivables	(69)	(280)	(515)
Inventories (Note 4)	12,857	14,353	96,487
Deferred tax assets (Note 8)	117	533	874
Prepaid expenses and other current assets	351	635	2,633
Total current assets	<u>65,628</u>	<u>76,840</u>	<u>492,516</u>
PROPERTY, PLANT AND EQUIPMENT (Note 5):			
Land	6,714	6,714	50,383
Buildings and structures	23,911	23,499	179,445
Machinery and equipment	63,308	63,740	475,109
Construction in progress	908	705	6,818
Total	<u>94,841</u>	<u>94,658</u>	<u>711,755</u>
Accumulated depreciation	<u>(62,940)</u>	<u>(61,654)</u>	<u>(472,345)</u>
Net property, plant and equipment	<u>31,901</u>	<u>33,004</u>	<u>239,410</u>
INVESTMENTS AND OTHER ASSETS:			
Investment securities (Notes 3 and 5)	5,705	6,733	42,816
Investments in unconsolidated subsidiaries and associated companies	6,255	3,714	46,943
Deferred tax assets (Note 8)	1,017	1,058	7,634
Other assets (Note 9)	1,474	1,756	11,058
Total investments and other assets	<u>14,451</u>	<u>13,261</u>	<u>108,451</u>
<b>TOTAL</b>	<u><b>¥111,980</b></u>	<u><b>¥123,105</b></u>	<u><b>\$ 840,377</b></u>

See notes to consolidated financial statements.

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2002	2001	2002
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
CURRENT LIABILITIES:			
Short-term borrowings (Note 5)	¥ 19,281	¥ 16,336	\$144,694
Current portion of long-term debt (Note 5)	2,441	3,045	18,319
Notes and accounts payable:			
Trade notes	4,803	7,703	36,042
Trade accounts	12,941	16,106	97,118
Unconsolidated subsidiaries and associated companies	229	43	1,716
Other	4,541	5,097	34,078
Income taxes payable (Note 8)	313	881	2,352
Accrued expenses	3,794	3,417	28,475
Deferred tax liabilities (Note 8)	74	76	558
Other current liabilities	670	947	5,030
Total current liabilities	<u>49,087</u>	<u>53,651</u>	<u>368,382</u>
LONG-TERM LIABILITIES:			
Long-term debt, less current portion (Note 5)	15,143	14,680	113,645
Liability for retirement benefits (Note 6)	7,596	6,397	57,005
Deferred tax liabilities (Note 8)	173	251	1,297
Other	55	67	411
Total long-term liabilities	<u>22,967</u>	<u>21,395</u>	<u>172,358</u>
MINORITY INTERESTS	<u>1,334</u>	<u>1,500</u>	<u>10,014</u>
COMMITMENTS AND CONTINGENT LIABILITIES (Notes 11 and 13)			
SHAREHOLDERS' EQUITY (Note 7):			
Common stock—authorized, 200,000,000 shares; issued and outstanding, 87,311,591 shares in 2002 and 2001	16,575	16,575	124,391
Additional paid-in capital	18,602	18,602	139,599
Retained earnings	3,694	11,821	27,720
Unrealized gain on available-for-sale securities	824	1,178	6,188
Foreign currency translation adjustments	(1,100)	(1,616)	(8,251)
Total	<u>38,595</u>	<u>46,560</u>	<u>289,647</u>
Treasury stock—at cost, 8,211 shares in 2002 and 889 shares in 2001	(3)	(1)	(24)
Total shareholders' equity	<u>38,592</u>	<u>46,559</u>	<u>289,623</u>
<b>TOTAL</b>	<u>¥111,980</u>	<u>¥123,105</u>	<u>\$840,377</u>

## CONSOLIDATED STATEMENTS OF OPERATIONS

Sankyo Seiki Mfg. Co., Ltd. and Consolidated Subsidiaries

Years Ended March 31, 2002 and 2001	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2002	2001	2002
NET SALES	<b>¥109,546</b>	¥135,424	<b>\$822,112</b>
COST OF SALES	<b>101,813</b>	118,268	<b>764,073</b>
Gross profit	<b>7,733</b>	17,156	<b>58,039</b>
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (Note 10)	<b>12,743</b>	14,892	<b>95,635</b>
Operating income (loss)	<b>(5,010)</b>	2,264	<b>(37,596)</b>
OTHER INCOME (EXPENSES):			
Interest expense	<b>(678)</b>	(1,264)	<b>(5,090)</b>
Interest and dividend income	<b>364</b>	745	<b>2,735</b>
Foreign exchange gain	<b>272</b>	715	<b>2,040</b>
Gain (loss) on sales of marketable and investment securities	<b>(3)</b>	809	<b>(26)</b>
Loss on devaluation of marketable and investment securities	<b>(478)</b>		<b>(3,589)</b>
Loss on sales of investment in associated company	<b>(48)</b>		<b>(363)</b>
Additional retirement benefits paid to employees	<b>(854)</b>	(203)	<b>(6,407)</b>
Loss on sales of property, plant and equipment	<b>(597)</b>	(91)	<b>(4,483)</b>
Loss on disposals of property, plant and equipment	<b>(387)</b>	(447)	<b>(2,905)</b>
Equity in earnings of unconsolidated subsidiaries and associated companies	<b>113</b>	115	<b>850</b>
Other—net	<b>396</b>	(16)	<b>2,975</b>
Other income (expenses)—net	<b>(1,900)</b>	363	<b>(14,263)</b>
INCOME (LOSS) BEFORE INCOME TAXES AND MINORITY INTERESTS	<b>(6,910)</b>	2,627	<b>(51,859)</b>
INCOME TAXES (Note 8):			
Current	<b>303</b>	1,216	<b>2,274</b>
Deferred	<b>643</b>	(422)	<b>4,822</b>
Total	<b>946</b>	794	<b>7,096</b>
MINORITY INTERESTS IN NET INCOME	<b>78</b>	(139)	<b>585</b>
NET INCOME (LOSS)	<b>¥ (7,778)</b>	¥ 1,694	<b>\$ (58,370)</b>
		Yen	U.S. Dollars
	<b>2002</b>	2001	<b>2002</b>
PER SHARE OF COMMON STOCK (Note 2.n):			
Net income (loss)	<b>¥ (89.08)</b>	¥ 19.40	<b>\$ (0.67)</b>
Diluted net income		18.45	
Cash dividends applicable to the year		4.00	

See notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Sankyo Seiki Mfg. Co., Ltd. and Consolidated Subsidiaries

Years Ended March 31, 2002 and 2001	Thousands		Millions of Yen				
	Outstanding Number of Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Unrealized Gain on Available-for-Sale Securities	Foreign Currency Translation Adjustments	Treasury Stock
BALANCE, APRIL 1, 2000	87,312	¥16,575	¥18,602	¥10,526			¥(2)
Net income				1,694			
Cash dividends, ¥4.00 per share				(349)			
Decrease resulting from changes in the scope of consolidation or adoption of the equity method				(50)			
Unrealized gain on available-for-sale securities—net					¥1,178		
Foreign currency translation adjustments						¥(1,616)	
Sale of treasury stock							1
BALANCE, MARCH 31, 2001	87,312	16,575	18,602	11,821	1,178	(1,616)	(1)
Net loss				(7,778)			
Cash dividends, ¥4.00 per share				(349)			
Net decrease in unrealized gain on available-for-sale securities					(354)		
Net increase in foreign currency translation adjustments						516	
Acquisition of treasury stock							(2)
BALANCE, MARCH 31, 2002	<b>87,312</b>	<b>¥16,575</b>	<b>¥18,602</b>	<b>¥ 3,694</b>	<b>¥ 824</b>	<b>¥(1,100)</b>	<b>¥(3)</b>

	Thousands of U.S. Dollars (Note 1)					
	Common Stock	Additional Paid-in Capital	Retained Earnings	Unrealized Gain on Available-for-Sale Securities	Foreign Currency Translation Adjustments	Treasury Stock
BALANCE, MARCH 31, 2001	\$124,391	\$139,599	\$ 88,711	\$ 8,838	\$(12,124)	\$ (4)
Net loss			(58,370)			
Cash dividends, \$0.03 per share			(2,621)			
Net decrease in unrealized gain on available-for-sale securities				(2,650)		
Net increase in foreign currency translation adjustments					3,873	
Acquisition of treasury stock						(20)
BALANCE, MARCH 31, 2002	<b>\$124,391</b>	<b>\$139,599</b>	<b>\$27,720</b>	<b>\$ 6,188</b>	<b>\$ (8,251)</b>	<b>\$ (24)</b>

See notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Sankyo Seiki Mfg. Co., Ltd. and Consolidated Subsidiaries

Years Ended March 31, 2002 and 2001	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2002	2001	2002
<b>OPERATING ACTIVITIES:</b>			
Income (loss) before income taxes and minority interests	<b>¥ (6,910)</b>	¥ 2,627	<b>\$ (51,859)</b>
Adjustments for:			
Income taxes—paid	<b>(874)</b>	(1,238)	<b>(6,564)</b>
Depreciation and amortization	<b>6,108</b>	6,073	<b>45,839</b>
Provision for doubtful receivables	<b>(130)</b>	176	<b>(975)</b>
Provision for retirement benefits—net	<b>1,222</b>	689	<b>9,173</b>
Loss (gain) on sales of marketable and investment securities	<b>3</b>	(809)	<b>26</b>
Loss on sale of associated company	<b>48</b>		<b>363</b>
Loss on sales of property, plant and equipment	<b>597</b>	91	<b>4,483</b>
Loss on disposal of property, plant and equipment	<b>387</b>	447	<b>2,905</b>
Equity in earnings of unconsolidated subsidiaries and associated companies	<b>(113)</b>	(115)	<b>(850)</b>
Loss on devaluation of marketable and investment securities	<b>478</b>		<b>3,589</b>
Changes in assets and liabilities:			
Decrease in trade receivables	<b>7,671</b>	1,658	<b>57,570</b>
Decrease in inventories	<b>1,535</b>	1,207	<b>11,516</b>
Decrease in trade payables	<b>(6,645)</b>	(6,773)	<b>(49,868)</b>
Other—net	<b>(1,300)</b>	907	<b>(9,759)</b>
Total adjustments	<b>8,987</b>	2,313	<b>67,448</b>
Net cash provided by operating activities	<b>2,077</b>	4,940	<b>15,589</b>
<b>INVESTING ACTIVITIES:</b>			
Proceeds from sale of property, plant and equipment	<b>1,118</b>	1,210	<b>8,390</b>
Purchases of property, plant and equipment	<b>(5,422)</b>	(7,591)	<b>(40,693)</b>
Proceeds from sales of marketable and investment securities	<b>161</b>	1,721	<b>1,208</b>
Purchases of marketable and investment securities	<b>(1,348)</b>	(83)	<b>(10,112)</b>
Proceeds from sales of consolidated subsidiaries and associated companies	<b>305</b>	6	<b>2,288</b>
Purchases of consolidated subsidiaries and associated companies	<b>(20)</b>	(102)	<b>(150)</b>
Purchases of unconsolidated subsidiaries and associated companies	<b>(2,354)</b>	(1,820)	<b>(17,667)</b>
Investment in (maturity of) time deposits	<b>(250)</b>	485	<b>(1,876)</b>
Decrease in other assets	<b>207</b>	487	<b>1,553</b>
Net cash used in investing activities	<b>(7,603)</b>	(5,687)	<b>(57,059)</b>
<b>FINANCING ACTIVITIES:</b>			
Increase (decrease) in short-term bank loans—net	<b>788</b>	(4,099)	<b>5,918</b>
Proceeds from long-term debt	<b>3,650</b>	1,815	<b>27,392</b>
Repayments of long-term debt	<b>(3,330)</b>	(4,716)	<b>(24,994)</b>
Proceeds from issuance of commercial paper	<b>1,500</b>		<b>11,257</b>
Repayments of commercial paper		(1,000)	
Proceeds from issuance of convertible bond		9,744	
Redemption of convertible bond	<b>(477)</b>		<b>(3,580)</b>
Cash dividends paid	<b>(349)</b>	(349)	<b>(2,621)</b>
Payment of cash dividends to minority interests	<b>(81)</b>	(46)	<b>(610)</b>
Other—net	<b>(3)</b>	1	<b>(21)</b>
Net cash provided by financing activities	<b>1,698</b>	1,350	<b>12,741</b>
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	<b>502</b>	1,145	<b>3,764</b>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<b>(3,326)</b>	1,748	<b>(24,965)</b>
CASH AND CASH EQUIVALENTS OF DECONSOLIDATED SUBSIDIARIES, BEGINNING OF YEAR	<b>(67)</b>	(530)	<b>(500)</b>
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<b>23,313</b>	22,095	<b>174,957</b>
CASH AND CASH EQUIVALENTS, END OF YEAR	<b>¥19,920</b>	¥23,313	<b>\$149,492</b>
<b>NON-CASH FINANCING ACTIVITIES:</b>			
Assets decreased by deconsolidation of subsidiary	<b>¥ 1,229</b>	¥ 3,012	<b>\$ 9,224</b>
Liabilities decreased by deconsolidation of subsidiary	<b>697</b>	1,115	<b>5,230</b>
<b>ADDITIONAL CASH FLOW INFORMATION:</b>			
Interest paid	<b>684</b>	1,262	<b>5,133</b>
Interest and dividends received	<b>399</b>	794	<b>2,995</b>

See notes to consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Sankyo Seiki Mfg. Co., Ltd. and Consolidated Subsidiaries

Years Ended March 31, 2002 and 2001

### 1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with accounting principles and practices generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Accounting Standards. The consolidated financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan.

The consolidated financial statements are stated in Japanese yen, the reporting currency of the country in which Sankyo Seiki Mfg. Co., Ltd. (the "Company") is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥133 to \$1, the approximate rate of exchange at March 31, 2002. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

### 2. Summary of Significant Accounting Policies

#### **a. Consolidation**

The accompanying consolidated financial statements include the accounts of the Company and its 25 (26 in 2001) significant subsidiaries (together, the "Group").

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

Investments in certain unconsolidated subsidiaries and associated companies are accounted for by the equity method. The number of the companies which are accounted for by the equity method is 3 (3 in 2001).

Investments in the remaining unconsolidated subsidiaries and associated companies are stated at cost. Effects of not adopting the equity method for the foregoing companies are immaterial.

The excess of the cost of the Company's investments in consolidated subsidiaries and associated companies accounted for by the equity method, over its equity in the net assets at the respective dates of acquisition, is charged to income as incurred.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

#### **b. Cash Equivalents**

Cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value. Cash equivalents include time deposits, certificate of deposits, commercial paper and mutual funds investing in bonds that represent short-term investments, all of which mature or become due within three months of the date of acquisition.

#### **c. Marketable and Investment Securities**

Marketable and investment securities are classified and accounted for, depending on management's intent, as follows: (1) held-to-maturity debt securities, which are expected to be held to maturity with the positive intent and ability to hold to maturity are reported at amortized cost and (2) available-for-sale securities, which are not classified as the aforementioned securities, are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of shareholders' equity. The cost of securities sold is determined based on the moving-average method.

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

#### **d. Inventories**

Inventories held by the Company and domestic consolidated subsidiaries are valued at cost and those held by foreign consolidated subsidiaries are valued at the lower of cost or market, all cost of inventories is determined by the first-in, first-out method.

#### **e. Property, Plant and Equipment**

Property, plant and equipment are stated at cost. Significant renewals and additions are capitalized; maintenance and repairs, and minor renewals and improvements, are charged to income as incurred. Interest costs relating to construction of property, plant and equipment are not capitalized.

Depreciation of property, plant and equipment of the Company and its consolidated domestic subsidiaries is computed by the declining-balance method while the straight-line method is applied to buildings acquired by the Company and its domestic consolidated subsidiaries on or after April 1, 1998. Those of foreign subsidiaries are principally computed by the straight-line method. The range of the estimated useful lives of the assets is principally as follows:

Buildings and structures .....	15-60 years
Machinery and equipment .....	2-20 years

#### **f. Allowance for Doubtful Receivables**

The allowance for doubtful accounts is stated in amounts considered to be appropriate based on the companies' past credit loss experience and an evaluation of potential losses in the receivables outstanding.

#### **g. Retirement and Pension Plans**

Effective April 1, 2000, the Group adopted a new accounting standard for employees' retirement benefits and accounted for the liability for retirement benefits based on the projected benefit obligations and plan assets at the balance sheet date. The transitional obligation of ¥12,624 million (\$94,739 thousand), determined as of April 1, 2000, is being amortized over 15 years.

The liability for retirement benefits for directors and corporate auditors is also established at the amount that would be required if all directors and corporate auditors retired at each balance sheet date.

#### **h. Leases**

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

#### **i. Income Taxes**

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

#### **j. Appropriations of Retained Earnings**

Appropriations of retained earnings at each year end are reflected in the consolidated financial statements in the following year in which shareholders' approval to the proposed appropriations has been obtained.

### k. Foreign Currency Transactions

All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the exchange rates at the balance sheet date. The foreign exchange gains and losses from translation are recognized in the statement of operations to the extent that they are not hedged by forward exchange contracts.

### l. Foreign Currency Financial Statements

The balance sheet accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the current exchange rate as of the balance sheet date except for shareholders' equity, which is translated at the historical rate.

Differences arising from such translation were shown as "Foreign currency translation adjustments" in a separate component of shareholders' equity.

Revenue and expense accounts of consolidated foreign subsidiaries are translated into yen at the average exchange rate.

### m. Derivative Financial Instruments

The Company uses derivative financial instruments to manage their exposures to fluctuations in foreign exchange and interest rates. Foreign exchange forward contracts, currency options, interest rate caps, collars and swaps are utilized by the Company to reduce foreign currency exchange and interest rate risks. The Company does not enter into derivatives for trading or speculative purposes.

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

The foreign currency forward contracts and currency options are utilized to hedge foreign currency exposures for export sales. Trade receivables denominated in foreign currencies are translated at the contracted rates if the forward contracts qualify for hedge accounting. Currency options applied for forecasted (or committed) transactions are also measured at the fair value but the unrealized gains/losses are deferred until the underlying transactions are completed.

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

### n. Per Share Information

The computation of net income per share is based on the weighted average number of shares of common stock outstanding during each year. The average number of common shares used in the computation was 87,309 thousand shares for 2002 and 87,311 thousand shares for 2001.

Diluted net income per share of common stock assumes full conversion of the outstanding convertible notes and bonds at the beginning of the year (or at the time of issuance) with an applicable adjustment for related interest expense, net of tax.

It is not disclosed in 2002 because of the Group's net loss position.

Cash dividends per share presented in the accompanying consolidated statements of operations are dividends applicable to the respective years and those dividends are to be paid after the end of respective fiscal year.

## 3. SHORT-TERM INVESTMENTS AND INVESTMENT SECURITIES

Short-term investments and investment securities at March 31, 2002 and 2001, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Current:			
Time deposits	¥1,251	¥ 964	\$ 9,385
Non-marketable corporate bonds	664	74	4,985
Commercial paper	532		3,993
Total	¥2,447	¥1,038	\$18,363
Non-current:			
Marketable equity securities	¥5,251	¥6,165	\$39,407
Trust fund investments and other	454	568	3,409
Total	¥5,705	¥6,733	\$42,816

Information regarding the category of the securities classified as available-for-sale at March 31, 2002 and 2001, was as follows:

March 31, 2002	Millions of Yen			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Marketable equity securities	<b>¥4,171</b>	<b>¥1,736</b>	<b>¥656</b>	<b>¥5,251</b>
Government and corporate bonds	<b>137</b>	<b>1</b>	<b>6</b>	<b>132</b>
Trust fund investment and other	<b>113</b>		<b>61</b>	<b>52</b>

March 31, 2001	Millions of Yen			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Marketable equity securities	¥4,075	¥2,365	¥275	¥6,155
Government and corporate bonds	158	1	4	155
Trust fund investment and other	122		53	69

March 31, 2002	Thousands of U.S. Dollars			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Marketable equity securities	<b>\$31,302</b>	<b>\$13,029</b>	<b>\$4,924</b>	<b>\$39,407</b>
Government and corporate bonds	<b>1,031</b>	<b>4</b>	<b>46</b>	<b>989</b>
Trust fund investment and other	<b>851</b>		<b>456</b>	<b>395</b>

Available-for-sale securities and held-to-maturity securities whose fair value is not readily determinable as of March 31, 2002 and 2001, were as follows:

	Carrying Amount		
	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Available-for-sale:			
Non-marketable securities	<b>¥ 228</b>	¥ 298	<b>\$ 1,712</b>
Bond investment trust	<b>222</b>	553	<b>1,666</b>
Commercial paper	<b>532</b>	499	<b>3,993</b>
Held-to-maturity—Non-marketable foreign debt	<b>484</b>		<b>3,631</b>
Total	<b>¥1,466</b>	¥1,350	<b>\$11,002</b>

Proceeds from sales of available-for-sale securities for the years ended March 31, 2002 and 2001, were ¥533 million (\$3,996 thousand) and ¥1,727 million, respectively. Gross realized gains and losses on these sales, computed on the moving-average-cost basis, were nil and ¥52 million (\$388 thousand), respectively, for the year ended March 31, 2002 and ¥846 million and ¥37 million, respectively, for the year ended March 31, 2001.

The carrying values of debt securities by contractual maturities for securities classified as available-for-sale and held-to-maturity at March 31, 2002, were as follows:

	Millions of Yen		Thousands of U.S. Dollars	
	Available for Sale	Held to Maturity	Available for Sale	Held to Maturity
Due in one year or less	<b>¥836</b>	<b>¥484</b>	<b>\$6,276</b>	<b>\$3,632</b>
Due after one year through five years	<b>157</b>		<b>1,180</b>	
Total	<b>¥993</b>	<b>¥484</b>	<b>\$7,456</b>	<b>\$3,632</b>

#### 4. INVENTORIES

Inventories at March 31, 2002 and 2001, were comprised of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Finished products	<b>¥ 4,192</b>	¥ 5,152	<b>\$31,460</b>
Work in process	<b>3,865</b>	3,997	<b>29,004</b>
Raw materials and supplies	<b>4,800</b>	5,204	<b>36,023</b>
Total	<b>¥12,857</b>	¥14,353	<b>\$96,487</b>

#### 5. SHORT-TERM BORROWINGS AND LONG-TERM DEBT

Short-term borrowings consisted of bank loans and commercial paper. The annual interest rates applicable to the short-term bank loans ranged from 0.60% to 5.27% and 1.18% to 8.31% at March 31, 2002 and 2001, respectively. The amount of commercial paper at March 31, 2002, was ¥1,500 million (\$11,257 thousand). Average rates applicable to commercial paper were 0.9% (no commercial paper was held in the 2001 fiscal year).

The Company executed an ¥8,000 million (\$60,038 thousand) revolving credit facilities with a certain domestic banking group during the fiscal year ended March 31, 2002.

Long-term debt at March 31, 2002 and 2001, was comprised of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
0.20% Japanese yen convertible unsecured bonds, due 2007	¥ 9,523	¥10,000	\$ 71,467
0.55% to 2.60% (0.55% to 3.30% in 2001) loans from banks and insurance companies, due serially to 2007	5,791	5,136	43,465
1.97% (6.71% in 2001) loans from banks, in foreign currencies, due serially to 2003	229	321	1,716
2.13% to 6.80% (2.20% to 6.80% in 2001) loans from government financing institutions, due serially to 2027	2,041	2,268	15,316
Total	17,584	17,725	131,964
Less current portion	(2,441)	(3,045)	(18,319)
Long-term debt, less current portion	¥15,143	¥14,680	\$113,645

The annual maturities of long-term debt for the years subsequent to March 31, 2002, are as follows:

Year Ending March 31	Millions of Yen	Thousands of U.S. Dollars
2003	¥ 2,441	\$ 18,319
2004	2,246	16,856
2005	1,390	10,434
2006	1,074	8,063
2007	578	4,336
Thereafter	9,855	73,956
Total	¥17,584	\$131,964

A summary of assets pledged as collateral for short-term borrowings of ¥3,059 million (\$22,956 thousand) and long-term debt of ¥7,098 million (\$53,270 thousand) at March 31, 2002, is as follows:

	Millions of Yen	Thousands of U.S. Dollars
Investment securities	¥ 3,157	\$ 23,693
Land	5,038	37,808
Buildings and structures (net book value)	6,192	46,471
Machinery and equipment (net book value)	2,392	17,948
Others	133	1,000
Total	¥16,912	\$126,920

As is customary in Japan, security must be provided if requested by a lending bank and such bank has the right to offset cash deposited with it against any debt or obligation that becomes due and, in the case of default or certain other specified events, against all debt payable to the bank.

The 0.2% Japanese yen convertible unsecured bonds are convertible into common stock by the holders on any date up to and including September 27, 2007, at a conversion price of ¥1,023 per share. The bonds are redeemable at the option of the Company in whole or in part, on or at any time, after October 1, 2001, at the same prices as the principal amount thereof.

The conversion price for the above convertible debt is subject to adjustments in certain instances, including common stock splits. At March 31, 2002, all outstanding convertible debt is convertible into 9,308,895 shares of common stock of the Company.

## 6. RETIREMENT AND PENSION PLANS

The Company and its certain consolidated subsidiaries have severance payment plans for employees, directors and corporate auditors.

Under most circumstances, employees terminating their employment are entitled to retirement benefits determined based on the rate of pay at the time of termination, years of service and certain other factors. Such retirement benefits are made in the form of a lump-sum severance payment from the Company or from certain consolidated subsidiaries and annuity payments from a trustee (the funds). Employees are entitled to larger payments if the termination is involuntary, by retirement at the mandatory retirement age, by death, or by voluntary retirement at certain specific ages prior to the mandatory retirement age. The liability for retirement benefits at March 31, 2002 for directors and corporate auditors was ¥587 million (\$4,405 thousand). The retirement benefits for directors and corporate auditors are paid subject to the approval of the shareholders.

The liability for employees' retirement benefits at March 31, 2002 and 2001, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Projected benefit obligation	¥ 60,202	¥ 52,078	\$ 451,795
Fair value of plan assets	(28,446)	(29,824)	(213,479)
Unrecognized prior service cost	3,597		26,995
Unrecognized actuarial loss	(17,446)	(4,696)	(130,928)
Unrecognized transitional obligation	(10,898)	(11,782)	(81,783)
Net liability	¥ 7,009	¥ 5,776	\$ 52,600

The components of net periodic benefit costs for the years ended March 31, 2002 and 2001, are as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Service cost	¥ 1,310	¥ 1,664	\$ 9,828
Interest cost	1,802	1,722	13,522
Expected return on plan assets	(1,172)	(1,592)	(8,792)
Recognized actuarial loss	419		3,147
Amortization of transitional obligation	838	842	6,291
Net periodic benefit costs	¥ 3,197	¥ 2,636	\$23,996

Assumptions used for the years ended March 31, 2002 and 2001, are set forth as follows:

	2002	2001
Discount rate	2.5%	3.5%
Expected rate of return on plan assets	4.0%	5.0%
Amortization period of prior service cost	12 years	
Recognition period of actuarial gain/loss	12 years	12 years
Amortization period of transitional obligation	15 years	15 years

## 7. SHAREHOLDERS' EQUITY

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

Prior to October 1, 2001, the Code required at least 50% of the issue price of new shares, with a minimum of the par value thereof, to be designated as stated capital as determined by resolution of the Board of Directors. Proceeds in excess of amounts designated as stated capital were credited to additional paid-in capital. Effective October 1, 2001, the Code was revised and common stock par values were eliminated resulting in all shares being recorded with no par value.

Prior to October 1, 2001, the Code also provided that an amount at least equal to 10% of the aggregate amount of cash dividends and certain other cash payments which are made as an appropriation of retained earnings applicable to each fiscal period shall be appropriated and set aside as a legal reserve until such reserve equals 25% of stated capital. Effective October 1, 2001, the revised Code allows for such appropriations to be set aside as a legal reserve until the total additional paid-in capital and legal reserve equals 25% of stated capital. The amount of total additional paid-in capital and legal reserve which exceeds 25% of stated capital can be transferred to retained earnings by resolution of the shareholders, which may be available for dividends. The Company's legal reserve amount, which is included in retained earnings, totals ¥773 million (\$5,801 thousand) and ¥738 million as of March 31, 2002 and 2001, respectively.

Under the Code, companies may issue new common shares to existing shareholders without consideration as a stock split pursuant to a resolution of the Board of Directors. Prior to October 1, 2001, the amount calculated by dividing the total amount of shareholders' equity by the number of outstanding shares after the stock split could not be less than ¥50. The revised Code eliminated this restriction.

Prior to October 1, 2001, the Code imposed certain restrictions on the repurchase and use of treasury stock. Effective October 1, 2001, the Code eliminated these restrictions allowing companies to repurchase treasury stock by a resolution of the shareholders at the general shareholders meeting and dispose of such treasury stock by resolution of the Board of Directors after March 31, 2002. The repurchased amount of treasury stock cannot exceed the amount available for future dividends plus the amounts of stated capital, additional paid-in capital or legal reserve to be reduced in the case where such reduction was resolved at the general shareholders meeting.

The Code permits companies to transfer a portion of additional paid-in capital and legal reserve to stated capital by resolution of the Board of Directors. The Code also permits companies to transfer a portion of unappropriated retained earnings, available for dividends, to stated capital by resolution of the shareholders.

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

## 8. INCOME TAXES

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 41% for the years ended March 31, 2002 and 2001. Foreign subsidiaries are subject to income taxes of the jurisdiction in which they operate.

The tax effects of significant temporary differences and loss carryforwards which resulted in deferred tax assets and liabilities at March 31, 2002 and 2001, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
<b>Current:</b>			
Deferred tax assets:			
Accrued bonuses	¥ 223	¥ 223	\$ 1,676
Accrued business tax	2	95	16
Unrealized profit incurred in intragroup transaction	16	64	120
Other	215	174	1,611
Offset		(23)	(2)
Less valuation allowance	(339)		(2,547)
<b>Total</b>	<b>¥ 117</b>	<b>¥ 533</b>	<b>\$ 874</b>
<b>Deferred tax liabilities:</b>			
Receivables		¥ 48	
Property and equipment	¥ 75		\$ 560
Other		51	
Offset	(1)	(23)	(2)
<b>Total</b>	<b>¥ 74</b>	<b>¥ 76</b>	<b>\$ 558</b>
<b>Non-current:</b>			
Deferred tax assets:			
Tax loss carryforwards	¥ 2,195	¥ 1,244	\$ 16,472
Pension and severance costs	2,612	1,588	19,600
Directors' retirement benefits	240	255	1,805
Other	540	200	4,055
Offset	(771)	(985)	(5,784)
Less valuation allowance	(3,799)	(1,244)	(28,514)
<b>Total</b>	<b>¥ 1,017</b>	<b>¥ 1,058</b>	<b>\$ 7,634</b>
<b>Deferred tax liabilities:</b>			
Unrealized gain on available-for-sale securities	¥ 589	¥ 844	\$ 4,418
Undistributed earnings of foreign subsidiaries	312	327	2,338
Other	43	65	325
Offset	(771)	(985)	(5,784)
<b>Total</b>	<b>¥ 173</b>	<b>¥ 251</b>	<b>\$ 1,297</b>

A reconciliation between the normal effective statutory tax rate for the years ended March 31, 2002 and 2001, and the actual effective tax rates reflected in the accompanying consolidated statements of operations is as follows:

	2002	2001
Normal effective statutory tax rate	<b>41.3%</b>	41.3%
Expenses not deductible for income tax purposes	<b>(0.5)</b>	1.2
Income not taxable for income tax purposes	<b>0.5</b>	(0.9)
Per capita portion of inhabitants taxes	<b>(0.4)</b>	1.0
Foreign tax credit	<b>3.3</b>	(1.2)
Valuation allowance	<b>(41.9)</b>	
Nondeductible taxes		2.6
Prior-period income taxes		(4.6)
Tax benefits not recognized on operating losses of subsidiaries		10.0
Income not taxable under the tax ordinance in the applicable foreign country	<b>(14.5)</b>	(22.6)
Other—net	<b>(1.5)</b>	3.4
Actual effective tax rate	<b>(13.7)%</b>	30.2%

At March 31, 2002, the Company and certain consolidated subsidiaries have loss carryforwards, which can be offset against taxable income, if any, of such Company and consolidated subsidiaries in the future, totaling approximately ¥7,430 million (\$55,761 thousand).

These tax loss carryforwards held by the Company and domestic subsidiaries, if not utilized, will expire as follows:

Year Ending March 31	Millions of Yen	Thousands of U.S. Dollars
2003	¥ 290	\$ 2,174
2004	220	1,649
2005	242	1,820
2006	32	241
2007	3,046	22,863
Total	<b>¥3,830</b>	<b>\$28,747</b>

The remaining balance of ¥3,600 million (\$27,014 thousand) held by foreign subsidiaries can be carried forward indefinitely provided that certain conditions are met.

## 9. RELATED PARTY/EMPLOYEE TRANSACTIONS

Related party transactions are not disclosed for the year ended March 31, 2001, because transactions with unconsolidated subsidiaries and associated companies became immaterial as a result of expansion of consolidation scope.

Transactions of the Company with unconsolidated subsidiaries and associated companies for the year ended March 31, 2002, were as follows:

	Millions of Yen	Thousands of U.S. Dollars
Acceptance capital increase	<b>¥2,481</b>	<b>\$18,619</b>

Loans to employees at March 31, 2002 and 2001, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Current	<b>¥ 20</b>	¥ 22	<b>\$ 153</b>
Non-current	<b>181</b>	282	<b>1,359</b>
Total	<b>¥201</b>	¥304	<b>\$1,512</b>

The loans bear annual interest ranging from 2.50% to 3.00%.

## 10. RESEARCH AND DEVELOPMENT COSTS

Research and development costs relating to new products and technologies were ¥1,044 million (\$7,832 thousand) and ¥1,068 million for the years ended March 31, 2002 and 2001, respectively.

## 11. LEASES

The Group leases certain machinery, computer equipment, office space and other assets.

Total rental expenses for the years ended March 31, 2002 and 2001, were ¥2,443 million (\$18,336 thousand) and ¥2,175 million, respectively, including ¥1,253 million (\$9,405 thousand) and ¥949 million of lease payments under finance leases.

On an "as if capitalized" basis, pro forma information of leased property such as acquisition cost, accumulated depreciation, lease payment obligations under finance lease, depreciation expense, interest expense of finance leases that do not transfer ownership of the leased property to the lessee for the years ended March 31, 2002 and 2001, was as follows:

	Millions of Yen			Thousands of U.S. Dollars		
	2002			2002		
	Machinery and Equipment	Furniture and Fixtures	Total	Machinery and Equipment	Furniture and Fixtures	Total
Acquisition cost	¥4,944	¥2,084	¥7,028	\$37,104	\$15,637	\$52,741
Accumulated depreciation	1,390	966	2,356	10,432	7,246	17,678
Net leased property	¥3,554	¥1,118	¥4,672	\$26,672	\$8,391	\$35,063
	Millions of Yen					
	2001					
	Machinery and Equipment	Furniture and Fixtures	Total			
Acquisition cost	¥2,825	¥1,546	¥4,371			
Accumulated depreciation	1,078	818	1,896			
Net leased property	¥1,747	¥728	¥2,475			

Obligations under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Due within one year	¥1,342	¥846	\$10,073
Due after one year	3,382	1,679	25,381
Total	¥4,724	¥2,525	\$35,454

Depreciation expense and interest expense under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
Depreciation expense	¥1,165	¥871	\$8,744
Interest expense	96	81	716
Total	¥1,261	¥952	\$9,460

Depreciation expense and interest expense, which were not reflected in the accompanying consolidated statements of operations, were computed by the straight-line method over the lease period.

## 12. DERIVATIVES

### a. Utilization

The Company utilizes various derivative financial instruments ("derivatives") to mitigate the risk of fluctuating foreign currency exchange rates and interest rates. The derivatives utilized by the Company include foreign exchange forward contracts, currency option contracts, interest rate caps, collars and swaps.

The Company enters into contracts with major financial institutions in order to avoid credit loss in the event of non-performance by counterparties to the contracts.

Exposure to market risk is managed through position limits, approvals and monitoring procedures. The operational reports prepared by the executive section with transaction report sent directly from financial institutions to the administrative section are regularly submitted to the Board of Directors for their analysis and monitoring of the current status of derivative activities.

For derivatives to hedge interest risk exposure, preapproval from the Board of Directors is required and basic policy and credit limits are established and approved by the Board of Directors.

### b. Market Value of Contracts

The Company had the following derivatives contracts outstanding at March 31, 2002 and 2001:

	Millions of Yen			
	2002		2001	
	Contract or Notional Amount	Fair Value	Contract or Notional Amount	Fair Value
Non-listed:				
Currency option trading:				
Selling—call option U.S.\$			¥2,001	¥105
Buying—put option U.S.\$			2,533	15
Interest rate option trading:				
Cap—buying	¥1,000		1,000	1
Collar:				
Floor—selling	500		500	13
Cap—buying	500	¥(10)	500	
Interest rate swaps trading (fixed rate payment, floating rate receipt)	1,000	(40)	1,000	(46)

	Thousands of U.S. Dollars	
	2002	
	Contract or Notional Amount	Fair Value
Non-listed:		
Interest rate option trading:		
Cap—buying	\$7,505	\$ 1
Collar:		
Floor—selling	3,752	
Cap—buying	3,752	(78)
Interest rate swaps trading (fixed rate payment, floating rate receipt)	7,505	(300)

Forward exchange contracts which are assigned to certain assets or liabilities denominated in foreign currency, shown by using that forward exchange rate in the consolidated balance sheets, are excluded from the above.

The contract or notional amounts of derivatives shown above do not represent the amounts of which those contracts could be exchanged to the counterparties and do not prescribe the index to credit or market risk sustained by the Company.

### 13. CONTINGENT LIABILITIES

At March 31, 2002, the Group had the following contingent liabilities:

	Millions of Yen	Thousands of U.S. Dollars
Trade notes discounted with banks	¥ 139	\$ 1,043
Guarantees and items of a similar nature:		
Unconsolidated subsidiaries and associated companies	808	6,064
Employees' housing loans	457	3,433
Total	¥1,404	\$10,540

## 14. SEGMENT INFORMATION

Information on operations in different industry segments, foreign operations and sales to foreign customers of the Company and its consolidated subsidiaries for the years ended March 31, 2002 and 2001, was as follows:

### (1) Operations in Different Industries

Year Ended March 31, 2002	Millions of Yen					Consolidated
	Audiovisual and Home Appliance Equipment	Communications and Peripheral Computer Equipment	Industrial Machinery and Equipment	Others	Eliminations and Corporate	
Sales to customers	¥46,350	¥41,641	¥16,187	¥5,368		¥109,546
Intersegment sales		109	1	1,218	¥(1,328)	
Total sales	46,350	41,750	16,188	6,586	(1,328)	109,546
Operating expenses	45,565	48,341	14,536	6,438	(324)	114,556
Operating income (loss)	¥ 785	¥ (6,591)	¥ 1,652	¥ 148	¥(1,004)	¥ (5,010)
Assets	¥32,114	¥43,122	¥ 9,089	¥ 6,883	¥20,772	¥111,980
Depreciation	2,150	3,073	407	311	167	6,108
Capital expenditures	2,009	3,065	143	133	775	6,125

Year Ended March 31, 2002	Thousands of U.S. Dollars					Consolidated
	Audiovisual and Home Appliance Equipment	Communications and Peripheral Computer Equipment	Industrial Machinery and Equipment	Others	Eliminations and Corporate	
Sales to customers	\$347,843	\$312,502	\$121,481	\$40,286		\$822,112
Intersegment sales		820	4	9,142	\$ (9,966)	
Total sales	347,843	313,322	121,485	49,428	(9,966)	822,112
Operating expenses	341,950	362,788	109,085	48,316	(2,431)	859,708
Operating income (loss)	\$ 5,893	\$(49,466)	\$ 12,400	\$ 1,112	\$ (7,535)	\$(37,596)
Assets	\$241,010	\$323,616	\$ 68,209	\$51,653	\$155,889	\$840,377
Depreciation	16,140	23,063	3,051	2,334	1,251	45,839
Capital expenditures	15,077	23,000	1,075	995	5,817	45,964

Year Ended March 31, 2001	Millions of Yen					Consolidated
	Audiovisual and Home Appliance Equipment	Communications and Peripheral Computer Equipment	Industrial Machinery and Equipment	Others	Eliminations and Corporate	
Sales to customers	¥50,722	¥58,806	¥19,474	¥6,422		¥135,424
Intersegment sales		106	132	1,481	¥(1,719)	
Total sales	50,722	58,912	19,606	7,903	(1,719)	135,424
Operating expenses	48,120	61,395	16,247	8,197	(799)	133,160
Operating income (loss)	¥ 2,602	¥ (2,483)	¥ 3,359	¥ (294)	¥ (920)	¥ 2,264
Assets	¥38,441	¥44,064	¥10,844	¥8,848	¥20,908	¥123,105
Depreciation	2,304	2,795	443	373	158	6,073
Capital expenditures	3,281	4,295	291	225	297	8,389

Notes: The audiovisual and home appliance equipment segment consists of micromotors, timers and motor units.

The communications and peripheral computer equipment segment contains micromotors, optical pick-up units and stepping motors.

The industrial machinery and equipment segment consists of magnetic card readers and machining units.

The others segment contains musical movements, etc.

The unallocated operating expenses is principally composed of general corporate expenses incurred by the Administration Headquarters of the Company.

## (2) Foreign Operations

The foreign operations of the Company and its consolidated subsidiaries for the years ended March 31, 2002 and 2001, were summarized as follows:

Year Ended March 31, 2002	Millions of Yen				Consolidated
	Japan	Asia	North America	Eliminations and Corporate	
Sales:					
Outside customers	¥62,496	¥43,486	¥3,564		¥109,546
Interarea	27,062	23,916	145	¥(51,123)	
Total sales	89,558	67,402	3,709	(51,123)	109,546
Operating expenses	94,055	67,586	3,381	(50,466)	114,556
Operating income (loss)	¥(4,497)	¥ (184)	¥ 328	¥ (657)	¥ (5,010)
Assets	¥70,166	¥33,272	¥2,288	¥ 6,254	¥111,980

Year Ended March 31, 2002	Thousands of U.S. Dollars				Consolidated
	Japan	Asia	North America	Eliminations and Corporate	
Sales:					
Outside customers	\$469,012	\$326,348	\$26,752		\$822,112
Interarea	203,090	179,484	1,088	\$(383,662)	
Total sales	672,102	505,832	27,840	(383,662)	822,112
Operating expenses	705,849	507,212	25,377	(378,730)	859,708
Operating income (loss)	\$ (33,747)	\$ (1,380)	\$ 2,463	\$ (4,932)	\$ (37,596)
Assets	\$526,579	\$249,695	\$17,168	\$ 46,935	\$840,377

Year Ended March 31, 2001	Millions of Yen				Consolidated
	Japan	Asia	North America	Eliminations and Corporate	
Sales:					
Outside customers	¥ 77,634	¥ 55,367	¥ 2,423		¥ 135,424
Interarea	36,315	24,683	94	¥(61,092)	
Total sales	113,949	80,050	2,517	(61,092)	135,424
Operating expenses	109,655	80,824	2,604	(59,923)	133,160
Operating income (loss)	¥ 4,294	¥ (774)	¥ (87)	¥ (1,169)	¥ 2,264
Assets	¥ 76,736	¥ 40,162	¥ 2,147	¥ 4,060	¥ 123,105

Notes: Asia area is composed of China, Hong Kong, Malaysia, Singapore, Chinese Taipei and Korea.  
North America area represents the United States of America.

## (3) Sales to Foreign Customers

Sales to foreign customers for the years ended March 31, 2002 and 2001, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2002	2001	2002
North America	¥ 2,935	¥ 2,678	\$ 22,024
Europe	3,247	3,654	24,370
Asia	55,782	69,191	418,629
Others	1,737	659	13,032
Total	¥63,701	¥76,182	\$478,055

## INDEPENDENT AUDITORS' REPORT

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**Deloitte  
Touche  
Tohmatsu**

To the Board of Directors of  
Sankyo Seiki Mfg. Co., Ltd.:

We have examined the consolidated balance sheets of Sankyo Seiki Mfg. Co., Ltd. and consolidated subsidiaries as of March 31, 2002 and 2001, and the related consolidated statements of operations, shareholders' equity, and cash flows for the years then ended, all expressed in Japanese yen. Our examinations were made in accordance with auditing standards, procedures and practices generally accepted and applied in Japan and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Sankyo Seiki Mfg. Co., Ltd. and consolidated subsidiaries as of March 31, 2002 and 2001, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles and practices generally accepted in Japan applied on a consistent basis.

Our examinations also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 1. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

*Deloitte Touche Tohmatsu*

June 27, 2002

