ISEKI

# Improving Agricultural Environments around the World

**ISEKI & CO., LTD.**

**2006**

**Annual Report**

Year ended March 31, 2006

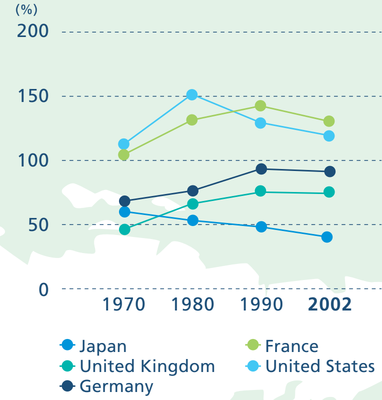
# Growing Together: Agriculture and the Global Community

**Cover illustrations:**
Each year, Iseki selects a Sanae Nationwide Children's Art Contest prizewinner on the theme of "families who work in agriculture." One of our aims is to support families that stay in touch with each other working together on the farm.

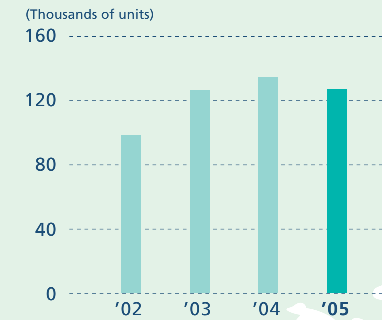
# Expanding and Developing Our Business—from Japan to the World

As the worldwide population continues to increase, providing sufficient food remains a topic of major global concern. One issue is how the rapid onslaught of global warming will affect the ability to expand food supplies. Agriculture will play a growing role as it attempts to address such serious issues. Iseki sees raising agricultural productivity in Japan and the rest of the world as its mission, thereby playing its part in helping to alleviate potential food shortages. As we continue our work to meet the wide-ranging needs of customers in Japan and other countries, we will contribute to shaping the future of agriculture.

Self-Sufficiency Ratios of Leading Advanced Nations (calorie basis)




U.S. Market for Compact Tractors




Source: U.S. Association of Equipment Manufacturers
* Engines of 50PS (PTO horsepower of 40) or less
** Excludes mowers

In the U.S. market for compact tractors, strong economic performance is fueling replacement demand, and the number of housing starts is rising. These factors caused compact tractor sales to surge from 83 thousand in 2000 to 134 thousand in 2004. In 2005, relatively high sales continued, at 127 thousand. Although the U.S. economic outlook is uncertain, we expect demand to remain at approximately 120 thousand during the three years beginning in 2006.

In the People's Republic of China, the National People's Congress (NPC) has announced a number of measures to raise income levels in agricultural communities and ensure stable food production volumes. The NPC has also introduced an agricultural equipment promotion law to encourage the modernization of agricultural equipment. Demand for Japanese combine harvesters is expanding rapidly, and measures are under way to increase the demand for rice transplanters. Consequently, we anticipate acceleration in demand for agricultural equipment from this market.

In Japan, the declining number of agricultural households is causing the scale of farms to grow, propelling demand for larger equipment. For the past few years, demand for agricultural equipment has remained steady at around ¥350 billion. In the short term, changes in agricultural policy may cause demand to decline, but over the medium to long term we expect the increasing scale of farms to invigorate Japanese agriculture, resulting in firm demand for agricultural equipment.

## Europe

**Sales of compact tractors and riding mowers**

Europe is generally considered a mature market, where demand for compact tractors and mowers is stable. However, in recent years market needs have changed. Riding-mower demand has shifted from models powered by gasoline engines to those using diesel engines, and an increasing number of compact tractor owners are replacing secondhand equipment with new models.

## China

**Sales of combine harvesters and rice transplanters**

## Japan

**Development, production and sales of agricultural equipment and the expansion of agriculture-related business, including facility construction and agricultural raw material sales**

## Other Asian Markets

**Sales of rice-farming equipment (tractors, combine harvesters and rice transplanters)**

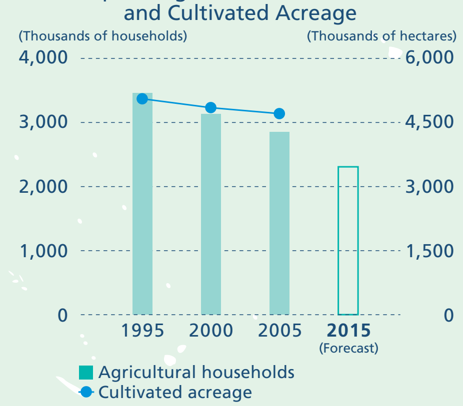
Rice is a staple foodstuff in Asia, and this area accounts for approximately 90% of global rice production. Ongoing mechanization in South Korea and Taiwan continues to drive the modernization of agriculture, and demand for large agricultural equipment that is highly efficient and durable is increasing as a result. Anticipated rises in the populations and economic strength of Southeast Asian countries should encourage agricultural mechanization, presenting a major market opportunity.

## Australia

**Sales of compact tractors* and riding mowers**

*Tractors with PTO horsepower of 40 or less

Japan's Agricultural Households and Cultivated Acreage




Source: Ministry of Agriculture, Forestry and Fisheries, 2005 Agriculture Census, *Basic Plan for Food, Agriculture and Agricultural Communities*, Outlook for the Agricultural Structure (2015)

## North America

**Sales of compact tractors and riding mowers**

With the number of Japanese agricultural households in decline and the average age of agricultural employees increasing, agricultural product imports are growing, creating ongoing challenges in Iseki's market. At the same time, while global food supplies are forecast to grow tighter over the medium to long term, Japan's food self-sufficiency ratio is one of the lowest among leading advanced nations. For this reason, in 2005, the Japanese government announced its *Basic Plan for Food, Agriculture and Agricultural Communities*, which aims to expand domestic agricultural production and sets self-sufficiency targets to be achieved by fiscal 2015. A new law to stabilize management by next-generation agriculturists went into effect in Japan in June 2006. The overriding aims of the law are to educate the core generation of farmers who are taking over farm operations about agricultural production, raise international competitiveness in agriculture, review pricing policies that have affected all farmers thus far, as well as to implement income support policies for people who are taking over farm operations. Furthermore, in June 2006, the Ministry of Economy, Trade and Industry announced its "Economic Growth Strategy Outline," which sets targets for strengthening agriculture in Japan and improving its international competitiveness.

## Profile: Management Principles

During the 80 years since its establishment in 1926 as a specialist manufacturer of agricultural equipment, ISEKI & CO., LTD. has contributed to the modernization of agriculture in Japan. Over this period, we have taken the lead in the development and introduction of agricultural equipment that has made farming more efficient and less labor-intensive.

Agriculture has a vital role in such issues as the increasing global population, food shortages, Japan's food self-sufficiency ratio and the protection of national boundaries. As a manufacturer of agricultural equipment, we believe that our mission in society will continue to expand.

Our core philosophy is to contribute to agriculture in Japan and the rest of the world by providing products that delight our customers. We will continue to expand our activities based on this principle.

## Contents



### Cautionary Note Regarding Forward-Looking Statements

This annual report contains forward-looking statements in which certain risks and uncertainties are inherent and actual performance may differ materially from the expectations indicated herein. Readers are therefore cautioned not to rely exclusively on these statements, which take into account the best information that is available to management at the time. The Company undertakes no responsibility to disclose revisions to these statements owing to future developments, which may reflect changes in the environment and unexpected climatic events.

# Using Agriculture to Help Achieve a Bountiful Environment

Japanese agriculture is in a period of change and Iseki is helping to lay the groundwork for its future. We are also substantially expanding our activities outside Japan.

## Fiscal 2006 Operating Performance

Q

### To start, please describe the operating environment and the Iseki Group's performance during fiscal 2006.

Fiscal 2006 was an important year for the Iseki Group, as we celebrated our 80th anniversary of operations. Successful efforts to expand sales both inside and outside the Group and reform our profit structure resulted in higher earnings and profits than during the previous fiscal year.

During the year, the Japanese economy moved into a phase of gradual recovery, but high crude oil and materials prices worldwide made the situation difficult to judge. Other factors also contrived to make this a time of major change for Japanese agriculture. For example, in October 2005 the Japanese government unveiled plans to increase the country's food self-sufficiency ratio.

Under these circumstances, domestic demand for agricultural equipment was nearly flat, but exports remained favorable. Consequently, net sales in Japan slipped, while overseas sales expanded significantly.

Such negative factors as high raw materials prices affected profits. However, we managed to overcome these hurdles by cutting expenses.

Q

### Fiscal 2006 was the final year of Iseki's three-year business plan. Could you describe some of your major goals and achievements?

Our previous medium-term plan set four primary targets. Of these, we exceeded our goal of increasing overseas sales 50%—actually raising these sales 80%. Another objective was to reduce interest-bearing debt to the ¥60 billion level. We met this goal one year early, further curtailing interest-bearing debt to ¥55.4 billion as of March 31, 2006.

However, we fell short of achieving two of our goals. We were unable achieve a 20% share of the Japanese market for agricultural equipment, and we missed our operating income target of ¥10 billion.

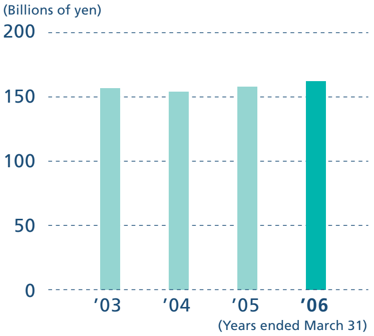
## Achieving New Levels of Growth

Q

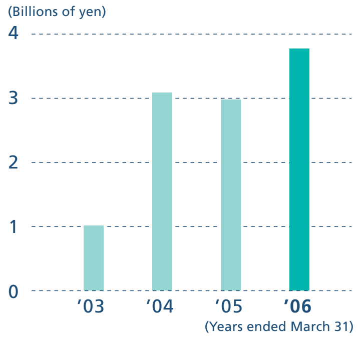
### Would you explain the primary targets of the new medium-term plan and describe some of the strategies to take you toward those objectives?

One major goal is to expand overseas sales. In fiscal 2006, overseas sales amounted to ¥20.5 billion, accounting for 12.7% of net sales, but by fiscal 2009 we plan to raise this ratio to 15%, or ¥27.0 billion. By fiscal 2011, we intend to expand this ratio further, reaching ¥36.0 billion, or 20% of net sales.

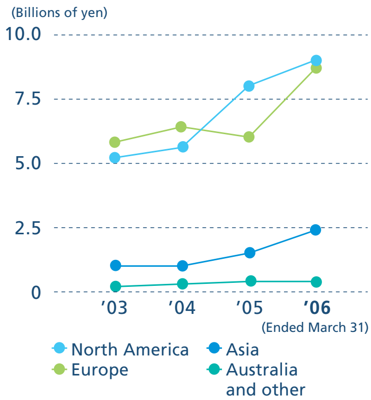
Net Sales




Net Income



Overseas Sales by Region (Including Machinery and Parts)




By fiscal 2011, we forecast that North America, Europe and Asia will each account for approximately ¥12.0 billion in sales. In the North American market, we expect sales to level off, as demand for compact tractors eases, but we will counter by proactively introducing new products to raise our market share. In Europe, we anticipate no major changes in demand for compact tractors and riding mowers. However, we will continue to introduce new products, expand our involvement in landscaping equipment and boost sales of tractors for use on small farms. In line with ongoing economic development in Asia, we expect agricultural equipment demand to accelerate. In response, we will develop products to meet the market needs of each country in this region, introduce these products and work to extend our sales network. Within Asia, we look forward to significant increases in sales to China.

## Q Could you describe the Chinese market and Iseki's initiatives in more detail?

In the near future, I believe the Chinese market for agricultural equipment will change substantially. Recently, the Chinese government announced plans to modernize the nation's agriculture, which has prompted a groundswell of expectation. In December 2005, the nation's agriculture ministry outlined its goals for the nationwide mechanization of wetland rice cultivation. By 2015, the ministry targets 70% mechanization of rice farming, including 80% mechanization for harvesting and 45% mechanization of the planting process.

In fiscal 2006, full-fledged sales commenced of the combine harvester manufactured by our subsidiary, ISEKI–CHANGZHOU MFG. CO., LTD., and the company also began exporting rice transplanters. The subsidiary is expanding its sales and service network, cultivating its own dealers and building up its structure through cooperation with CHANGZHOU DONGFENG AGRICULTURAL MACHINERY GROUP CO., LTD., which is also located in Changzhou. As rapid demand increases are expected for both types of equipment, we look forward with anticipation to this subsidiary's ongoing expansion of its sales and service networks.

"We are expanding our sales region and strengthening our agriculture business in China."

## New Three-Year Business Plan

### Plan for Consolidated Profits

| | Fiscal 2006 performance | | Fiscal 2009 plans |
|---|---|---|---|
| Net sales | ¥161.7 billion | +13.3 | ¥175.0 billion |
| Operating income | ¥7.4 billion | +2.6 | ¥10.0 billion |
| Ordinary income | ¥6.8 billion | +2.7 | ¥9.5 billion |
| Net income | ¥3.7 billion | +1.3 | ¥5.0 billion |

### Primary Targets

| | Fiscal 2006 performance | | Fiscal 2009 targets |
|---|---|---|---|
| Overseas sales ratio | 12.7% | +2.3% | 15% |
| Japanese agricultural equipment market share | 18.1% | +1.9% | 20% |
| Ratio of operating income to net sales | 4.6% | +0.9% or more | 5.5% or more |
| Shareholders' equity ratio | 31.9% | +8.1% or more | 40% or more |
| Ratio of interest-bearing debt to shareholders equity (debt-equity ratio) | 0.9 times | | 0.6 times or less |

### Basic Strategies

- Expand overseas sales
- Achieve a 20% share of the Japanese market for agricultural equipment
- Further strengthen product competitiveness
- Improve our consolidated financial structure by raising profitability and cash flow

**New Products in 2006**

TJW series of large tractors

PZ series of rice planters

Tiller for the hobby market

## How will changes in agricultural policy impact the Japanese market? Also, please explain Iseki's plans to develop these operations.

The part of the current changes in agricultural policy that will have the greatest impact on farmers are the cross-product operational stabilization measures, which establish a direct payment system. Currently in the period of changing over to this new system, the time needed for farmers to assume operations and the state of progress are unclear, which has caused the domestic market for agricultural equipment to slacken slightly since the beginning of 2006. However, we believe this phenomenon is only temporary. The measures themselves are limited to motivated and capable new farmers, and are designed to stabilize operations. We expect these measures to result in a greater number of large-scale operations that will require more large-scale agricultural equipment.

We foresee the diversification and renewed vigor of domestic agriculture, with an increase in agribusiness and a growing number of hobby farms where baby boomers can enjoy tending their vegetable patches.

We will put forth our best efforts to respond precisely to these changes in our operating environment by adjusting our systems and introducing new products. In January 2006, we established the Next Generation Support Office to establish strategic sales plans targeting people who are taking over farms and to strengthen our support systems for these people at our sales companies. We are also aggressively introducing new products, centering on large agricultural equipment. In fiscal 2007, we plan to introduce two large tractors—95 horsepower and 105 horsepower models—and we are performing model changes on our mainstay rice transplanter series. Within three years, we plan to complete model changes for all rice transplanter series, as we work to raise our sales volume and market share in this category.

## What measures are you taking to strengthen product competitiveness?

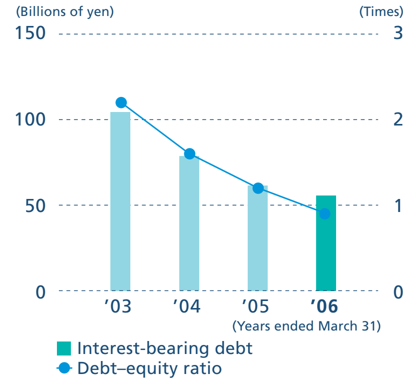
To boost product competitiveness, we will reflect market needs through detailed product development that enhances price, performance, quality and service. From a cost perspective, we aim to reduce the cost of production by 30%, and we are implementing thorough cost-cutting initiatives that cover design, purchasing and production. These measures should strengthen our price competitiveness, while ensuring appropriate profits. We are also working to improve performance and quality, as well as service levels, by investing in equipment to expand sales companies' maintenance factories. This level of investment is higher than in our previous three-year plan.

## The Company's financial structure appears to have improved. What future directions are you considering?

In line with our previous three-year plan, we worked to reduce interest-bearing debt, slim our balance sheet and reform our financial structure. Such efforts culminated in the annual accumulation of shareholders' equity and significantly improved our debt–equity and shareholders' equity ratios. In terms of profit and losses, we concentrated on our financial balance, greatly improving non-operating categories. These moves were also effective.

In the future, we will work together as a group to raise profitability and cash flow, further enhancing our financial structure. We will focus on holding down interest-bearing debt and invest our Groupwide equity and assets more efficiently.

Interest-Bearing Debt and Debt–Equity Ratio




## Corporate Governance

### Q Japan's Corporate Law, which went into effect in May 2006, obliges companies to create internal control systems. In recent years, many questions have arisen on the topic of corporate governance. What is Iseki's status in this area?

The Company is making every effort to strengthen its corporate governance and disclose information appropriately and in a timely manner. We consider these measures a vital part of maintaining positive relations with our stakeholders, including shareholders, business partners, members of regional communities and employees. We also keep in close contact with business partners, sales agents and employees so that we remain aware of currently shared issues and implement management principles thoroughly.

We recognize the establishment of Groupwide internal control systems as a topic of prime management importance. We are establishing controls to ensure that our business activities are efficient and conform to all applicable regulations and policies, while creating strategies to store and manage information appropriately. In April 2006, we established the Internal Control Department, as well as the Internal Control Promotion Council, whose membership includes all directors, as well as certified public accountants and other external advisors. In these ways, we are promoting the development of an internal control system.

### Q Are there any closing messages that you would like to leave with shareholders?

The environment in which Iseki operates is shaped by changes in national politics and the economy, and we expect this situation to continue. We will continue to respond quickly and adeptly to shifts in our operating environment. At the same time, we will work toward a corporate structure that ensures stable operating performance.

I would like to thank our shareholders for their confidence in us to date, and ask for their continued support.

August 2006

Hiroyuki Nakano,
President

Special Feature

# What We Can Offer the Next Generation

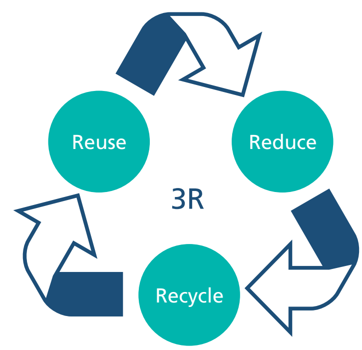
We at Iseki want to ensure that the next generation can also enjoy bountiful agriculture and the abundant natural environment that makes it all possible. To achieve this aim, we make the most of the expertise and technical skills we have built up over the years in the fields of agriculture and agricultural equipment, contributing to this aim in Japan and throughout the world.

## Environmental Initiatives

We believe that agriculture, which forms the base for our operations, is one of the gentlest industries, blessed as it is by the changing seasons, the sun and the rain. Our connection with the natural environment brings our responsibilities to society into sharp relief, in a way that other industries may not appreciate. This awareness underpins the environmental preservation initiatives of the entire Iseki Group.

Based on our management concept of an "axis of agriculture and agricultural machinery," we have created the Green Circle Eco-Vision, which underpins the environmental preservation efforts through which we aim to achieve harmony between nature and society. On this foundation, we have created an environmental concept, a basic environmental policy and environmental conduct guidelines. We have also established medium- to long-term environmental objectives to be accomplished by 2010, which we are approaching from the four angles outlined below.

Medium- to Long-Term Environmental Targets


### Eco-Friendly Factories—Production Activities that Place Little Burden on the Environment

To reduce $CO_2$ emissions per production output, we have mounted initiatives to prevent global warming, reduce water usage, minimize waste material and control chemical substances.

### Eco-Friendly Products—Provision of Environment-Friendly Products

We conduct life-cycle assessments to evaluate, and then minimize, the environmental load at each stage, involving raw materials, production, distribution, use, recovery, breakdown and processing, as well as to improve fuel consumption. We also seek to develop products that are easy to reuse, reduce and recycle.

Furthermore, we work to minimize the environmental impact of packaging, promote green procurement and foster environment-friendly agriculture.

### Building Our Environmental Management Base

We are working to extend the scope of our environmental management system beyond production divisions to encompass the entire Group. We also have established a project team that is working to achieve environmental certification. Three of our manufacturing plants have received ISO 14001 certification, and in May 2005 the Group's business locations received EA-21 designation under a program by Japan's Ministry of the Environment that evaluates environmental activities.

### Creating Harmony with Stakeholders

We are also promoting environmental education and environmental communication. In addition to promoting environmental education at morning meetings, through internal newsletters and at training seminars, environmental volunteers conduct "green" activities at various locations, and we transmit and provide information over the Internet.

In March 2005, we became the first entity in the agricultural machinery industry to be certified by the Development Bank of Japan as an "environment-aware management promotion business" under the bank's financing system. Under the bank's screening (credit rating) system, companies are awarded points, and interest rates are set accordingly at one of three levels corresponding to the number of points awarded. This financing system is the world's first to apply environmental credit ratings. In 2005, we received a number two ranking, but after improving in each of the areas cited for improvement, we achieved a top-level ranking in March 2006.

As a result, we have become the first company to improve its ranking since the system was introduced. We believe these results point to the proactiveness and forward thinking of the Iseki Group's environmental preservation efforts.

## Iseki the Technology Company

As a pioneer in agricultural equipment, many of Iseki's developments parallel the development of agriculture in Japan, such as the introduction of the nation's first integrated system of rice-cultivation equipment. In such ways, we have earned a reputation as "Iseki the technology company," steadily developing new products ahead of the pack and delivering them throughout the world.

Compact tractor for the European market

Combine harvester for the Chinese market

Although Japanese agriculture is currently in a state of change, we are developing large-scale equipment that we expect to be used in the medium to long term by the people who are now taking over in the farm industry. To make agriculture more efficient and less labor-intensive, in addition to our mainstay rice cultivation equipment we are developing equipment for types of agriculture that have substantial opportunities to save labor through mechanization, such as dryland crops and vegetables. Iseki is also developing components related to agricultural equipment.

For the export market, an area of current emphasis, we are developing products for the lawn and garden machinery markets in North America and Europe, which continue to expand. We are also developing products that meet the specific needs of other markets. These include combine harvesters and rice transplanters for China and tractors for Southeast Asia.

### R&D Structure

In all our technical endeavors, we abide by four keywords: satisfaction, safety, reliability and the environment. We continually pursue R&D that is superior in terms of product development capability, quality and cost-competitiveness.

Iseki's R&D system comprises the head office, whose facilities develop components for agricultural equipment and facilities, and affiliated companies, which develop engines, compact agricultural equipment, food processing machinery and such precision machinery as testing equipment.

Rounding out our development network are N.V. ISEKI EUROPE S.A., our North American representative office, ISEKI–CHANGZHOU MFG. CO., LTD., in China, and our Thai representative office. We have established these R&D bases with a view to accelerating technical development in Europe, North America, China and other parts of Asia.

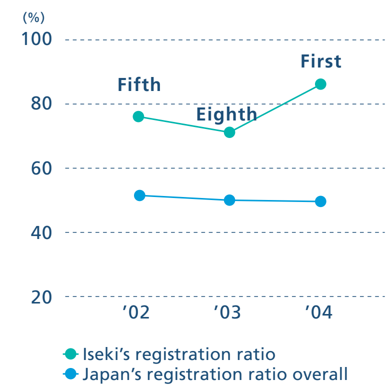
## Intellectual Property Rights

The Company's emphasis on technology and the development of its R&D capabilities have delivered numerous results. Not only the development divisions but also the Company as a whole promotes invention proposal activities, and the number of invention proposals increases every year. Public patent statistics reflect Iseki's R&D prowess.

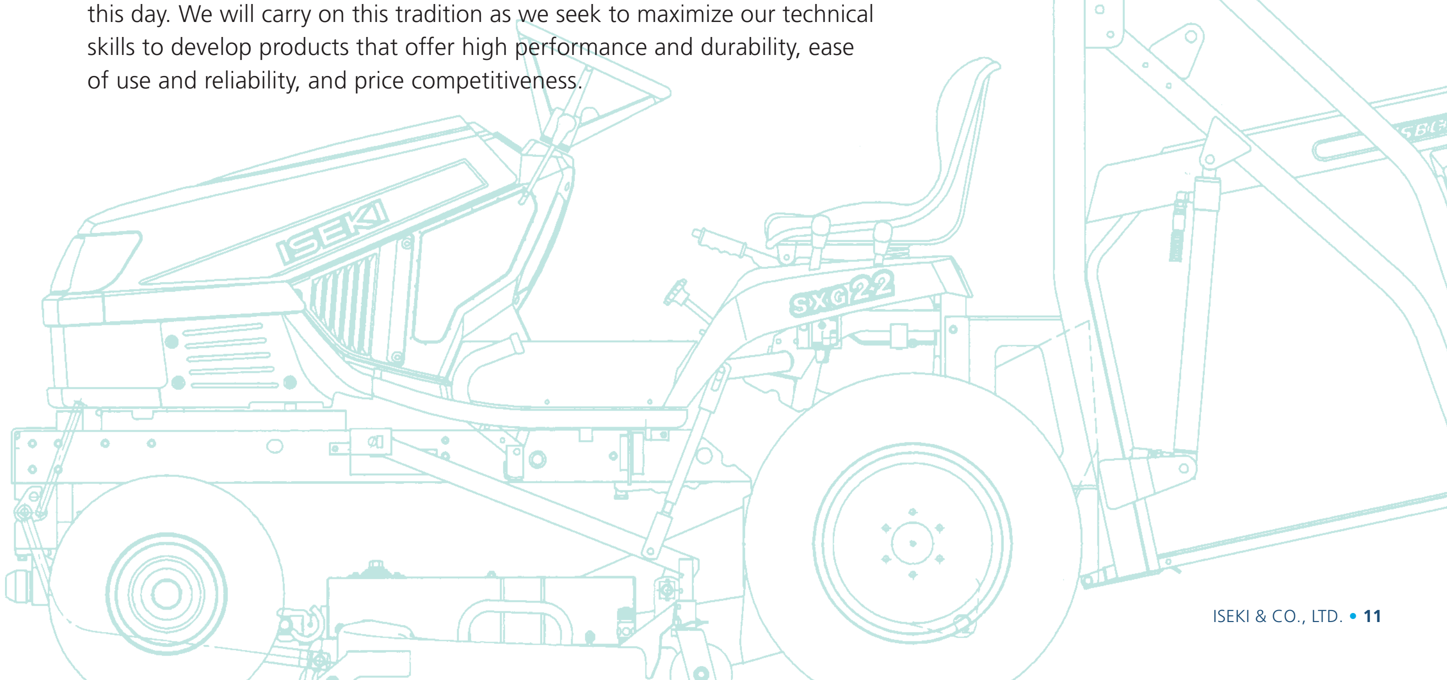
According to the 2005 annual report published by the Japan Patent Office (JPO) in August 2005, Iseki ranked first among all industries for the number of patents granted in 2004. This is the third consecutive year we have ranked in the top 10, evincing the high quality of our published patents. At the same time, the JPO announced the number of published patents in the agriculture and fisheries sector in 2003. In this category, Iseki ranked first for the fourth consecutive year. Such results indicate that the Iseki Group leads its competitors in technical invention and patent applications.

Of these patent applications, the majority represents promising technologies that have yet to be incorporated into products. Such Iseki-owned rights contribute substantially to assuring the superiority of Iseki products by protecting the capabilities and functions that are sales points for products already available, and highlight new technology research directions when new products are developed.

Patent Registration Ratios




Since its time of establishment, Iseki's engineers have won numerous awards, such as those bestowed by the Japan Institute of Invention and Innovation, for their contributions to the development, education and implementation of technologies related to agricultural equipment. The spirit of pushing R&D frontiers that began with the Company's founder—who was also an engineer—imbued Iseki with a tradition of success in transforming intellectual creative endeavors into practical technologies that endures to this day. We will carry on this tradition as we seek to maximize our technical skills to develop products that offer high performance and durability, ease of use and reliability, and price competitiveness.



# Directors and Corporate Auditors

(As of June 27, 2006)

From left: Akio Kikuchi, Ryoichi Murakami, Keiichi Takeshita, Hideki Arikawa, Kenji Minami, Hiroyuki Nakano, Katsumi Imanishi, Seiichiro Gamoh, Kazuyoshi Sonoda, Susumu Tada

## Board of Directors

| | |
|---|---|
| President | Hiroyuki Nakano* |
| Executive Managing Directors | Kenji Minami* |
| | Katsumi Imanishi* |
| | Hideki Arikawa* |
| Managing Directors | Seiichiro Gamoh |
| | Keiichi Takeshita |
| | Kazuyoshi Sonoda |
| Directors | Ryoichi Murakami |
| | Susumu Tada |
| | Akio Kikuchi |

*Representative Director

## Corporate Auditors

| | |
|---|---|
| Corporate Auditors | Hiroshi Ueno |
| | Hiroyoshi Enokida |
| | Keiji Itoh |
| | Norio Yasunaga |

Back row, from left: Keiji Itoh, Norio Yasunaga
Front row, from left: Hiroshi Ueno, Hiroyoshi Enokida

# Financial Section

# Consolidated Five-Year Financial Summary

ISEKI & CO., LTD. and Consolidated Subsidiaries
Years ended March 31

| | Millions of yen | | | | | Thousands of U.S. dollars |
|---|---|---|---|---|---|---|
| | **2006** | 2005 | 2004 | 2003 | 2002 | **2006** |
| **For the year:** | | | | | | |
| Net sales | **¥161,744** | ¥157,462 | ¥153,624 | ¥156,381 | ¥162,361 | **$1,376,897** |
| Cost of sales | **107,959** | 105,128 | 103,101 | 105,374 | 111,418 | **919,035** |
| Selling, general and administrative expenses | **53,785** | 45,817 | 44,149 | 44,814 | 46,662 | **457,862** |
| Operating income | **7,459** | 6,517 | 6,374 | 6,193 | 4,281 | **63,497** |
| Net income | **3,757** | 2,965 | 3,077 | 1,009 | 1,749 | **31,983** |
| Capital expenditures | **5,652** | 5,411 | 5,080 | 4,919 | 6,144 | **48,114** |
| Depreciation and amortization | **3,910** | 4,167 | 4,483 | 4,898 | 5,002 | **33,285** |
| **At year-end:** | | | | | | |
| Total assets | **183,831** | 184,477 | 197,156 | 215,163 | 231,440 | **1,564,919** |
| Net shareholders' equity | **58,645** | 51,726 | 49,576 | 46,483 | 45,197 | **499,234** |
| Number of employees | **6,680** | 6,665 | 6,644 | 6,743 | 7,052 | |

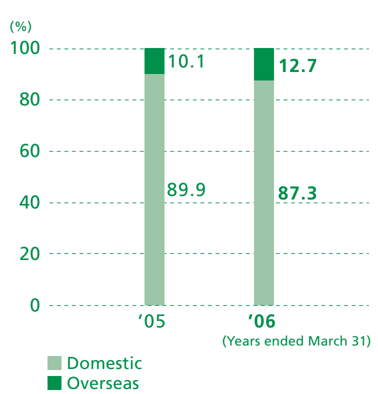
| | Yen | | | | | U.S. dollars |
|---|---|---|---|---|---|---|
| **Per share data:** | | | | | | |
| Net income | **¥ 17.23** | ¥ 13.61 | ¥ 13.90 | ¥ 4.56 | ¥ 7.79 | **$ 0.15** |
| Diluted net income | **15.27** | 12.74 | — | — | — | **0.13** |
| Net assets | **259.64** | 238.88 | 226.85 | 210.44 | 201.12 | **2.21** |
| Cash dividends | **3.00** | 3.00 | 3.00 | — | — | **0.03** |

| | (%) | | | | |
|---|---|---|---|---|---|
| **Ratios:** | | | | | |
| Return on equity | **6.8%** | 5.9% | 6.4% | 2.2% | 4.0% |
| Return on assets | **2.0** | 1.6 | 1.5 | 0.5 | 0.7 |
| Shareholders' equity to total assets | **31.9** | 28.0 | 25.1 | 21.6 | 19.5 |

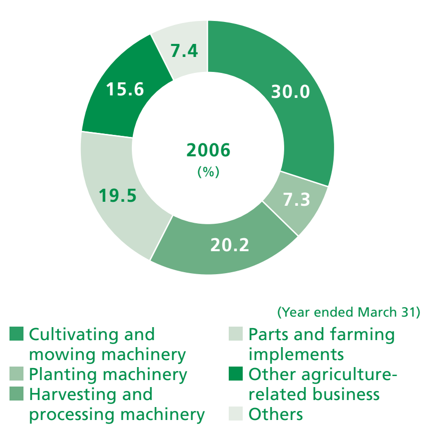
Note: U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥117.47 to US$1.00, the approximate rate of exchange at March 31, 2006.

Definitions: Return on equity = 100 x net income / average net shareholders' equity in the fiscal period
Return on assets = 100 x net income / average total assets in the fiscal period
Shareholders' equity to total assets = 100 x net shareholders' equity / total assets

Breakdown of Sales by Market




Composition of Sales by Product Category



# Management's Discussion and Analysis

## Overview

In fiscal 2006, ended March 31, 2006, domestic shipments of agricultural equipment were on a par with the preceding term, while exports remained buoyant. In this environment, the Iseki Group sought to meet increasingly diverse customer needs by rounding out its new product offerings and through proactive sales efforts, aiming to expand domestic and export sales. As a result, net sales expanded 2.7%, or ¥4.3 billion, to ¥161.7 billion.

### Overseas

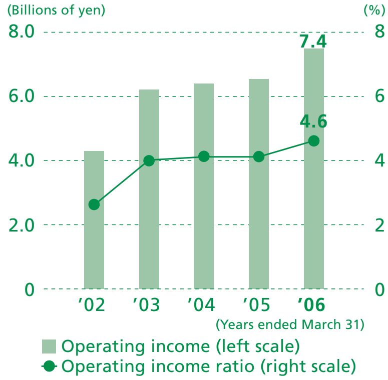
Overseas sales surged 29.2%, or ¥4.6 billion, to ¥20.5 billion. Of this amount, sales of finished products amounted to ¥18.9 billion, up 29.5%, or ¥4.3 billion and sales of parts grew 24.9%, or ¥0.3 billion, to ¥1.6 billion.

Overseas sales in each region expanded. The rise was particularly notable in Europe, where we have enjoyed favorable results since commencing sales of tractors and riding mowers in 2004. Sales in Asia benefited from the commencement of full-fledged sales in China of combine harvesters, and these sales expanded in line with our plans. We also introduced rice transplanters, which boosted sales.

### Domestic

Sales in the Japanese market dipped 0.2%, or ¥0.3 billion, to ¥141.2 billion, with mainstay agricultural equipment sales amounting to ¥74.0 billion, down 0.1% or ¥0.1 billion. In fiscal 2005, the GEAS-AT tractor series contributed substantially to sales of cultivating and mowing machinery, which includes tractors and cultivators, boosting sales ¥2.2 billion. In fiscal 2006, however, sales of these products amounted to ¥31.4 billion, down 1.4% or ¥0.5 billion. Sales of planting machinery (rice transplanters and vegetable transplanters) declined 7.2%, or ¥0.8 billion, to ¥10.7 billion, as mainstay rice transplanters reached the end of their product cycle. Sales of harvesting and processing machinery (including combine harvesters and dryers) grew 3.8%, or ¥1.2 billion, to ¥31.9 billion, helped by higher sales of full-swath cutting combine harvesters.

Operating Income and Operating Income Ratio



In areas of business other than agricultural equipment, sales of parts for maintenance and farming equipment expanded 1.2%, to ¥30.5 billion. For agricultural facilities and other agriculture-related products, sales fell 5.1%, to ¥24.8 billion. Of this amount, construction of agricultural facilities generated ¥5.1 billion, down 25.8%. Sales in other businesses grew 6.4%, to ¥11.9 billion.

## Costs, Expenses and Earnings

Operating income improved 14.5%, or ¥0.9 billion, to ¥7.4 billion. Raw materials costs rose ¥1.3 billion and distribution costs increased causing selling, general and administrative expenses to increase ¥0.5 billion. Higher earnings drove up gross profit ¥1.4 billion, and cost reductions saved ¥1.3 billion, which absorbed the higher costs.

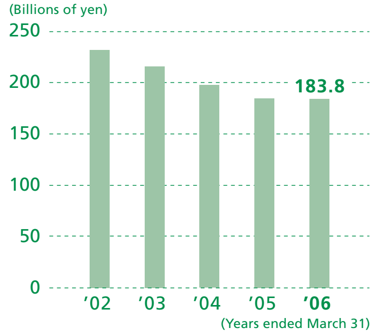
Income before income taxes and minority interests grew 15.2%, or ¥0.8 billion, to ¥5.8 billion. Factors included a ¥0.9 billion rise in operating income and the curtailment of interest-bearing debt, engendering a ¥0.3 billion improvement in the financial balance. Impairment losses on fixed assets were ¥0.5 billion, and the cost of liquidating affiliated companies was ¥0.5 billion. Net income improved 26.7%, or ¥0.8 billion, to ¥3.8 billion, helped by lower corporate, residence and business taxes.

## Financial Condition

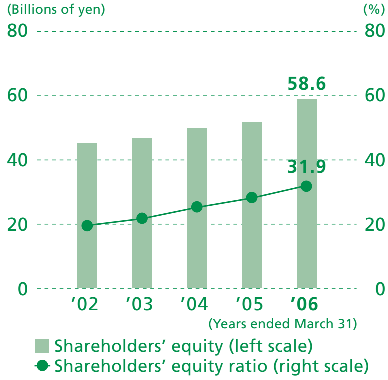
Total assets at the end of the term were ¥183.8 billion, down ¥0.7 billion. The main reason for this decline was a ¥2.3 billion decrease in notes and accounts receivable, triggered by the downturn in facility construction sales.

On the liabilities side, the exercise of stock acquisition rights on bonds reduced bond obligations ¥3.2 billion, and the scheduled paydown of long-term debt caused interest-bearing debt to fall ¥5.6 billion.

Total Assets




Shareholders' Equity and Shareholders' Equity Ratio



The exercise of stock acquisition rights bolstered shareholders' equity ¥3.2 billion, and net income added another ¥3.8 billion. Such contributions caused net shareholders' equity to grow ¥6.9 billion, to ¥58.6 billion, and the shareholders' equity ratio improved to 31.9%.

## Cash Flows

Cash provided by operating activities during the year was ¥4.3 billion, representing a decline of ¥2.0 billion from the preceding term. Income before income taxes and minority interests provided ¥5.8 billion, and the decrease in notes and accounts payable provided ¥3.1 billion.

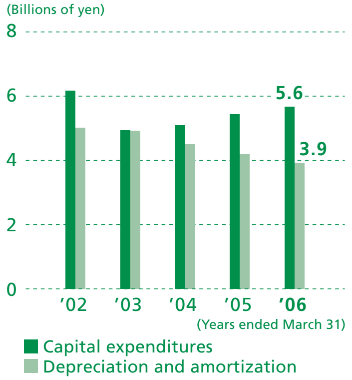
Net cash used in investing activities was ¥2.6 billion. This amount compares with the ¥8.8 billion provided by these activities in fiscal 2005, which was helped by proceeds from the sale of our credit business. Net cash used in financing activities was ¥3.0 billion, ¥15.3 billion less than in the previous term.

## Basic Strategies of the Three-Year Business Plan

Fiscal 2007 is the first year of the Iseki Group's new three-year business plan. Four basic strategies have been established to achieve the plan's targets:

1. Expand overseas sales
2. Achieve a 20% share of the Japanese market for agricultural equipment
3. Further strengthen product competitiveness
4. Improve our consolidated financial structure by raising profitability and cash flow

Capital Expenditures and Depreciation and Amortization



1. Overseas Sales

Market-specific activities to achieve an overseas sales ratio of 15% by fiscal 2009 and 20% by fiscal 2011 are as follows:

- Raise our market share in North America by introducing new products
- In Europe, raise market share by expanding our involvement in landscaping equipment and cultivating new markets and demand for compact agricultural equipment
- In China, introduce products—chiefly such rice-cultivation equipment as combine harvesters and rice transplanters, develop our sales structure and expand sales
- Introduce products that meet the needs of other Asian markets, enhance our sales network in this region and expand sales

2. Domestic Market

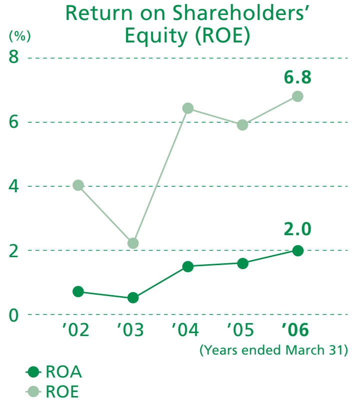
- Strengthen business, targeting operators taking over farms
- Aggressively introduce new products, further increase customer satisfaction by expanding maintenance factories at sales companies and improving services

3. Product Competitiveness

More closely reflect regional needs in Japan and overseas and develop and introduce products with improved competitiveness. Continue efforts outlined in the previous medium-term plan to reduce cost of sales and implement the following:

- Introduce new products for operators taking over farms and compact agricultural equipment for the hobby farming market
- Introduce specialized equipment for overseas
- Reduce costs on new equipment (target: 30% cost reduction)
- Increase overseas procurement

**Return on Assets (ROA) and Return on Shareholders' Equity (ROE)**



4. Consolidated Financial Structure

Strive to strengthen the profitability and cash flow of consolidated subsidiaries, thereby improving the consolidated financial structure. Continue efforts to hold down interest-bearing debt and improve the Group's overall efficiency of cash and other assets.

## Dividends

The Company will position stable and increasing shareholder dividends as a vital management topic. To this end, in addition to improving consolidated financial performance, we will work to enhance the Group's financial structure, expand operations and respond collectively to changes in our operating environment. In line with its basic policy, the Company decided on a year-end per-share dividend of ¥3.00 for fiscal 2006.

## Outlook for Fiscal 2007

In fiscal 2007, we expect the operating environment to become increasingly challenging, with crude oil and raw materials prices remaining high, interest rates rising and the yen continuing to appreciate against other currencies. We also expect increasingly rapid changes in the agricultural environment, with competition growing fiercer. Against this backdrop, the Group will shore up its corporate base to ensure stable earnings.

In fiscal 2007, we anticipate net sales of ¥164.0 billion, up ¥2.3 billion from fiscal 2006. Of this amount, we expect domestic sales to account for ¥143.0 billion, up ¥1.8 billion, and overseas sales for ¥21.0 billion, up ¥0.5 billion.

On the other hand, we forecast a ¥0.9 billion decline in operating income, to ¥6.5 billion, as materials costs continue to rise and foreign exchange rates remain uncertain. We also expect to face higher costs as we invest in the expansion of maintenance facilities at sales companies. Our financial balance, which incorporates the risk of higher interest rates, will remain approximately even, but extraordinary costs should decline. Consequently, we anticipate net income of ¥3.5 billion, down ¥0.2 billion.

In fiscal 2007, we expect to award year-end dividends of ¥3.00 per share, the same as in fiscal 2006.

## Consolidated Balance Sheets

ISEKI & CO., LTD. and Consolidated Subsidiaries
March 31, 2006, 2005 and 2004

| | Millions of yen | | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|---|
| **Assets** | **2006** | 2005 | 2004 | **2006** |
| **Current assets:** | | | | |
| Cash and deposits (Note 4) | **¥ 6,972** | ¥ 8,202 | ¥ 13,466 | **$ 59,351** |
| Marketable securities (Note 6) | **146** | 285 | 277 | **1,243** |
| Notes and accounts receivable | **34,743** | 37,015 | 46,910 | **295,761** |
| Allowance for doubtful accounts | **(126)** | (671) | (757) | **(1,073)** |
| Inventories (Note 7) | **42,486** | 40,852 | 38,921 | **361,675** |
| Deferred income taxes (Note 11) | **1,678** | 2,073 | 1,604 | **14,284** |
| Prepaid expenses and other current assets | **4,011** | 4,113 | 3,819 | **34,146** |
| Total current assets | **89,910** | 91,869 | 104,240 | **765,387** |
| **Property, plant and equipment:** | | | | |
| Land (Notes 8, 9 and 10) | **50,174** | 50,460 | 50,400 | **427,122** |
| Buildings and structures (Notes 8 and 10) | **44,265** | 43,465 | 42,986 | **376,820** |
| Machinery, equipment and vehicles | **42,351** | 42,384 | 43,416 | **360,526** |
| Tools, furniture and fixtures | **25,553** | 25,067 | 25,352 | **217,528** |
| Other | **581** | 563 | 930 | **4,946** |
| Construction in progress | **2,058** | 1,813 | 1,162 | **17,519** |
| Less accumulated depreciation | **(85,963)** | (84,334) | (84,441) | **(731,787)** |
| Property, plant and equipment, net | **79,019** | 79,418 | 79,805 | **672,674** |
| **Investments and other assets:** | | | | |
| Investment securities (Note 6) | **9,165** | 7,967 | 7,624 | **78,020** |
| Investments in an unconsolidated subsidiary and affiliates | **70** | 437 | 75 | **596** |
| Intangible assets | **1,037** | 1,102 | 1,059 | **8,828** |
| Deferred income taxes (Note 11) | **650** | 530 | 477 | **5,533** |
| Others | **4,639** | 4,061 | 4,654 | **39,491** |
| Allowance for doubtful accounts | **(659)** | (907) | (778) | **(5,610)** |
| Total investments and other assets | **14,902** | 13,190 | 13,111 | **126,858** |
| **Total assets** | **¥183,831** | ¥184,477 | ¥197,156 | **$1,564,919** |

See accompanying notes to consolidated financial statements.

| Liabilities, minority interests and shareholders' equity | Millions of yen | | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| **Current liabilities:** | | | | |
| Short-term borrowings (Note 10) | **¥ 19,885** | ¥ 20,306 | ¥ 39,337 | **$ 169,277** |
| Current portion of long-term debt (Note 10) | **18,390** | 7,391 | 10,539 | **156,551** |
| Notes and accounts payable, trade | **41,537** | 44,493 | 39,938 | **353,597** |
| Notes and accounts payable, construction | **388** | 498 | 506 | **3,303** |
| Accrued expenses | **4,408** | 4,622 | 4,064 | **37,524** |
| Accrued income taxes (Note 11) | **1,156** | 1,718 | 1,751 | **9,841** |
| Other current liabilities | **4,073** | 3,575 | 6,061 | **34,673** |
| Total current liabilities | **89,837** | 82,603 | 102,196 | **764,766** |
| **Long-term liabilities:** | | | | |
| Long-term debt (Note 10) | **17,040** | 33,180 | 28,219 | **145,058** |
| Accrued retirement benefits (Note 12) | **5,068** | 4,740 | 5,049 | **43,143** |
| Deferred income taxes (Note 11) | **9,805** | 8,691 | 8,371 | **83,468** |
| Other long-term liabilities | **1,878** | 2,035 | 2,286 | **15,987** |
| Total long-term liabilities | **33,791** | 48,646 | 43,925 | **287,656** |
| Total liabilities | **123,628** | 131,249 | 146,121 | **1,052,422** |
| **Minority interests in consolidated subsidiaries** | **1,558** | 1,502 | 1,459 | **13,263** |
| **Contingent liabilities** (Note 17) | | | | |
| **Shareholders' equity** (Notes 5 and 13)**:** | | | | |
| Common stock: | | | | |
| Authorized—696,037,000 shares | | | | |
| Issued—226,536,329 shares at March 31, 2006; and 225,054,088 shares at March 31, 2005 and 2004 | **22,785** | 22,534 | 22,534 | **193,964** |
| Capital surplus | **12,815** | 11,664 | 11,645 | **109,092** |
| Retained earnings (Note 21) | **9,760** | 6,830 | 4,519 | **83,085** |
| Land revaluation reserve (Note 9) | **10,527** | 10,697 | 10,697 | **89,614** |
| Net unrealized holding gain on securities (Note 6) | **2,896** | 1,956 | 1,584 | **24,653** |
| Foreign currency translation adjustments | **16** | (14) | (8) | **137** |
| | **58,799** | 53,667 | 50,971 | **500,545** |
| Treasury stock, at cost: 666,946 shares in 2006; 8,512,787 shares in 2005; and 6,507,892 shares in 2004 | **(154)** | (1,941) | (1,395) | **(1,311)** |
| Net shareholders' equity | **58,645** | 51,726 | 49,576 | **499,234** |
| **Total liabilities, minority interests and shareholders' equity** | **¥183,831** | ¥184,477 | ¥197,156 | **$1,564,919** |

## Consolidated Statements of Income

ISEKI & CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2006, 2005 and 2004

| | Millions of yen | | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|---|
| | 2006 | 2005 | 2004 | 2006 |
| **Net sales** | ¥161,744 | ¥157,462 | ¥153,624 | $1,376,897 |
| **Cost of sales** (Note 14) | 107,959 | 105,128 | 103,101 | 919,035 |
| Gross profit | 53,785 | 52,334 | 50,523 | 457,862 |
| **Selling, general and administrative expenses** (Note 14) | 46,326 | 45,817 | 44,149 | 394,365 |
| Operating income | 7,459 | 6,517 | 6,374 | 63,497 |
| **Other income (expenses):** | | | | |
| Interest and dividend income | 403 | 332 | 254 | 3,431 |
| Interest expense | (1,000) | (1,277) | (1,621) | (8,513) |
| Gain on sales of investment securities, net (Note 6) | 720 | 311 | 63 | 6,129 |
| Loss on impairment of fixed assets (Notes 3 and 8) | (506) | — | — | (4,307) |
| Gain on sale of credit business | — | 461 | — | — |
| Loss on sales or disposal of property, plant and equipment, net | (225) | (277) | (405) | (1,915) |
| Loss on liquidation of a consolidated subsidiary (Note 15) | (523) | — | — | (4,452) |
| Loss on prior year's adjustment (Note 15) | (178) | — | — | (1,515) |
| Other, net | (322) | (1,008) | (419) | (2,742) |
| Income before income taxes and minority interests | 5,828 | 5,059 | 4,246 | 49,613 |
| **Income taxes** (Note 11)**:** | | | | |
| Current | 1,656 | 2,517 | 2,298 | 14,098 |
| Deferred | 365 | (452) | (1,188) | 3,107 |
| | 2,021 | 2,065 | 1,110 | 17,205 |
| **Income before minority interests** | 3,807 | 2,994 | 3,136 | 32,408 |
| **Minority interests in consolidated subsidiaries** | 50 | 29 | 59 | 425 |
| Net income | ¥ 3,757 | ¥ 2,965 | ¥ 3,077 | $ 31,983 |

See accompanying notes to consolidated financial statements.

# Consolidated Statements of Shareholders' Equity

ISEKI & CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2006, 2005 and 2004

| | Millions of yen | | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|---|
| | 2006 | 2005 | 2004 | 2006 |
| **Common stock:** | | | | |
| Balance at beginning of the year | **¥22,534** | ¥22,534 | ¥22,534 | **$191,828** |
| Issuance of common stock upon the exercise of stock acquisition rights of convertible bonds | **251** | — | — | **2,136** |
| Balance at end of the year | **¥22,785** | ¥22,534 | ¥22,534 | **$193,964** |
| **Capital surplus:** | | | | |
| Balance at beginning of the year | **¥11,664** | ¥11,645 | ¥11,599 | **$ 99,293** |
| Issuance of common stock upon the exercise of stock acquisition rights of convertible bonds | **250** | — | — | **2,128** |
| Gain on disposal of treasury stock | **901** | 19 | 46 | **7,671** |
| Balance at end of the year | **¥12,815** | ¥11,664 | ¥11,645 | **$109,092** |
| **Retained earnings:** | | | | |
| Balance at beginning of the year | **¥ 6,830** | ¥ 4,519 | ¥ 1,442 | **$ 58,143** |
| Net income | **3,757** | 2,965 | 3,077 | **31,983** |
| Transfer to land revaluation reserve | **(177)** | — | — | **(1,507)** |
| Dividends paid | **(650)** | (654) | — | **(5,534)** |
| Balance at end of the year | **¥ 9,760** | ¥ 6,830 | ¥ 4,519 | **$ 83,085** |
| **Land revaluation reserve:** | | | | |
| Balance at beginning of the year | **¥10,697** | ¥10,697 | ¥10,697 | **$ 91,062** |
| Transfer from retained earnings | **177** | — | — | **1,507** |
| Decrease resulting from adjustments to deferred tax assets on land revaluation reserve | **(347)** | — | — | **(2,955)** |
| Balance at the end of the year | **¥10,527** | ¥10,697 | ¥10,697 | **$ 89,614** |
| **Net unrealized holding gain on securities:** | | | | |
| Balance at beginning of the year | **¥ 1,956** | ¥ 1,584 | ¥ 514 | **$ 16,651** |
| Net change | **940** | 372 | 1,070 | **8,002** |
| Balance at end of the year | **¥ 2,896** | ¥ 1,956 | ¥ 1,584 | **$ 24,653** |
| **Foreign currency translation adjustments:** | | | | |
| Balance at beginning of the year | **¥ (14)** | ¥ (8) | ¥ — | **$ (118)** |
| Net change | **30** | (6) | (8) | **255** |
| Balance at end of the year | **¥ 16** | ¥ (14) | ¥ (8) | **$ 137** |

See accompanying notes to consolidated financial statements.

# Consolidated Statements of Cash Flows

ISEKI & CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2006, 2005 and 2004

| | Millions of yen | | | Thousands of U.S. dollars (Note 1) |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| **Cash flows from operating activities:** | | | | |
| Income before income taxes and minority interests | **¥ 5,828** | ¥ 5,059 | ¥ 4,246 | **$ 49,613** |
| Adjustments for: | | | | |
| Depreciation and amortization | **3,910** | 4,167 | 4,483 | **33,285** |
| Loss on impairment of fixed assets | **506** | – | – | **4,307** |
| Gain on sales of investment securities, net | **(699)** | (311) | (63) | **(5,950)** |
| Interest and dividend income | **(403)** | (332) | (254) | **(3,431)** |
| Interest expense | **1,000** | 1,277 | 1,621 | **8,513** |
| Loss on sales or disposal of property, plant and equipment, net | **225** | 277 | 405 | **1,915** |
| Gain on sale of credit business | **—** | (461) | — | **—** |
| Change in operating assets and liabilities: | | | | |
| Decrease (increase) in notes and accounts receivable | **862** | (927) | 310 | **7,338** |
| (Increase) decrease in inventories | **(1,536)** | (1,930) | 896 | **(13,076)** |
| (Decrease) increase in notes and accounts payable, trade | **(3,067)** | 4,555 | 2,517 | **(26,109)** |
| Other, net | **1,379** | (1,476) | 663 | **11,740** |
| Subtotal | **8,005** | 9,898 | 14,824 | **68,145** |
| Interest and dividends received | **404** | 333 | 255 | **3,439** |
| Interest paid | **(1,000)** | (1,300) | (1,772) | **(8,513)** |
| Proceeds from insurance claim | **—** | — | 152 | **—** |
| Income taxes paid | **(3,071)** | (2,581) | (1,090) | **(26,142)** |
| Net cash provided by operating activities | **4,338** | 6,350 | 12,369 | **36,929** |
| **Cash flows from investing activities:** | | | | |
| Purchases of marketable securities | **(4)** | (11) | (35) | **(34)** |
| Proceeds from sales of marketable securities | **283** | 259 | 261 | **2,409** |
| Purchases of property, plant and equipment | **(5,483)** | (5,095) | (5,024) | **(46,676)** |
| Proceeds from sales of property, plant and equipment | **1,646** | 1,292 | 895 | **14,012** |
| Purchases of investment securities | **—** | (589) | (80) | **—** |
| Proceeds from sales of investment securities | **943** | 554 | 106 | **8,028** |
| Decrease in long-term loans receivable included in investments and other assets—other | **17** | 35 | 66 | **145** |
| Decrease in time deposits with maturity more than 3 months | **17** | 2,037 | 8,989 | **145** |
| Proceeds from sale of credit business | **—** | 10,410 | — | **—** |
| Other, net | **(26)** | (134) | 456 | **(222)** |
| Net cash (used in) provided by investing activities | **(2,607)** | 8,758 | 5,634 | **(22,193)** |
| **Cash flows from financing activities:** | | | | |
| Decrease in short-term borrowings | **(471)** | (18,971) | (33,179) | **(4,010)** |
| Proceeds from long-term loans | **4,966** | 4,036 | 26,690 | **42,275** |
| Repayment of long-term loans | **(7,861)** | (12,244) | (11,399) | **(66,919)** |
| Proceeds from bonds issued | **1,000** | 10,000 | 420 | **8,513** |
| Redemption of bonds | **(40)** | (40) | (8,000) | **(341)** |
| Purchases of treasury stock | **(46)** | (563) | (1,235) | **(392)** |
| Proceeds from sales of treasury stock | **56** | 49 | 66 | **477** |
| Dividends paid | **(650)** | (654) | — | **(5,534)** |
| Other, net | **(3)** | (4) | (3) | **(25)** |
| Net cash used in financing activities | **(3,049)** | (18,391) | (26,640) | **(25,956)** |
| **Effect of exchange rate changes on cash and cash equivalents** | **(43)** | 56 | 102 | **(366)** |
| **Net decrease in cash and cash equivalents** | **(1,361)** | (3,227) | (8,535) | **(11,586)** |
| **Cash and cash equivalents at beginning of year** | **7,803** | 11,030 | 19,565 | **66,425** |
| **Increase in cash and cash equivalents resulting from merger** | **148** | — | — | **1,260** |
| **Cash and cash equivalents at end of year** (Notes 4 and 5) | **¥ 6,590** | ¥ 7,803 | ¥ 11,030 | **$ 56,099** |

See accompanying notes to consolidated financial statements.

# Notes to Consolidated Financial Statements

ISEKI & CO., LTD. and Consolidated Subsidiaries
March 31, 2006

## 1. Basis of Presentation

ISEKI & CO., LTD. (the "Company") and its domestic subsidiaries maintain their accounts and records in accordance with accounting principles generally accepted in Japan. The Company's overseas subsidiary maintains its accounts and records in conformity with accounting principles generally accepted in its respective country of domicile.

The accompanying consolidated financial statements of the Company and its consolidated subsidiaries are prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and have been compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan.

The translation of yen amounts into U.S. dollar amounts is included solely for the convenience of readers outside Japan and has been made at ¥117.47=U.S.$1.00, the exchange rate prevailing on March 31, 2006. This translation should not be construed as a representation that yen have been, could have been, or could in the future be, converted into U.S. dollars at the above or any other rate.

## 2. Summary of Significant Accounting Policies

### (a) Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Company and all significant companies which it controls directly or indirectly. The assets and liabilities of the initially consolidated subsidiaries are stated at fair value by the full value method as of their respective dates of acquisition of control.

The fiscal year-end of certain consolidated subsidiaries is December 31. If necessary, adjustments are made to reflect any significant differences in intercompany accounts arising from intervening intercompany transactions during the period from January 1 through March 31.

The differences between the cost and the underlying equity in net assets at the dates of acquisition of the consolidated subsidiaries are amortized by the straight-line method over a period of 20 years or less.

### (b) Foreign currency translation

Foreign currency amounts are translated into yen at the rates of exchange in effect at the balance sheet date for monetary assets and liabilities, and at their historical rates for other assets and liabilities. All revenues and expenses associated with foreign currencies are translated at the rates of exchange prevailing when such transactions were made. Gain or loss resulting from the translation of foreign currency transactions is credited or charged to income as incurred.

Revenue and expense accounts of the overseas consolidated subsidiary and its balance sheet accounts (except for shareholders' equity) are translated into yen at the rates of exchange in effect at the balance sheet date. The components of shareholders' equity are translated at their respective historical exchange rates. The Company has presented foreign currency translation adjustments as a component of shareholders' equity and minority interests in consolidated subsidiaries in the accompanying consolidated financial statements.

### (c) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, deposits with banks withdrawable on demand, and short-term investments which are readily convertible into cash subject to an insignificant risk of any change in their value and which were purchased with an original maturity of three months or less.

### (d) Marketable securities and investment securities

Securities are classified into three categories: trading, held-to-maturity or other securities. Trading securities are carried at fair value and held-to-maturity debt securities are carried at amortized cost. Marketable securities classified as other securities are carried at fair value with any changes in unrealized holding gain or loss, net of the applicable income taxes, included directly in shareholders' equity. Cost of securities sold is determined principally by the moving average method. Non-marketable securities classified as other securities are carried at cost principally by the moving average method.

### (e) Derivative financial instruments and hedging activities

Derivatives are stated at fair value with any changes in fair value being charged or credited to income for the period in which they arise, except for derivatives which meet the criteria for deferral hedge accounting under which unrealized gain or loss is deferred as an asset or a liability. Receivables and payables hedged by forward foreign exchange contracts which meet certain conditions are translated at the corresponding foreign exchange contract rates.

### (f) Allowance for doubtful accounts

The Company and its consolidated subsidiaries provide an allowance for doubtful accounts at the estimated aggregate amount of probable bad debts plus an amount calculated at a rate based on their historical experience.

### (g) Inventories

Inventories are principally stated at the lower of cost determined by the average method, or market.

### (h) Property, plant and equipment

Depreciation is computed principally by the declining-balance method over the estimated useful lives of the respective assets, except for tools and buildings (other than structures attached to the buildings) acquired on or after April 1, 1998, which are depreciated by the straight-line method over their respective useful lives.

The principal estimated useful lives are as follows:

| | |
|---|---|
| Buildings and structures | 3 to 50 years |
| Machinery, equipment and vehicles | 2 to 17 years |
| Tools, furniture and fixtures | 2 to 20 years |

Depreciation of minor tangible assets whose acquisition costs were ¥100 thousand or more, but less than ¥200 thousand, are computed principally by the straight-line method over 3 years.

### (i) Intangible assets

Amortization is calculated by the straight-line method over the useful lives of the respective assets.

Costs incurred for computer software developed or obtained for internal use are capitalized and amortized on a straight-line basis over an estimated useful life of 5 years. Costs incurred for computer software used for marketing are also capitalized and amortized on a straight-line basis over their estimated marketable period of 3 years.

### (j) Bond issuance expenses

Bond issuance expenses are charged to income as incurred.

### (k) Leases

Finance leases other than those which transfer the ownership of the leased property to the lessee are accounted for as operating leases.

### (l) Income taxes

Deferred income taxes are recognized by the liability method. Under this method, deferred tax assets and liabilities are determined based on the differences between financial reporting and the tax bases of the assets and liabilities and are measured using the enacted tax rates and laws which will be in effect when the differences are expected to reverse.

### (m) Accrued retirement benefits

Accrued retirement benefits for employees have been provided principally at an amount calculated based on the retirement benefit obligation and the fair value of the pension plan assets, as adjusted for net unrecognized actuarial gain or loss and unrecognized prior service cost. The retirement benefit obligation is attributed to each period by the straight-line method over the estimated years of service of the eligible employees.

The net retirement benefit obligation at transition is being amortized over a period of 15 years by the straight-line method. Prior service cost is amortized as incurred primarily by the straight-line method over 10 to 13 years, the estimated average remaining years of service of the eligible employees. Actuarial gain or loss is amortized commencing the year following the year in which the gain or loss is recognized primarily by the straight-line method over 10 to 13 years, the estimated average remaining years of service of the eligible employees.

Certain domestic consolidated subsidiaries, upon the enactment of the Defined Contribution Pension Plan Law, converted their tax-qualified pension plans and lump-sum payment plans to defined contribution plans effective April 2004, and adopted a new accounting standard governing the transition between the retirement benefit plans. The effect of this change was that a loss of ¥20 million was recorded and included in “Other income (expenses)—Other, net” in the consolidated statement of income for the year ended March 31, 2005.

Subject to approval at a shareholders’ meeting, the directors and corporate auditors of the Company and certain domestic consolidated subsidiaries are entitled to lump-sum payments under unfunded retirement benefit plans. The provision for retirement benefits for directors and corporate auditors has been made at estimated amounts based on the Company’s internal regulations.

### (n) Revenue on installment sales

A domestic consolidated subsidiary handles the installment sales business. The unrealized profit on installment sales corresponding to the portion of installment receivables due in subsequent years is deferred and is recorded as a component of “Other current liabilities” in the accompanying consolidated balance sheets.

### (o) Appropriation of retained earnings

Under the Commercial Code of Japan, the appropriation of retained earnings with respect to a given financial period is made by resolution of the shareholders at a general meeting held subsequent to the close of the financial period. The accounts for that period do not reflect such appropriations. (Refer to Note 21.)

## 3. Change in Method of Accounting

Effective the year ended March 31, 2006, the Company and its domestic subsidiaries have adopted a new accounting standard for the impairment of fixed assets which requires that tangible and intangible fixed assets be carried at cost less depreciation, and be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Companies are required to recognize an impairment loss in their statement of income if certain indicators of asset impairment exist and the book value of an asset exceeds the undiscounted sum of its future cash flows. The standard states that impairment losses should be measured as the excess of the book value over the higher of (1) the fair market value of the asset, net of disposition costs, and (2) the present value of future cash flows arising from ongoing utilization of the asset and from its disposal after use. The standard covers land, factories, buildings and other forms of property, plant and equipment as well as intangible assets. Fixed assets are to be grouped at the lowest level for which there are identifiable cash flows which are independent of the cash flows from other groups of assets.

As a result of the adoption of this new accounting standard, a loss on impairment of fixed assets in the amount of ¥506 million ($4,307 thousand) was recognized and income before income taxes and minority interests decreased by the same amount for the year ended March 31, 2006, as compared with the corresponding amount under the previous method.

The accumulated impairment loss on such assets has been deducted directly from the carrying amounts of the respective assets in the consolidated balance sheet at March 31, 2006.

### 4. Cash and Cash Equivalents

A reconciliation of cash and deposits in the consolidated balance sheets and cash and cash equivalents in the consolidated statements of cash flows at March 31, 2006, 2005 and 2004 is as follows:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Cash and deposits | **¥6,972** | ¥8,202 | ¥13,466 | **$59,351** |
| Less: time deposits with original maturities exceeding three months | **(382)** | (399) | (2,436) | **(3,252)** |
| Cash and cash equivalents | **¥6,590** | ¥7,803 | ¥11,030 | **$56,099** |

### 5. Supplemental Cash Flow Information

Significant noncash transactions for the year ended March 31, 2006 are summarized as follows:

| | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| Exercise of stock acquisition rights of convertible bonds: | | |
| Increase in common stock | ¥ 251 | $ 2,136 |
| Increase in capital surplus | 250 | 2,128 |
| Gain on disposal of treasury stock | 871 | 7,415 |
| Decrease in treasury stock | 1,833 | 15,605 |
| Decrease in convertible bonds | ¥3,205 | $27,284 |

### 6. Securities

(a) Information regarding marketable securities classified as held-to-maturity debt securities at March 31, 2006, 2005 and 2004 is summarized as follows:

| | Millions of yen | | | Thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | **2006** | | | **2006** | | |
| | Carrying value | Fair value | Unrealized gain (loss) | Carrying value | Fair value | Unrealized gain (loss) |
| Securities whose fair value exceeds their carrying value | **¥ —** | **¥ —** | **¥—** | **$ —** | **$ —** | **$—** |
| Securities whose fair value does not exceed their carrying value | **390** | **386** | **4** | **3,320** | **3,286** | **34** |
| Total | **¥390** | **¥386** | **¥ 4** | **$3,320** | **$3,286** | **$34** |

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | |
| | Carrying value | Fair value | Unrealized gain (loss) | Carrying value | Fair value | Unrealized gain (loss) |
| Securities whose fair value exceeds their carrying value | ¥635 | ¥637 | ¥ 2 | ¥455 | ¥458 | ¥ 3 |
| Securities whose fair value does not exceed their carrying value | 30 | 30 | (0) | 190 | 189 | (1) |
| Total | ¥665 | ¥667 | ¥ 2 | ¥645 | ¥647 | ¥ 2 |

(b) Information regarding marketable securities classified as other securities at March 31, 2006, 2005 and 2004 is summarized as follows:

| | Millions of yen | | | Thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | **2006** | | | **2006** | | |
| | Acquisition costs | Carrying value | Unrealized gain (loss) | Acquisition costs | Carrying value | Unrealized gain (loss) |
| Securities whose carrying value exceeds their acquisition costs: | | | | | | |
| Equity securities | **¥2,716** | **¥7,570** | **¥4,854** | **$23,120** | **$64,442** | **$41,322** |
| Other | **—** | **—** | **—** | **—** | **—** | **—** |
| Subtotal | **2,716** | **7,570** | **4,854** | **23,120** | **64,442** | **41,322** |
| Securities whose carrying value does not exceed their acquisition costs: | | | | | | |
| Equity securities | **16** | **13** | **(3)** | **137** | **111** | **(26)** |
| Subtotal | **16** | **13** | **(3)** | **137** | **111** | **(26)** |
| Total | **¥2,732** | **¥7,583** | **¥4,851** | **$23,257** | **$64,553** | **$41,296** |

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | |
| | Acquisition costs | Carrying value | Unrealized gain (loss) | Acquisition costs | Carrying value | Unrealized gain (loss) |
| Securities whose carrying value exceeds their acquisition costs: | | | | | | |
| Equity securities | ¥2,937 | ¥6,209 | ¥3,272 | ¥3,058 | ¥5,719 | ¥2,661 |
| Other | 0 | 1 | 1 | 2 | 2 | 0 |
| Subtotal | 2,937 | 6,210 | 3,273 | 3,060 | 5,721 | 2,661 |
| Securities whose carrying value does not exceed their acquisition costs: | | | | | | |
| Equity securities | 18 | 13 | (5) | 118 | 101 | (17) |
| Subtotal | 18 | 13 | (5) | 118 | 101 | (17) |
| Total | ¥2,955 | ¥6,223 | ¥3,268 | ¥3,178 | ¥5,822 | ¥2,644 |

**(c)** Sales of securities classified as other securities for the years ended March 31, 2006, 2005 and 2004 were as follows:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Carrying value of other securities sold | **¥945** | ¥550 | ¥104 | **$8,045** |
| Gain on sales | **720** | 311 | 63 | **6,129** |

**(d)** The carrying value of held-to-maturity debt securities and other securities with no determinable fair value at March 31, 2006, 2005 and 2004 is summarized as follows:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Held-to-maturity debt securities: | | | | |
| Discounted financial bonds | **¥ 6** | ¥ 10 | ¥ 56 | **$ 51** |
| Other securities: | | | | |
| Unlisted equity securities | **1,332** | 1,354 | 1,378 | **11,339** |

**(e)** The redemption schedule for securities with maturity dates classified as other securities and held-to-maturity debt securities at March 31, 2006 is summarized as follows:

| | Millions of yen | | |
|---|---|---|---|
| | Due in one year or less | Due after one year through five years | Due after five years through ten years |
| Other debt securities | ¥146 | ¥250 | ¥— |
| Total | ¥146 | ¥250 | ¥— |

| | Thousands of U.S. dollars | | |
|---|---|---|---|
| | Due in one year or less | Due after one year through five years | Due after five years through ten years |
| Other debt securities | $1,243 | $2,128 | $— |
| Total | $1,243 | $2,128 | $— |

## 7. Inventories

Inventories at March 31, 2006, 2005 and 2004 consisted of the following:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Finished goods and merchandise | **¥34,939** | ¥34,140 | ¥33,175 | **$297,428** |
| Semifinished goods | **60** | 50 | 52 | **511** |
| Work in process | **6,429** | 5,659 | 4,614 | **54,729** |
| Raw materials and supplies | **1,058** | 1,003 | 1,080 | **9,007** |
| Total | **¥42,486** | ¥40,852 | ¥38,921 | **$361,675** |

## 8. Loss on Impairment of Fixed Assets

Loss on impairment of fixed assets of ¥506 million ($4,307 thousand) was recorded for the year ended March 31, 2006, related to buildings and structures of ¥48 million ($409 thousand) and land of ¥458 million ($3,898 thousand), which are outlined as follows:

| Use | Classification | Location | Millions of yen 2006 | Thousands of U.S. dollars 2006 |
|---|---|---|---|---|
| Idle property | Land | Inashiki Gun, Ibaraki Prefecture | ¥222 | $1,890 |
| Idle property | Land | Kirishima City, Kaogoshima Prefecture | 78 | 664 |
| Idle property | Land and buildings | Kuma Gun, Kumamoto Prefecture | 57 | 485 |
| Idle property | Land | Sasayama City, Hyogo Prefecture | 39 | 332 |
| Idle property | Buildings | Matsuyama City, Ehime Prefecture | 33 | 281 |
| Idle property | Land | Kasumigaura City, Ibaraki Prefecture | 23 | 196 |
| Idle property | Land and structures | Kamiminochi Gun, Nagano Prefecture | 18 | 153 |
| Idle property | Land, buildings and structures | Sapporo City, Hokkaido Prefecture and other areas (8 items) | 36 | 306 |
| | | Total | ¥506 | $4,307 |

Loss on impairment of fixed assets was recorded as the assets and asset groups listed above remain unused, there is no expectation of future utilization, and the market value of the land declined.

The Company and its consolidated subsidiaries group their fixed assets as each unit which manages receipts and payments independently. They also group idle properties and properties loaned out at each asset.

The recoverable amounts of such assets and asset groups are measured at their estimated selling value. An estimate of the selling value of the impaired land is a reasonable reflection of its value as assessed for property tax purposes.

## 9. Land Revaluation

Effective March 31, 2001, the Company revalued its land held for business use in accordance with the "Law on Land Revaluation." Differences on land revaluation have been accounted for as land revaluation reserve under shareholders' equity at the net amount of the relevant tax effect. The method followed in determining the land revaluation was in accordance with the "Enforcement Act Concerning Land Revaluation." The carrying value of this land exceeded its corresponding fair value by ¥8,245 million ($70,188 thousand), ¥6,082 million and ¥4,560 million at March 31, 2006, 2005 and 2004, respectively.

## 10. Short-term Borrowings and Long-term Debt

Short-term borrowings principally represent short-term notes, short-term bank borrowings on deeds, and bank overdrafts at average interest rates of 1.28%, 1.45% and 1.54% at March 31, 2006, 2005 and 2004, respectively.

The Company has concluded line-of-credit agreements with certain banks to reduce its interest-bearing debt, to achieve efficient financing, and to improve its financial cash flows. The status of these lines of credit at March 31, 2006 is summarized as follows:

| | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| Lines of credit | ¥25,000 | $212,820 |
| Short-term borrowings | 1,300 | 11,066 |
| Available credit | ¥23,700 | $201,754 |

Long-term debt at March 31, 2006, 2005 and 2004 consisted of the following:

| | Millions of yen 2006 | 2005 | 2004 | Thousands of U.S. dollars 2006 |
|---|---|---|---|---|
| Zero coupon yen convertible bonds | **¥ 6,795** | ¥10,000 | ¥ — | **$ 57,844** |
| 0.31% unsecured bonds due 2010 | **1,000** | — | — | **8,513** |
| 0.87% unsecured bonds due 2007 | **100** | 100 | 100 | **851** |
| 0.45% unsecured bonds due 2006 | **60** | 60 | 60 | **511** |
| 0.57% unsecured bonds due 2008 | **60** | 60 | 60 | **511** |
| 0.67% unsecured bonds due 2010 | **220** | 260 | 300 | **1,873** |
| Loans principally from banks and insurance companies due through 2023 at an average interest rate of 1.57% | **27,195** | 30,091 | 38,238 | **231,506** |
| | **35,430** | 40,571 | 38,758 | **301,609** |
| Less: current portion | **(18,390)** | (7,391) | (10,539) | **(156,551)** |
| | **¥ 17,040** | ¥33,180 | ¥ 28,219 | **$ 145,058** |

On October 5, 2004, the Company issued ¥10 billion of zero coupon yen convertible bonds with stock acquisition rights. An outline of these bonds is as follows:

| | |
|---|---|
| Type of shares to which acquisition rights apply | Common stock of the Company |
| Issue price of stock acquisition rights | Nil |
| Exercise price of stock acquisition rights | ¥338 |
| Principal of bonds | ¥10 billion |
| Payment to be made upon exercise of stock acquisition rights | 100% of the amount paid for each bond |
| Exercise period | October 19, 2004 to September 21, 2009 |

Exercise of the stock acquisition rights shall be deemed as payment by the bondholder of the full amount required to be paid upon exercise of the stock acquisition rights, rather than as a redemption of the bond at its principal amount.

At March 31, 2006, assets pledged as collateral for short-term borrowings of ¥5,925 million ($50,438 thousand) and long-term debt of ¥4,165 million ($35,456 thousand) including the current portion of ¥2,720 million ($23,155 thousand) were as follows:

| | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| Property, plant and equipment: | | |
| Land | ¥ 9,450 | $ 80,446 |
| Buildings and structures | 3,141 | 26,739 |
| | ¥12,591 | $107,185 |

The aggregate annual maturities of long-term debt subsequent to March 31, 2006 are summarized as follows:

| Year ending March 31 | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| 2007 | ¥18,390 | $156,551 |
| 2008 | 3,759 | 31,999 |
| 2009 | 3,159 | 26,892 |
| 2010 | 8,022 | 68,290 |
| 2011 | 1,816 | 15,459 |
| 2012 and thereafter | 284 | 2,426 |
| Total | ¥35,430 | $301,609 |

## 11. Income Taxes

Income taxes applicable to the Company and its domestic consolidated subsidiaries comprise corporate tax, inhabitants' taxes and enterprise tax which, in the aggregate, resulted in statutory tax rates of 40.0% for the years ended March 31, 2006 and 2005, and 42% for the year ended March 31, 2004. Overseas subsidiaries are subject to the income taxes of the countries in which they operate.

The effective tax rates for the years ended March 31, 2006 and 2004 differ from the statutory tax rates for the following reasons:

| | **2006** | 2004 |
|---|---|---|
| Statutory tax rates | 40.0% | 42.0% |
| Permanently non-deductible expenses | 2.0 | 3.0 |
| Per capita portion of inhabitants' taxes | 2.5 | 3.2 |
| Changes in valuation allowance for deferred tax assets | (12.3) | (23.1) |
| Other | 2.5 | 1.0 |
| Effective tax rates | 34.7% | 26.1% |

Reconciliation of the statutory tax rate to the effective tax rate for the year ended March 31, 2005 was not presented, since the difference was less than five percent of the statutory tax rate.

The tax effects of temporary differences which gave rise to a significant portion of the deferred tax assets and liabilities at March 31, 2006, 2005 and 2004 are presented below:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Deferred tax assets: | | | | |
| Accrued retirement benefits | **¥ 989** | ¥ 697 | ¥ 667 | **$ 8,419** |
| Accrued bonuses for employees | **516** | 507 | 425 | **4,393** |
| Unrealized gain on sales of inventories and property, plant and equipment | **355** | 1,196 | 926 | **3,022** |
| Tax loss carryforwards | **672** | — | — | **5,721** |
| Other | **273** | 225 | 168 | **2,323** |
| Offset against deferred tax liabilities | **(477)** | (22) | (105) | **(4,061)** |
| Net deferred tax assets | **¥2,328** | ¥2,603 | ¥2,081 | **$19,817** |
| Deferred tax liabilities: | | | | |
| Reserve for deferred taxation on compensation for expropriation or exchange of property | **¥ 188** | ¥ 176 | ¥ 188 | **$ 1,600** |
| Unrealized holding gain on securities | **1,940** | 1,307 | 1,058 | **16,515** |
| Land revaluation reserve | **7,595** | 7,131 | 7,131 | **64,655** |
| Prepaid pension cost | **270** | — | — | **2,298** |
| Other | **289** | 99 | 99 | **2,461** |
| Offset against deferred tax assets | **(477)** | (22) | (105) | **(4,061)** |
| Net deferred tax liabilities | **¥9,805** | ¥8,691 | ¥8,371 | **$83,468** |

## 12. Accrued Retirement Benefits

The Company and certain domestic consolidated subsidiaries have defined benefit plans, i.e., tax-qualified pension plans and lump-sum payment plans, covering substantially all employees who are entitled to lump-sum or annuity payments, the amounts of which are determined by reference to their basic rates of pay, length of service, and the conditions under which termination occurs. In addition to the retirement benefit plans described above, the Company and certain domestic consolidated subsidiaries pay additional retirement benefits under certain conditions. During the year ended March 31, 2005, certain domestic consolidated subsidiaries converted their tax-qualified pension plans and lump-sum payment plans to defined contribution plans.

The following table sets forth the funded and accrued status of the plans, and the amounts recognized in the consolidated balance sheets at March 31, 2006, 2005 and 2004, for the defined benefit plans of the Company and the consolidated subsidiaries:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Retirement benefit obligation | **¥(30,317)** | ¥(29,927) | ¥(30,446) | **$(258,083)** |
| Plan assets at fair value | **12,109** | 8,725 | 7,112 | **103,082** |
| Unfunded retirement benefit obligation | **(18,208)** | (21,202) | (23,334) | **(155,001)** |
| Unrecognized benefit obligation at transition | **13,144** | 14,604 | 16,085 | **111,892** |
| Unrecognized actuarial loss | **1,462** | 2,914 | 3,306 | **12,446** |
| Unrecognized prior service cost | **(528)** | (627) | (725) | **(4,495)** |
| Net retirement benefit obligation | **(4,130)** | (4,311) | (4,668) | **(35,158)** |
| Prepaid pension cost | **679** | 203 | 154 | **5,780** |
| Accrued retirement benefits | **¥ (4,809)** | ¥ (4,514) | ¥ (4,822) | **$ (40,938)** |

The components of retirement benefit expenses for the years ended March 31, 2006, 2005 and 2004 are outlined as follows:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Service cost | **¥1,296** | ¥1,397 | ¥1,403 | **$11,033** |
| Interest cost | **499** | 507 | 633 | **4,248** |
| Expected return on plan assets | **(133)** | (100) | (105) | **(1,132)** |
| Amortization: | | | | |
| Net retirement benefit obligation at transition | **1,460** | 1,461 | 1,462 | **12,429** |
| Actuarial loss | **326** | 331 | 277 | **2,775** |
| Prior service cost | **(98)** | (98) | (98) | **(834)** |
| Other | **52** | 45 | 56 | **442** |
| Retirement benefit expenses | **3,402** | 3,543 | 3,628 | **28,961** |
| Additional retirement benefits | **—** | 4 | 12 | **—** |
| Gain on conversion of pension plans | **—** | 20 | — | **—** |
| Total | **¥3,402** | ¥3,567 | ¥3,640 | **$28,961** |

As permitted under the accounting standard for retirement benefits, certain domestic consolidated subsidiaries calculate accrued retirement benefits for their employees by simplified methods. The related retirement benefit expenses for these subsidiaries are included in service cost presented in the above table.

The effect of the conversion of the defined benefit plans to defined contribution plans during the year ended March 31, 2005 is summarized as follows:

| | Millions of yen |
|---|---|
| Reduction of benefit obligation | ¥142 |
| Reduction of pension plan assets | (94) |
| Net retirement benefit obligation at transition | (20) |
| Decrease in accrued retirement benefits | ¥ 28 |

The assumptions used in accounting for the defined benefit plans for the years ended March 31, 2006, 2005 and 2004 are summarized as follows:

| | **2006** | 2005 | 2004 |
|---|---|---|---|
| Discount rate | **2.0%** | 2.0% | 2.0% |
| Expected rates of return on plan assets | **2.0%** | 2.0% | 2.5% |

Accrued retirement benefits in the accompanying consolidated balance sheets include accrued retirement benefits for directors and statutory auditors of the Company and certain of the Company's domestic consolidated subsidiaries of ¥259 million ($2,205 thousand), ¥226 million and ¥227 million at March 31, 2006, 2005 and 2004, respectively.

## 13. Shareholders' Equity

The Commercial Code of Japan (the "Code") provides that an amount equivalent to at least 10% of cash dividends paid and bonuses to directors and corporate auditors, and exactly 10% of interim cash dividends paid be appropriated to the legal reserve until the sum of additional paid-in capital and the legal reserve equals 25% of stated capital. The Code also provides that additional paid-in capital and the legal reserve are not available for dividends, but may be used to reduce a capital deficit by resolution of the shareholders or may be capitalized by resolution of the Board of Directors. The Code also stipulates that, to the extent that the sum of the additional paid-in capital account and the legal reserve exceeds 25% of the common stock account, the amount of any such excess is available for appropriation by resolution of the shareholders. Additional paid-in capital and the legal reserve are included in capital surplus and retained earnings, respectively, in the accompanying consolidated balance sheets and statements of shareholders' equity. The legal reserve of the Company was nil at March 31, 2006, 2005 and 2004.

The new Corporation Law of Japan (the "Law"), which superseded most of the provisions of the Code, went into effect on May 1, 2006. The Law stipulates requirements on distribution of earnings similar to those of the Code. Under the Law, however, such distributions can be made at any time by resolution of the shareholders, or by the Board of Directors if certain conditions are met.

**14. Research and Development Costs**

Research and development costs included in manufacturing costs and selling, general and administrative expenses amounted to ¥4,209 million ($35,830 thousand), ¥3,939 million and ¥3,822 million for the years ended March 31, 2006, 2005 and 2004, respectively.

**15. Other Income (Expense)**

Loss on liquidation of a consolidated subsidiary presented in the consolidated statement of income for the year ended March 31, 2006 represented loss resulting from the liquidation of AIEFU & CO., LTD.

Loss on prior year's adjustment presented in the consolidated statement of income for the year ended March 31, 2006, represented an adjustment to the carrying value of certain assets owned by a consolidated subsidiary.

**16. Leases**

The following pro forma amounts represent the acquisition costs, accumulated depreciation and net book value of the leased assets at March 31, 2006, 2005 and 2004, which would have been reflected in the consolidated balance sheets if finance lease accounting had been applied to the finance leases currently accounted for as operating leases:

| | Millions of yen | | | Thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | **2006** | | | **2006** | | |
| | Acquisition costs | Accumulated depreciation | Net book value | Acquisition costs | Accumulated depreciation | Net book value |
| Buildings and structures | **¥ 36** | **¥ 23** | **¥ 13** | **$ 306** | **$ 196** | **$ 110** |
| Machinery, equipment and vehicles | **3,004** | **1,167** | **1,837** | **25,573** | **9,935** | **15,638** |
| Tools, furniture and fixtures | **4,890** | **2,916** | **1,974** | **41,628** | **24,823** | **16,805** |
| | **¥7,930** | **¥4,106** | **¥3,824** | **$67,507** | **$34,954** | **$32,553** |

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | |
| | Acquisition costs | Accumulated depreciation | Net book value | Acquisition costs | Accumulated depreciation | Net book value |
| Buildings and structures | ¥ 36 | ¥ 18 | ¥ 18 | ¥ 36 | ¥ 13 | ¥ 23 |
| Machinery, equipment and vehicles | 2,565 | 1,084 | 1,481 | 2,185 | 1,078 | 1,107 |
| Tools, furniture and fixtures | 4,713 | 2,456 | 2,257 | 3,706 | 1,753 | 1,953 |
| | ¥7,314 | ¥3,558 | ¥3,756 | ¥5,927 | ¥2,844 | ¥3,083 |

Lease payments relating to finance leases accounted for as operating leases for the years ended March 31, 2006, 2005 and 2004, and the corresponding depreciation and interest expense computed by the straight-line method and the interest method, respectively, are summarized as follows:

| | Millions of yen | | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Lease payments | **¥1,609** | ¥1,441 | ¥1,275 | **$13,697** |
| Depreciation | **1,481** | 1,324 | 1,169 | **12,607** |
| Interest expense | **135** | 124 | 113 | **1,149** |

Future minimum lease payments subsequent to March 31, 2006, for finance leases accounted for as operating leases are summarized as follows:

| Year ending March 31 | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| 2007 | ¥1,284 | $10,931 |
| 2008 and thereafter | 2,639 | 22,465 |
| Total | ¥3,923 | $33,396 |

Future minimum lease payments subsequent to March 31, 2006, for non-cancelable operating leases were as follows:

| Year ending March 31 | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| 2007 | ¥142 | $1,209 |
| 2008 and thereafter | 249 | 2,120 |
| Total | ¥391 | $3,329 |

**17. Contingent Liabilities**

The contingent liabilities of the Company and its consolidated subsidiaries at March 31, 2006 were as follows:

| Year ending March 31 | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| Guarantees of bank loans of others | ¥9,930 | $84,532 |
| Notes receivable discounted with banks | 95 | 809 |
| Notes receivable endorsed | 643 | 5,474 |

## 18. Derivatives

The Company and certain consolidated subsidiaries utilize derivative financial instruments to reduce foreign exchange rate and interest-rate risk, and manage them efficiently. The Company and certain consolidated subsidiaries utilize forward foreign exchange contracts to hedge the risk of fluctuation of foreign currency assets and liabilities in the course of their import and export operations. In addition, the Company and certain consolidated subsidiaries utilize interest-rate swaps to hedge the risk of fluctuation in interest rates on their borrowings. The Company and these consolidated subsidiaries do not enter into derivatives contracts for speculative or short-term trading purposes.

The Company and certain consolidated subsidiaries are exposed to certain market risk arising from their forward foreign exchange contracts and interest-rate swap agreements. They are also exposed to the risk of credit loss in the event of nonperformance by the counterparties with respect to forward foreign exchange contracts or interest-rate swap agreements; however, the Company and these subsidiaries do not anticipate nonperformance by any of the counterparties, all of whom are financial institutions with high credit ratings. In addition, the Company and these subsidiaries have established internal policies which include procedures and authorization processes governing derivatives and comply fully with these guidelines.

## 19. Amounts per Share

Amounts per share at March 31, 2006, 2005 and 2004, and for the years then ended were as follows:

| | Yen | | | U.S. dollars |
|---|---|---|---|---|
| | **2006** | 2005 | 2004 | **2006** |
| Net income: | | | | |
| Basic | **¥ 17.23** | ¥ 13.61 | ¥ 13.90 | **$0.15** |
| Diluted | **15.27** | 12.74 | — | **0.13** |
| Cash dividends applicable to the year | **3.00** | 3.00 | 3.00 | **0.03** |
| Net assets | **259.64** | 238.88 | 226.85 | **2.21** |

Diluted net income per share for the year ended March 31, 2004 has not been presented because there were no potentially dilutive shares at March 31, 2004.

## 20. Segment Information

### (1) Business segment information

As the percentage of manufacturing and sales of agricultural machinery exceeded 90% of total assets, sales and operating income at March 31, 2006, 2005 and 2004, and for the years then ended, the disclosure of business segment information has been omitted.

### (2) Geographical segment information

As sales and assets of the Company and the consolidated domestic subsidiaries exceeded 90% of consolidated total assets and sales at March 31, 2006, 2005 and 2004, and for the years then ended, the disclosure of geographical segment information has been omitted.

### (3) Overseas sales information

Overseas sales for the years ended March 31, 2006 and 2005 were as follows:

| | Millions of yen | | | | Thousands of U.S. dollars | | | |
|---|---|---|---|---|---|---|---|---|
| | **2006** | | | | **2006** | | | |
| | United States | Europe | Other | Total | United States | Europe | Other | Total |
| Overseas sales | **¥9,072** | **¥8,674** | **¥2,767** | **¥ 20,513** | **$77,228** | **$73,840** | **$23,555** | **$ 174,623** |
| Consolidated net sales | **—** | **—** | **—** | **161,744** | **—** | **—** | **—** | **1,376,897** |
| Overseas sales as a percentage of consolidated net sales | **5.6%** | **5.4%** | **1.7%** | **12.7%** | **—** | **—** | **—** | **—** |

| | Millions of yen | | | |
|---|---|---|---|---|
| | 2005 | | | |
| | United States | Europe | Other | Total |
| Overseas sales | ¥8,031 | ¥6,011 | ¥1,839 | ¥ 15,881 |
| Consolidated net sales | — | — | — | 157,462 |
| Overseas sales as a percentage of consolidated net sales | 5.1% | 3.8% | 1.2% | 10.1% |

(a) The principal countries and areas in each segment are as follows:
Europe: France, Germany, the United Kingdom, Belgium, Switzerland, the Netherlands, etc.
Other: South Korea, Taiwan, China, Thailand, Australia, New Zealand, etc.
(b) Overseas sales consisted of export sales of the Company, and sales of an overseas consolidated subsidiary.
(c) As the percentage of overseas sales for the year ended March 31, 2004 was less than 10% of consolidated net sales, the disclosure of overseas sales has been omitted.

## 21. Subsequent Event

The following appropriation of retained earnings of the Company, which has not been reflected in the accompanying consolidated financial statements for the year ended March 31, 2006 were approved at a meeting of the Company's shareholders held on June 27, 2006:

| | Millions of yen | Thousands of U.S. dollars |
|---|---|---|
| Year-end cash dividends (¥3 = U.S.$0.03 per share) | ¥677 | $5,763 |

# Report of Independent Auditors

The Board of Directors
ISEKI & CO., LTD.

We have audited the accompanying consolidated balance sheets of ISEKI & CO., LTD. and consolidated subsidiaries as of March 31, 2006, 2005 and 2004, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of ISEKI & CO., LTD. and consolidated subsidiaries at March 31, 2006, 2005 and 2004, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

**Supplemental Information**
As described in Note 3, effective April 1, 2005, the Company and its domestic consolidated subsidiaries adopted a new accounting standard for the impairment of fixed assets.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2006 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1.

June 28, 2006
Ernst & Young Shin Nihon

# Corporate Data

(As of March 31, 2006)

**Head Office**
700 Umaki-cho, Matsuyama, Ehime 799-2692, Japan
Tel: 81-89-979-6111
Fax: 81-89-978-6440

**Tokyo Headquarters**
3-14, Nishi-Nippori 5-chome, Arakawa-ku, Tokyo 116-8541, Japan
Tel: 81-3-5604-7602
Fax: 81-3-5604-7701

**Web Site**
http://www.iseki.co.jp/

**Founded**
August 1926

**Paid-in Capital**
¥22,785 million

**Number of Employees (Consolidated)**
6,680

**Stock Listings**
Tokyo Stock Exchange (1st Section)
Osaka Securities Exchange (1st Section)

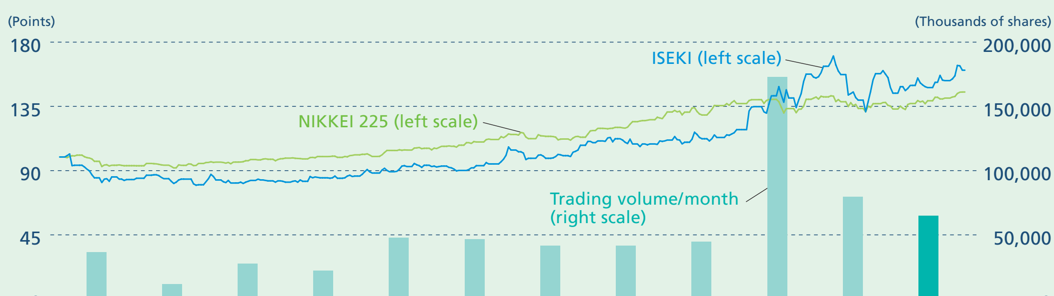
**Transfer Agent and Registrar**
The Chuo Mitsui Trust and Banking Company, Limited.
33-1, Shiba 3-chome, Minato-ku, Tokyo 105-8574, Japan

**Shares Issued and Outstanding**
226,536,329

**Number of Shareholders**
27,776

**Independent Auditor**
Ernst & Young ShinNihon

## Stock Performance and Trading Volume per Month




| | '05/4 | '05/5 | '05/6 | '05/7 | '05/8 | '05/9 | '05/10 | '05/11 | '05/12 | '06/1 | '06/2 | '06/3 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Opening price | 323 | 279 | 276 | 273 | 286 | 306 | 340 | 367 | 362 | 407 | 501 | 500 |
| High | 339 | 292 | 291 | 290 | 316 | 355 | 369 | 384 | 393 | 526 | 563 | 566 |
| Low Closing price | 267 | 261 | 266 | 270 | 284 | 296 | 320 | 352 | 356 | 405 | 426 | 468 |
| Trading volume/ month | 277 | 279 | 273 | 285 | 306 | 345 | 365 | 365 | 392 | 511 | 520 | 529 |
| (Unit: thousands) | 37,043 | 12,133 | 27,994 | 22,646 | 48,447 | 47,080 | 42,238 | 42,198 | 45,361 | 173,658 | 80,195 | 65,287 |

Share Price on April 1, 2005 (¥329)=100

ISEKI & CO., LTD.
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URL: http://www.iseki.co.jp/

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