FINANCIAL REVIEW

Operating Results

SEGMENT SALES

Consolidated net sales rose 0.3% from ¥655.8 billion to ¥657.9 billion ($6,148 million) in fiscal 2005, the year ended March 31, 2005.

The Company's operations are affected by the economies of various regions of the world, including Japan, the United States, Europe and China. Despite rising crude oil prices and other factors that restricted growth, the U.S. economy generally expanded steadily due in part to an upturn in capital expenditures and improvements in employment statistics and household incomes. European economies, while resilient in the first half of fiscal 2005, suffered a slowdown in the second half due to the effects of a strengthening euro, rising crude oil prices and other negative factors. China, meanwhile, maintained a high economic growth rate. In comparison, the Japanese economy slowed due to a drop-off in exports, the result of second-half production cutbacks by manufacturers of IT and digital products, despite strength in capital expenditures that was supported by strong corporate earnings.

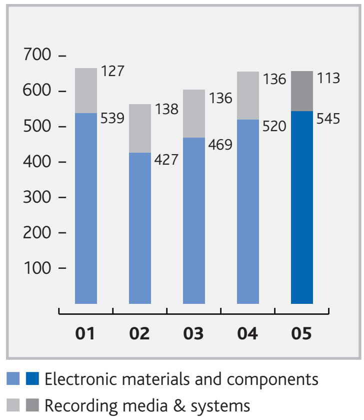
In the electronics industry in the first half of fiscal 2005, demand for digital home appliances, such as LCD and plasma TVs and DVD recorders, was boosted by the Summer Olympic Games in Athens and other factors. This resulted in strong demand for the Company's electronic components in the first half. However, demand for these components began to cool in the second half in line with production cutbacks of finished products that use them.

In this business environment, the Company continued to implement cost structure reforms, for example, the improvement of variable expenses by reviewing terms of supply and requesting discounts from purchased materials vendors. The Company also actively made investments to drive growth, such as by ramping up production capacity of capacitors and forging a strategic alliance in HDD heads.

As a result, the electronic materials and components segment posted net sales of ¥545.2 billion ($5,095 million), up 4.9% from ¥519.8 billion in the previous fiscal year.

Sales in the electronic materials sector rose 4.8% from ¥166.8 billion to ¥174.8 billion ($1,634 million). Sales of multilayer chip capacitors, a mainstay of capacitor products, increased year over year. In the first half of fiscal 2005, the Athens Olympics propelled demand for digital home appliances higher, which had an add-on effect for components used in them. In the second half, however, demand for components cooled, this time the result of cutbacks in the production of digital home appliances, and prices also dropped. But, against this market backdrop, the Company absorbed the sales price declines and the effect of unfavorable foreign exchange movements through improvements

Net Sales
(Yen in billions)



to its product mix. In ferrite cores, sales declined from the previous fiscal year, despite higher demand for general-purpose power supply cores for digital home appliances and cores for communications equipment. This decrease was due to a reduction in output of deflection yoke cores and flyback transformer cores used in CRT TVs. Magnet sales increased year over year, the result of steadily rising demand for use in automotive and HDD applications.

Sales in the electronic devices sector increased 7.8% from ¥108.0 billion to ¥116.4 billion ($1,088 million). Inductive devices, the largest product category in this sector, posted higher sales, despite lower sales prices and the negative effect of foreign exchange movements. This increase was attributable to higher demand spurred by acceleration in the pace at which automobiles are incorporating electronics and the increasing sophistication of mobile phones, as well as by new product launches. Sales of high-frequency components declined marginally year over year because higher sales volume and an improved product mix failed to completely offset persistently strong discounting pressure from mobile phone handset manufacturers, the main customer for these components. In power systems, sales of DC-DC converters and DC-AC inverters were healthy. Sensors and actuators recorded higher sales due to growth in demand for use in PCs and peripherals and communications equipment.

In the recording devices sector, sales rose 1.9% from ¥230.1 billion to ¥234.6 billion ($2,192 million). Sales of HDD heads, the main product in this sector, rose year over year. However, the Company had to overcome the loss of business from a major customer that started producing heads in house in 2004, as well as the impact of falling sales prices and unfavorable foreign exchange movements. Cutbacks in HDD inventories at customers in the first half of fiscal 2005 also affected the sector's performance. However, demand for HDD heads rose in the second half of the fiscal year following the end of these cutbacks. Sales of other heads declined year over year due to sluggish sales of optical pickups.

Sales in the semiconductors and others sector climbed 30.8% from ¥14.9 billion to ¥19.4 billion ($182 million). The Company recorded slightly higher sales of anechoic chambers for electromagnetic noise control and equipment used in these chambers. There was also growth in external sales of manufacturing equipment due to higher investments in semiconductor facilities and equipment by customers.

Operating income of the electronic materials and components segment in fiscal 2005 was ¥67.5 billion, up ¥8.8 billion from fiscal 2004. In spite of the deep-rooted pressure for sales price discounts, operating income increased due to higher sales of capacitors and inductive devices, discounts in raw materials and cost improvements by rationalization.

In the recording media & systems segment, sales declined 17.2% from ¥136.0 billion to ¥112.6 billion ($1,053 million). Sales of audiotapes and videotapes declined year over year. While the Company maintained a high market share, demand is declining for these products as a whole. Sales of optical media increased, with higher DVD sales volume offsetting a sharp fall in DVD prices and lower CD-R sales. Sales of other products decreased year over year. There was an increase in sales of LTO-standard* (Linear Tape-Open) tape-based data storage media for computers. However, a decline in sales caused by the sale in the previous fiscal year of a U.S. software development subsidiary and lower sales of recording equipment brought overall sales of other products down year over year.

Operating loss of the recording media & systems segment in fiscal 2005 was ¥7.7 billion, up ¥5.5 billion from fiscal 2004. Operating loss increased due to a decline in demand of audiotapes and videotapes as a whole, decrease in sales as a result of sale of a subsidiary in the United States of America in fiscal 2004, and continuous drop in sales prices mainly in optical media.

*Linear Tape-Open, LTO, LTO logo, Ultrium and Ultrium logo are trademarks of HP, IBM and Certance LLC in the U.S., other countries or both.

SALES BY REGION

Yen in millions (%)

Years ended March 31	2005		2004		2003	
Japan	**¥184,025**	**(28.0)**	168,623	(25.7)	165,484	(27.4)
Americas	**77,813**	**(11.8)**	88,734	(13.5)	104,134	(17.2)
Europe	**71,702**	**(10.9)**	80,710	(12.3)	77,713	(12.9)
Asia (excluding Japan)	**321,612**	**(48.9)**	314,875	(48.0)	254,925	(42.1)
Middle East and Africa	**2,701**	**(0.4)**	2,850	(0.5)	2,609	(0.4)
Net sales	**¥657,853**	**(100.0)**	655,792	(100.0)	604,865	(100.0)

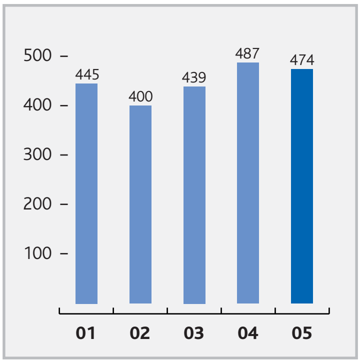
Note: Sales by region are classified by the customer location.

By region, sales in Japan rose 9.1% from ¥168.6 billion to ¥184.0 billion ($1,720 million). Overseas sales declined 2.7% from ¥487.2 billion to ¥473.8 billion ($4,428 million). Overseas sales accounted for 72.0% of consolidated net sales.

In Japan, sales in the electronic devices sector and recording media & systems segment declined, while higher sales were recorded in the electronic materials, recording devices and semiconductors and others sectors. The electronics materials and components segment saw its operating income increase by ¥17.6 billion due to increase in operating ratio, discount in raw materials and decrease in cost by rationalization. Although operating loss of the recording media & systems segment increased slightly, operating income in fiscal 2005 was ¥25.8 billion, up ¥16.9 billion from fiscal 2004.

In Asia (excluding Japan) and Oceania, sales declined in the recording devices sector and recording media & systems segment, but sales increased in the electronic materials and electronic devices sectors. The operating income of the electronic materials and components segment decreased by ¥8.8 billion. This decrease is due to a significant decline in sales prices mainly in recording devices and capacitors. Operating income of the recording media & systems segment also decreased slightly, resulting in operating income for fiscal 2005 of ¥33.6 billion, ¥9.5 billion less than fiscal 2004.

Overseas Sales
(Yen in billions)



In the Americas, sales decreased in the electronic materials and recording devices sectors as well as the recording media & systems segment. The higher yen versus the U.S. dollar also impacted sales in the Americas. The operating income of the electronic materials and components segment decreased ¥0.9 billion from fiscal 2004. However, operating income in fiscal 2005 was ¥5.5 billion, up ¥0.9 billion from fiscal 2004, due to decrease in operating loss of the recording media & systems segment as a result of sale of a subsidiary engaged in software development.

In Europe, lower sales were recorded in the electronic materials and semiconductors and others sectors as well as the recording media & systems segment. While operating loss of the electronic materials and components decreased, operating loss of the recording media & systems segment in fiscal 2005 reversed from operating income in fiscal 2004 to operating loss of ¥4.7 billion by decrease of ¥5.8 billion, due to a significant decline in sales prices mainly in optical media. As a result, operating loss in fiscal 2005 was ¥5.1 billion, ¥5.0 billion less than fiscal 2004.

EFFECT OF FOREIGN EXCHANGE MOVEMENTS

In fiscal 2005, overseas sales accounted for 72.0% of consolidated net sales, down 2.3 percentage points. As a result, fluctuations in foreign exchange rates have a significant effect on the Company's consolidated sales and income. During fiscal 2005, the yen appreciated 5.0% in relation to the U.S. dollar and depreciated 1.9% in relation to the euro, based on the Company's average internal exchange rates. Overall, the Company estimates that each ¥1 movement in the exchange rates during fiscal 2005 had the effect of reducing net sales by about ¥4.0 billion and operating income by about ¥1.0 billion, in relation to the prior fiscal year.

By region, foreign exchange fluctuations reduced sales in Japan by about ¥3.8 billion, in Asia (excluding Japan) and Oceania by about ¥23.6 billion and in the Americas by about ¥5.5 billion, but increased sales in Europe by about ¥1.4 billion. The effect of foreign exchange fluctuations on consolidated net sales after the elimination of intersegment transactions was about ¥20.6 billion.

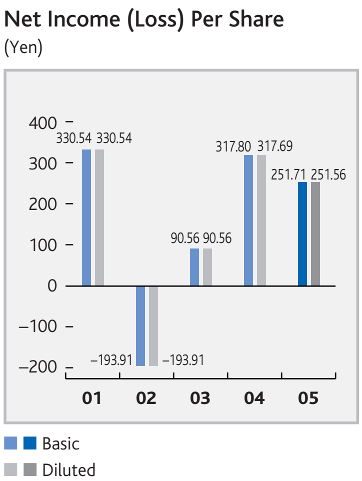
The Company conducts a large share of business activities outside Japan as one way to offset the impact of exchange-rate fluctuations. Such activities include manufacturing and sales, as well as research, design and procurement. In-region production in fiscal 2005 represented 112.1% of sales in Asia (excluding Japan) and Oceania, 20.9% in the Americas, and 23.9% in Europe. Overseas production accounted for 59.0% of total sales in fiscal 2005, compared with 58.6% one year earlier, and for 81.9% of overseas sales, compared with 78.9% one year earlier. The rise in the percentage of overseas production in fiscal 2005 is mainly due to higher production in Asia in the electronic materials and components segment.

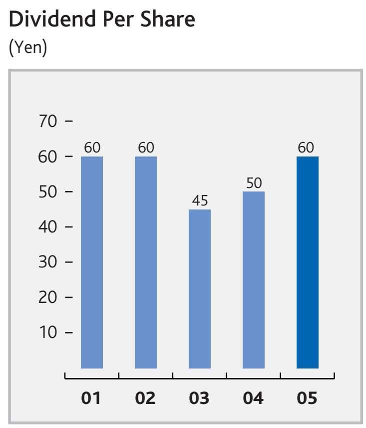
The Company and certain overseas consolidated subsidiaries hedge exposure to foreign exchange movements by entering into forward foreign exchange contracts and swaps for some foreign currency-denominated obligations. Foreign exchange risk arising in operating activities is hedged by using forward foreign exchange contracts. In principle, the Company's policy is to hedge up to 50% of expected foreign currency-denominated accounts receivable for each month for the next six months. Due to the global nature of operations, management realizes that currency movements continue to have the potential to exert a material influence on consolidated performance.

EXPENSES AND NET INCOME

Yen in millions (%)

Years ended March 31	2005		2004		2003	
Net sales	**¥657,853**	**(100.0)**	655,792	(100.0)	604,865	(100.0)
Cost of sales	**484,323**	**(73.6)**	476,407	(72.6)	459,552	(76.0)
Selling, general and administrative expenses	**119,886**	**(18.2)**	122,875	(18.8)	115,569	(19.1)
Settlement gain, net	**6,186**	**(0.9)**	–	–	–	–
Restructuring cost	**–**	**–**	–	–	5,197	(0.9)
Other income (other expenses)	**898**	**(0.1)**	(663)	(–0.1)	(3,995)	(–0.7)
Income taxes and minority interests	**23,763**	**(3.6)**	12,492	(1.9)	6,959	(1.1)
Loss from discontinued operations, net of tax	**3,665**	**(0.5)**	1,254	(0.2)	1,574	(0.2)
Net income	**¥ 33,300**	**(5.1)**	42,101	(6.4)	12,019	(2.0)





The cost of sales increased 1.7% from ¥476.4 billion in fiscal 2004 to ¥484.3 billion ($4,526 million) in fiscal 2005 due to higher sales. Cost of sales increased from 72.6% to 73.6% of net sales, respectively. This reflected the negative effects on earnings of strong discounting pressure in all segments and foreign exchange movements, mainly the appreciation of the yen relative to the U.S. dollar. These factors outweighed positive influences such as cost reductions from structural reforms and numerous other actions to cut costs, including the receipt of discounts on purchased materials. As a result, gross profit decreased 3.3% year over year.

Selling, general and administrative expenses decreased ¥3.0 billion from ¥122.9 billion in fiscal 2004 to ¥119.9 billion ($1,120 million) in fiscal 2005, and decreased from 18.8% to 18.2% of net sales, respectively. Selling, general and administrative expenses decreased despite a 0.3% rise in net sales due to efforts to strictly manage fixed expenses, such as by lowering personnel expenses through greater operational efficiency. The main components of this decrease were reductions in personnel expenses of ¥3.1 billion and marketing expenses of ¥1.3 billion. Research and development expenses included in selling, general and administrative expenses increased ¥3.4 billion from ¥32.9 billion in fiscal 2004 to ¥36.3 billion ($340 million) in fiscal 2005, and increased from 5.0% to 5.5% of net sales, respectively.

In addition, pursuant to the newly enacted Contributed Benefit Pension Plan Law, the Company received an exemption from the Minister of Health, Labor and Welfare, effective September 25, 2003, from the obligation to pay benefits related to future employee services with respect to the substitutional portion of its Employees' Pension Fund (EPF). The Company was also granted an exemption from the obligation to pay benefits in relation to past employee services in October 2004 with respect to the substitutional portion of its domestic contributory plan. The transfer of the substitutional portion of the Company's EPF liabilities to the government was completed on January 31, 2005. As a result of the transfer, the Company recognized as a subsidy from the Japanese government an amount equal to the difference between the fair value of the obligation deemed "settled" with the Japanese government and the assets required to be transferred to the government. The subsidy that the Company recognized amounted to ¥33.5 billion ($313 million). In addition, the Company recognized a settlement loss in an amount equal to the product of (i) the ratio of the obligation settled to the total EPF obligation outstanding immediately prior to settlement, both of which exclude the effect of future salary progression relating to the substitutional portion of the EPF obligation, and (ii) the net unrecognized gain/loss immediately prior to settlement, which amounted to ¥27.3 billion ($256 million). This gain and loss is included in operating income in the accompanying consolidated statements of income for the year ended March 31, 2005.

Other income (deductions) improved ¥1.6 billion from the previous fiscal year, reflecting a ¥2.2 billion decline in foreign exchange losses and a ¥1.0 billion decrease in loss on securities, net, as well as other factors.

The ratio of income taxes to income from continuing operations before income taxes (the effective tax rate) increased from 21.7% in fiscal 2004 to 38.3% in fiscal 2005. The increase reflects mainly the fact that the Company received a notification and assessment of additional tax from the Tokyo Regional Tax Bureau (Nihonbashi Tax Office) asserting that prices charged and paid by the Company in connection with sales and purchases of products involving its overseas subsidiaries have not been commensurate with the prices of similar transactions involving unrelated third parties. The period of additional assessments covers tax years ending March 1999 through March 2003. The additional tax assessed by the Tokyo Regional Tax Bureau amounted to ¥12.0 billion including interest and penalty, which has been reflected as additional tax expense and other expense, net of deferred income tax benefits, in the accompanying consolidated statements of income for the year ended March 31, 2005.

The Company posted net income of ¥33.3 billion ($311 million), resulting in net income per diluted share of ¥251.56 ($2.35), compared with ¥317.69 in the previous fiscal year. Return on equity (ROE) decreased from 7.5% to 5.5%. This was due to an approximate ¥62.8 billion increase in stockholders' equity, which reflected a decrease of about ¥38.7 billion in accumulated other comprehensive loss due to such factors as a decrease of about ¥32.9 billion in minimum pension liability adjustments following the transfer of the substitutional portion of EPF liabilities, as well as an increase in retained earnings.

Cash dividends per share paid during the fiscal year totaled ¥60 ($0.56). This dividend is the sum of the June 2004 year-end dividend of ¥30 and the December 2004 interim dividend of ¥30. Shareholders of record on March 31, 2005 received a cash dividend of ¥40 per share at the end of June 2005.

In fiscal 2005, consolidated net income included loss from discontinued operations of ¥3.7 billion related to TDK Semiconductor Corporation. See discussion at Discontinued Operations.

FISCAL 2004 VS. FISCAL 2003

SEGMENT SALES

Consolidated net sales increased 8.4% to ¥655.8 billion in fiscal 2004, the year ended March 31, 2004, from ¥604.9 billion one year earlier.

The Japanese economy in fiscal 2004 tended toward recovery, led by IT-related production and exports. However, with no upturn evident in household incomes, consumer spending failed to rebound. Meanwhile, the U.S. economy, the driving force for the world economy, expanded compared with the previous year, with consumer spending, housing investment and capital expenditures all rising, as the government eased fiscal and monetary policy.

In the electronics industry, the year was characterized by the rising popularity of LCD and plasma flat-screen TVs, digital cameras and DVD recorders, as well as by the increasing sophistication of mobile phones, replacement demand for PCs, and the growing use of electronics in automobiles. However, deflationary trends in world markets affected these finished products, placing unrelenting pricing pressure on electronic materials and components and recording media & systems, the Company's main products.

The Company saw orders drop in the first quarter (April-June 2003) of fiscal 2004 due to factors such as the Severe Acute Respiratory Syndrome (SARS) outbreak and fallout from the Iraq war. Nevertheless, the Company remained focused on implementing cost structure reforms, carrying on initiatives from fiscal 2003 to improve asset productivity and concentrate resources on strategic businesses.

In the electronic materials and components segment, net sales increased 10.9% from ¥468.5 billion to ¥519.8 billion.

Sales in the electronic materials sector decreased 1.3% from ¥168.9 billion to ¥166.8 billion. Sales of multilayer chip capacitors, a mainstay of capacitor products, increased. Higher orders for capacitors, which reflected growing demand for communications products, offset falling sales prices and the negative effect of exchange rate movements. In ferrite cores, deflection yoke cores and flyback transformer cores saw sales drop due to falling demand and sales prices. The drop in orders for these cores was a reflection of a rapid shift in consumer demand from CRT TVs to LCD, plasma and other flat-panel models. Higher sales of small coils and transformer cores, a category where demand increased, failed to offset this decrease, resulting in a decline in overall sales of ferrite cores. Magnet sales declined as the effect of falling sales prices outweighed higher sales volumes.

In the electronic devices sector, sales decreased 4.2% from ¥112.7 billion to ¥108.0 billion. Inductive devices, the largest product category in this sector, posted higher sales as demand for communications applications increased in line with advances in the performance of mobile phones. However, sales growth was held back by lower sales prices and foreign currency movements. Sales of high-frequency components decreased despite an upswing in shipment volumes that resulted from strong demand for components used in mobile phones, the main market for these components, and successful activities to win new orders. The decrease reflected the continuing glut in the supply of high-frequency components in the market as a whole, which prompted customers to demand price reductions that were greater than in other electronic component categories. Sensors and actuators recorded higher sales due to growth in demand for communications applications and PCs and peripherals. However, sales of power systems declined due to lackluster demand associated with the amusement field, a sector where demand was strong in the previous fiscal year.

Recording devices sales climbed 30.8% from ¥176.0 billion to ¥230.1 billion. Sales of HDD heads, the main product in this sector, were up sharply. This was primarily because of continuing expansion in the HDD market and the resulting robust HDD sales by major Company customers. Sales of other heads also increased.

Sales in the semiconductors and others sector climbed 37.1% from ¥10.9 billion to ¥14.9 billion. Growth reflected higher sales of anechoic chambers for noise control and equipment used in these chambers.

Operating income of the electronic materials and components segment in fiscal 2004 was ¥58.7 billion, up ¥35.7 billion from fiscal 2003. This increase was due to significantly higher sales of recording devices and cost reductions such as reduced depreciation from reforms to the profit structure. This increase offset declines in profit due to lower sales of other products and the negative effect of the appreciation of the yen.

In the recording media & systems segment, sales edged down 0.3% from ¥136.4 billion to ¥136.0 billion.

While the Company continued to command a high share of the audiotape and videotape markets, sales in these two categories decreased as demand continued to shrink due to structural changes. Optical media products posted increased sales, with higher sales volumes of CD-Rs and DVDs in an expanding market offsetting lower sales prices. Sales of other products decreased. Higher sales of LTO-standard* (Linear Tape-Open) tape-based data storage media for computers failed to offset lower sales of PC software, recording equipment and other products.

The recording media & systems segment saw some increased profits due to higher sales of optical media products. However, the segment experienced losses of ¥2.2 billion in fiscal 2004, down ¥3.7 billion from fiscal 2003, due to falling sales prices of other products and significantly reduced profits from the negative effect of the appreciation of the yen.

*Linear Tape-Open, LTO, LTO logo, Ultrium and Ultrium logo are trademarks of HP, IBM and Certance LLC in the U.S., other countries or both.

SALES BY REGION

By region, sales in Japan increased 1.9% to ¥168.6 billion in fiscal 2004 from ¥165.5 billion in fiscal 2003. There was a 10.9% rise in overseas sales year over year to ¥487.2 billion from ¥439.4 billion in fiscal 2003. Overseas sales accounted for 74.3% of consolidated net sales.

In Japan, sales edged up from the previous fiscal year as higher sales in the recording devices sector offset sales decreases caused by lower orders for DC-DC converters for the amusement field and falling demand for audiotapes. The electronic materials and components segment saw its operating income increase by ¥7.2 billion due to ongoing cutbacks in expenses and improvements in cost categories mainly in raw materials price reductions resulting from structural reforms. This increase offset losses in the recording media & systems segment. Accordingly, operating income for fiscal 2004 increased to ¥8.5 billion, up ¥3.3 billion from fiscal 2003.

In Asia (excluding Japan) and Oceania, sales increased due to higher sales of recording devices, as the Company regained market share, and strong sales of electronic materials and electronic devices. The operating income of the electronic materials and components segment significantly increased by ¥22.2 billion. This increase accounted for almost the entire increase in operating income across the region, which was due mainly to increased sales of recording devices. The profits of the recording media & systems segment remained practically unchanged, resulting in operating income for fiscal 2004 of ¥42.9 billion, ¥22.3 billion more than fiscal 2003.

In the Americas, sales decreased due to the effect of foreign exchange translation resulting from the appreciation of the yen. Other factors were lower sales in the recording media & systems segment despite higher sales of optical media products, including DVDs, due to lower sales of other products; and lower sales in the electronic materials and components segment. The operating income of the electronic materials and components segment increased by ¥5.7 billion. This increase resulted mainly from an increase in sales of recording devices. This increase offset losses in the recording media & systems segment, which resulted from reduced sales of PC software and recording equipment. Accordingly, operating income for fiscal 2004 was ¥5.0 billion, up ¥3.6 billion from fiscal 2003.

In Europe, sales increased. Sales were sluggish in the electronic materials and components segment, but rose in the recording media & systems segment as sharply higher sales of DVDs and other optical media products countered falling demand for audiotapes. The operating income of the recording media & systems segment increased by ¥2.3 billion, due mainly to increased sales of optical media, which, when combined with increased profits in the electronic materials and components segment, resulted in operating losses for fiscal 2004 of ¥0.1 billion, an improvement of ¥3.4 billion on fiscal 2003.

EFFECT OF FOREIGN EXCHANGE MOVEMENTS

In fiscal 2004, overseas sales accounted for 74.3% of consolidated net sales, up 1.7 percentage points. As a result, fluctuations in foreign exchange rates have a significant effect on the Company's consolidated sales and income. During fiscal 2004, the yen appreciated 7.2% in relation to the U.S. dollar and depreciated 9.7% in relation to the euro, based on the Company's average internal exchange rates. Overall, the Company estimates that each ¥1 movement in exchange rates during fiscal 2004 had the net effect of reducing net sales by about ¥4.0 billion and operating income by about ¥1.5 billion, in relation to the prior fiscal year.

By region, foreign exchange fluctuations reduced sales in Japan by about ¥11.0 billion, sales in Asia (excluding Japan) and Oceania by about ¥31.0 billion and sales in the Americas by about ¥9.3 billion, but increased sales in Europe by about ¥4.5 billion. The negative effect of foreign exchange fluctuations on consolidated net sales after the elimination of intersegment transactions was about ¥25.8 billion.

The Company conducts a large share of business activities outside Japan as one way to offset the impact of exchange-rate fluctuations. Such activities include manufacturing and sales, as well as research, design and procurement. In-region production in fiscal 2004 represented 111.6% of sales in Asia (excluding Japan) and Oceania, 22.5% in the Americas, and 23.8% in Europe. Overseas production accounted for 58.6% of total sales in fiscal 2004, compared with 55.8% one year earlier, and for 78.9% of overseas sales, compared with 76.8% one year earlier. The rise in the percentage of overseas production in fiscal 2004 is mainly due to higher production in Asia in the electronic materials and components segment primarily as a result of an increase in overseas production, which rose in line with sales growth resulting from a recovery in market share in recording devices.

The Company and certain overseas subsidiaries hedge exposure to foreign exchange movements by entering into forward foreign exchange contracts and swaps for some foreign currency-denominated obligations. Foreign exchange risk arising in operating activities is hedged by using forward foreign exchange contracts. In principle, the Company's policy is to hedge up to 50% of expected foreign currency-denominated accounts receivable for each month for the next six months. Due to the global nature of operations, management realizes that currency movements continue to have the potential to exert a material influence on consolidated performance.

EXPENSES AND NET INCOME

Cost of sales increased 3.7% from ¥459.6 billion in fiscal 2003 to ¥476.4 billion in fiscal 2004 due to higher sales. Cost of sales decreased from 76.0% to 72.6% of net sales, respectively. This reflected both an improvement in the capacity utilization rate accompanying higher sales, and cutbacks in expenses and improvements in various cost categories resulting from structural reforms. These benefits outweighed strong downward pressure on prices and the adverse effects of foreign exchange movements. As a result, gross profit increased 23.4%.

Selling, general and administrative expenses increased ¥7.3 billion from ¥115.6 billion in fiscal 2003 to ¥122.9 billion in fiscal 2004, and decreased from 19.1% to 18.8% of net sales, respectively. Selling, general and administrative expenses rose in line with the 8.4% rise in net sales as the Company prevented further growth in these expenses by strictly managing fixed expenses. Personnel, which is the payment of salaries, bonuses and retirement payments, freight charges, marketing expenses and outsourcing expenses increased ¥2.6 billion, ¥0.9 billion, ¥0.7 billion, and ¥0.4 billion, respectively. Research and development expenses represented 5.0% of net sales, the same as in the previous fiscal year.

Other income (deductions) improved ¥3.3 billion from the previous fiscal year. While there was a ¥1.6 billion increase in foreign exchange losses, there was a ¥2.2 billion decrease in loss on securities, net and increase of ¥1.3 billion in equity in earnings of affiliates.

The ratio of income taxes to income from continuing operations before income taxes (the effective tax rate) decreased from 30.1% in fiscal 2003 to 21.7% in fiscal 2004. The decrease reflects decrease in additional valuation allowance provided during the year and the higher amounts of income earned in China, etc. during fiscal 2004, which were taxed at rates lower than the Company's effective rate for all other jurisdictions in which it pays income taxes.

The Company posted a net income of ¥42.1 billion, resulting in net income per diluted share of ¥317.69, compared with ¥90.56 in the previous fiscal year. The return on equity increased from 2.1% to 7.5%. Cash dividends per share paid during the fiscal year totaled ¥50. This dividend is the sum of the June 2003 year-end dividend of ¥25 and the December 2003 interim dividend of ¥25. Shareholders of record on March 31, 2004 received a cash dividend of ¥30 per share at the end of June 2004.

In fiscal 2004, consolidated net income included loss from discontinued operations of ¥1.3 billion related to TDK Semiconductor Corporation. See discussion at Discontinued Operations.

Discontinued Operations

On March 31, 2005, the Company entered into an agreement to sell all outstanding stock of its wholly owned subsidiary, TDK Semiconductor Corporation ("TSC") for ¥1.5 billion ($14 million) to Golden Gates Capital ("Buyer"). The sale of TSC is part of the Company's continuing shift away from non-core products and technologies. The sale agreement also includes earn-out payments, to be made by the Buyer to the Company, of up to ¥3.5 billion ($33 million). The payments are contingent upon certain milestones being met related to future revenue targets extending through 2007. The transaction was completed on April 8, 2005. The Company has accounted for the sale of TSC as a discontinued operation. The results of operations for this subsidiary have been reported as discontinued operations for all periods presented and selected financial information for the years ended March 31, 2005, 2004 and 2003 for the discontinued operations, are summarized as follows:

	Yen (Millions)			U.S. Dollars (Thousands)
	2005	2004	2003	**2005**
Net sales	**¥ 2,242**	3,070	4,015	**$20,953**
Loss from operations before income taxes (including loss on disposal of ¥454 million in 2005)	**3,509**	244	2,471	**32,794**
Income tax expense (benefit)	**156**	1,010	(897)	**1,458**
Loss from discontinued operations	**¥ 3,665**	1,254	1,574	**$34,252**
Loss from discontinued operations per share:				
Basic	**¥(27.70)**	(9.47)	(11.86)	**$ (0.26)**
Diluted	**(27.69)**	(9.46)	(11.86)	**(0.26)**

See Note 20 to the Consolidated Financial Statements for further discussion.

Liquidity and Capital Resources

OPERATING CAPITAL REQUIREMENTS

The Company's requirements for operating capital primarily are for the purchase of raw materials and parts for use in the manufacture of its products. These expenses are booked as manufacturing expenses and selling, general and administrative expenses. The payment of payroll expenses, marketing expenses accompanying sales activities, and distribution-related expenses account for a significant portion of operating expenses. Personnel expenses account for a significant portion of R&D expenses. The necessary funds for these expenses are provided from cash generated by operations.

CAPITAL EXPENDITURES

In fiscal 2005, capital expenditures on a cash basis rose ¥16.5 billion from ¥44.5 billion to ¥61.0 billion ($570 million). This was the result of aggressive investment in IT home electronics appliances; high-speed, large-capacity networks; and car electronics, which are fields the Company regards as strategically important for growth.

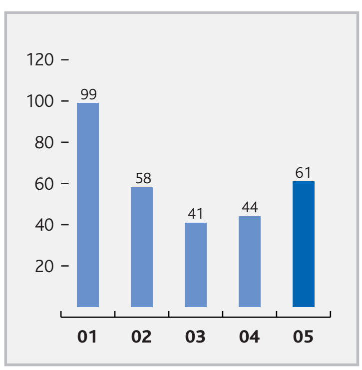
In the electronic materials and components segment, capital expenditures totaled ¥57.2 billion. The Company invested in the expansion of production capacity of HDD heads, facilities for rationalizing these activities and the development of technology for coping with increasing areal density. These investments centered mainly on China, the U.S. and the Philippines. Furthermore, investments were made to increase production and rationalize operations in multilayer chip capacitors and inductors, where growth in sales is expected due to acceleration in the pace at which electronics are being incorporated in automobiles, the increasingly sophisticated nature of mobile phones and other factors. These investments were made mainly in Japan and China.

In the recording media & systems segment, capital expenditures totaled ¥3.8 billion, mainly for facilities to increase DVD production.

The funds for these capital expenditures are provided from cash generated by operations.

Capital expenditures for fiscal 2004, which are described in detail on the following page increased by ¥3.5 billion, from ¥41.0 billion for fiscal 2003 to ¥44.5 billion.

Capital Expenditures
(Yen in billions)



In the electronic materials and components segment, due to the expansion of the market for recording devices, the Company has made investments principally in Asia, but also in the Americas and Japan, to increase production and rationalization for its recording devices. Other major expenditures include investments to increase production and rationalization for electronic materials and electronic devices (principally capacitors), and investments into the development of new products. Capital expenditures for fiscal 2004 of this segment increased by ¥1.7 billion from ¥38.4 billion to ¥40.1 billion.

In the recording media & systems segment, investments have been made in Europe and Japan to increase production and develop optical media products, whose market is expanding. Capital expenditures of this segment increased by ¥1.8 billion from ¥2.6 billion to ¥4.4 billion.

In principle, the funds for these capital expenditures are provided from cash generated by operations.

OFF-BALANCE SHEET ARRANGEMENTS

As part of its ongoing business, the Company does not conduct transactions with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which have been established for the purpose of facilitating off-balance sheet arrangements or other limited purposes.

On March 31, 2005, commitments outstanding for the purchase of property, plant and equipment approximated ¥12.3 billion ($115 million). The Company has entered into several purchase agreements with certain suppliers whereby the Company is committed to purchase a minimum amount of raw materials to be used in the manufacture of its products. Future minimum purchases remaining under the agreements approximated ¥3.8 billion ($36 million) at March 31, 2005. Contingent liabilities for guarantees of loans of the Company's employees and affiliates amounted to approximately ¥6.3 billion ($59 million).

The Company has various pension plans covering its employees. The unfunded amount as of March 31, 2005 was ¥42.3 billion ($396 million). The unfunded amount decreased by ¥47.7 billion as compared with last year mainly due to the transfer of the substitutional portion of EPF liabilities. As of March 31, 2005, ¥28.8 billion was accrued on the balance sheet as retirement and severance benefits, ¥44.7 billion less than a year ago.

Regarding loans, the Company essentially uses group funds, based on a policy of, in principle, not borrowing from banks or other outside sources. However, certain of the Company's overseas subsidiaries have their own credit facilities based on commercial paper issuing programs, allowing them to raise short-term funds should they be required.

Regarding the Company's capital expenditure plans, the Company's policy is to invest actively in targeted strategic fields to drive growth. Capital expenditures will be funded using internally generated funds.

The Company is planning capital expenditures of ¥65.0 billion in fiscal 2006, primarily for the expansion of production facilities and upgrading of facilities. Actual capital expenditures could differ from this forecast as a result of factors such as shifts in technology, demand, prices, competition, economic environments and foreign exchange rates.

Contractual obligations on March 31, 2005 are summarized as follows:

	Payments Due by Period (Yen in millions)				
	Total	Less than 1 year	1 to 3 years	3 to 5 years	After 5 years
Contractual obligations:					
Long-term debt	¥ 184	103	74	7	–
Operating leases	6,808	2,355	2,830	900	723
Purchase commitment of raw materials	3,841	3,247	291	177	126
Purchase commitment of property, plant and equipment	12,292	12,292	–	–	–
Total	¥23,125	17,997	3,195	1,084	849

FINANCIAL MANAGEMENT

Operating capital and capital expenditures are, in principle, funded by cash generated through operating activities. To improve capital efficiency, to the extent possible, the Company centralizes financial management in the Head Office, having introduced a cash management system (CMS) in Japan, the U.S. and Europe. Surplus funds are invested with an emphasis on low risk and liquidity. Funds from within the group will be utilized, to the extent possible, to extend financing to subsidiaries that cannot procure operating capital or funds for capital expenditures themselves.

CASH FLOWS

Years ended March 31	2005	2004	2003
			Yen in millions
Income from continuing operations	**¥ 36,965**	43,355	13,593
Adjustments to reconcile net income to net cash provided by operating activities	**56,617**	70,465	92,323
Net cash provided by operating activities	**93,582**	113,820	105,916
Net cash used in investing activities	**(60,863)**	(37,647)	(46,220)
Net cash used in financing activities	**(9,458)**	(9,661)	(7,925)
Net cash provided by (used in) discontinued operations	**(1,625)**	761	(1,983)
Effect of exchange rate changes on cash and cash equivalents	**2,717**	(10,669)	(4,998)
Net change in cash and cash equivalents	**¥ 24,353**	56,604	44,790

Fiscal 2005 cash and cash equivalents increased ¥24.3 billion from ¥227.2 billion to ¥251.5 billion ($2,351 million). Operating activities provided net cash of ¥93.6 billion ($875 million), ¥20.2 billion less than in fiscal 2004. The major component of cash provided by operating activities was depreciation and amortization of ¥52.8 billion, up ¥2.1 billion. In terms of changes in assets and liabilities, inventories decreased ¥11.3 billion, the result of efforts to reduce inventories, while retirement and severance benefits declined ¥6.8 billion due to the transfer of the substitutional portion of EPF liabilities and changes to the pension system. In addition, trade payables and accrued expenses decreased ¥8.0 billion and ¥11.4 billion, respectively, and income taxes payables, net increased ¥8.8 billion.

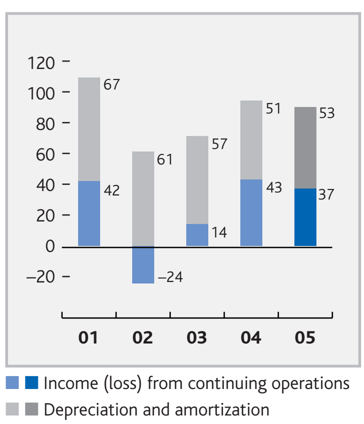
Investing activities used net cash of ¥60.9 billion ($569 million), ¥23.3 billion more than the ¥37.6 billion used in the previous fiscal year. The Company used ¥61.0 billion for capital expenditures, ¥16.5 billion more than in fiscal 2004, as a result of making aggressive investments to drive growth. Furthermore, payment for purchase of investments in securities increased ¥2.4 billion year over year. Regarding research and development expenses, the Company's policy is to focus investments in the strategic fields of IT home electronic appliances, high-speed and large-capacity networks and car electronics. Funds for research and development will be appropriated from internal funds.

Financing activities used net cash of ¥9.5 billion ($88 million), a decrease of ¥0.2 billion from the ¥9.7 billion used in fiscal 2004. There was an increase of ¥1.3 billion in dividends paid due to the increase in the dividend. On the other hand, there was a decline in the repayment of debt because debt has been virtually eliminated.

Regarding procurement costs, the Company has long-term corporate credit ratings of AA- and A1 from Standard & Poor's and Moody's, respectively. Furthermore, Standard & Poor's gives the Company their highest short-term credit rating, A-1+, and the Company's U.S. subsidiaries have been given the highest short-term rating of P-1 by Moody's. These ratings allow the Company to procure funds if needed at low interest rates.

The Company's fundamental policy is to give consideration to a consistent increase in dividends based on factors such as the return on equity (ROE), dividends as a percentage of equity (DOE) and the Company's results of operations on a consolidated basis. Funds for paying dividends are allocated from internal funds.

Net Cash Flows
(Yen in billions)



In the dynamically changing electronics industry, it is necessary to make well-timed investments. Given this need, and the possibility that unstable financial conditions will continue in Japan, the Company's policy is to maintain a high level of liquidity. The Company thus has no immediate plans to repurchase its stock.

The Company estimates that operating cash flows and other internal resources will provide adequate liquidity in fiscal 2006. Regarding cash flows for the fiscal years ending March 31, 2006 and onward, the Company expects to provide the necessary funds from operating cash flows by increasing profitability and improving the return on assets.

Fiscal 2004 cash and cash equivalents increased ¥56.6 billion to ¥227.2 billion from ¥170.6 billion in the previous fiscal year. Operating activities provided net cash of ¥113.8 billion, a year-on-year increase of ¥7.9 billion. This reflected mainly a ¥30.1 billion increase in net income to ¥42.1 billion and a ¥6.4 billion decrease in depreciation and amortization to ¥50.7 billion, as well as decreases in trade receivables and inventories of ¥5.0 billion and ¥21.4 billion, respectively. Regarding the shortfall in pension assets, the Company plans to take action in response to certain recent reforms to the pension system, including transferring the substitutional portion of Employees' Pension Fund ("EPF") liabilities.

Investing activities used net cash of ¥37.6 billion, a decrease of ¥8.6 billion from ¥46.2 billion in the previous fiscal year. The main factor was a ¥6.2 billion decrease in payment for purchase of other investments to ¥0.4 billion. Regarding research and development expenses, the Company's policy is to focus investments in the strategic fields of IT home electronic appliances, high-speed and large-capacity networks and car electronics. Funds for research and development will be appropriated from internal funds.

Financing activities used net cash of ¥9.7 billion, ¥1.8 billion more than the ¥7.9 billion in cash used in the previous fiscal year. This mainly represented an increase of ¥0.8 billion in repayments of short-term debt and a ¥0.7 billion increase in dividends paid.

Fiscal 2003 cash and cash equivalents increased ¥44.8 billion to ¥170.6 billion, from ¥125.8 billion in the previous fiscal year. Operating activities provided net cash of ¥105.9 billion, a year over year increase of ¥61.7 billion. This reflected mainly a ¥37.8 billion increase in net income to ¥12.0 billion; a decrease of ¥3.8 billion in depreciation and amortization to ¥57.1 billion; a decrease in inventories of ¥14.9 billion; and an increase of ¥20.9 billion in trade payables. Regarding the shortfall in pension assets, the Company is currently considering reforms to the pension system, including transferring the substitutional portion of employee pension fund liabilities.

Investing activities used net cash of ¥46.2 billion, a decrease of ¥11.3 billion, from ¥57.5 billion in the previous fiscal year. The main factor was a ¥17.3 billion decrease in capital expenditures to ¥41.0 billion. Regarding research and development expenses, the Company's policy is to focus investments in the strategic fields of IT home electronic appliances, high-speed and large-capacity networks and car electronics. Funds for research and development will be appropriated from internal funds.

Financing activities used net cash of ¥7.9 billion, ¥5.3 billion less than the ¥13.2 billion in cash used in the previous fiscal year. This mainly represented a ¥3.3 billion decrease in repayments of short-term debt and a ¥2.0 billion decrease in dividends paid.

FINANCIAL POSITION

Yen in millions (%)

Years ended March 31	2005		2004		2003	
Short-term debt	¥ –	–	315	(0.1)	1,431	(0.3)
Current installments of long-term debt	103	(0.0)	101	(0.0)	488	(0.1)
Long-term debt, excluding current installments	81	(0.0)	27	(0.0)	94	(0.0)
Stockholders' equity	639,067	(100.0)	576,219	(99.9)	553,885	(99.6)
Total capital	¥639,251	(100.0)	576,662	(100.0)	555,898	(100.0)

Total assets amounted to ¥808.0 billion ($7,551 million) as of March 31, 2005, up ¥37.7 billion from ¥770.3 billion at the previous fiscal year-end. As of March 31, 2005, cash and cash equivalents were ¥251.5 billion ($2,351 million), ¥24.3 billion higher than ¥227.2 billion a year ago. Trade receivables were ¥148.0 billion ($1,383 million), ¥9.7 billion higher than ¥138.3 billion a year ago. Property, plant and equipment increased ¥8.1 billion from ¥208.9 billion to ¥217.0 billion ($2,028 million) and noncurrent deferred income taxes decreased ¥25.5 billion from ¥34.1 billion to ¥8.6 billion ($81 million).

Total liabilities decreased ¥27.0 billion from ¥190.8 billion to ¥163.8 billion ($1,531 million). Trade payables rose ¥2.2 billion from ¥59.9 billion to ¥62.1 billion ($580 million), and income taxes payables increased ¥14.6 billion from ¥4.7 billion to ¥19.3 billion ($180 million). However, retirement and severance benefits declined ¥44.7 billion from ¥73.5 billion to ¥28.8 billion ($270 million) due to the transfer of the substitutional portion of EPF liabilities and changes to the pension system. Accrued expenses decreased ¥2.4 billion from ¥33.4 billion to ¥31.0 billion ($290 million).

Total stockholders' equity increased ¥62.9 billion from ¥576.2 billion to ¥639.1 billion ($5,973 million). Retained earnings increased ¥24.8 billion from ¥560.8 billion to ¥585.6 billion ($5,472 million) and accumulated other comprehensive loss decreased ¥38.7 billion from ¥90.4 billion to ¥51.7 billion ($483 million).

Total assets amounted to ¥770.3 billion as of March 31, 2004, up ¥23.0 billion from ¥747.3 billion at the previous fiscal year-end. As of March 31, 2004, cash and cash equivalents were ¥227.2 billion, ¥56.6 billion higher than ¥170.6 billion a year ago. However, property, plant and equipment decreased ¥17.0 billion to ¥208.9 billion from ¥225.9 billion, and noncurrent deferred income taxes decreased ¥9.8 billion to ¥34.1 billion from ¥43.9 billion.

Total liabilities increased ¥0.7 billion, from ¥190.1 billion to ¥190.8 billion. Trade payables increased ¥2.9 billion, from ¥57.0 billion to ¥59.9 billion, accrued expenses increased ¥5.3 billion from ¥28.1 billion to ¥33.4 billion, and income taxes payables increased ¥3.6 billion, from ¥1.1 billion to ¥4.7 billion. Retirement and severance benefits decreased ¥11.5 billion, from ¥85.0 billion to ¥73.5 billion.

Total stockholders' equity increased ¥22.3 billion, from ¥553.9 billion to ¥576.2 billion. Retained earnings rose ¥34.9 billion, from ¥525.9 billion to ¥560.8 billion, while accumulated other comprehensive loss rose ¥11.6 billion, from ¥78.8 billion to ¥90.4 billion.

Research and development, patents and licenses, etc.

R&D expenditures amounted to ¥36.3 billion ($340 million), 5.5% of net sales in fiscal 2005; ¥32.9 billion, 5.0% of net sales in fiscal 2004; and ¥30.1 billion, 5.0% of net sales in fiscal 2003.

In its R&D activities, the group continues to work on strengthening and expanding development of new products that respond to diversification in the electronics market. In particular, the group is concentrating on next-generation recording-related products, micro electronics modules for mobile communications-related applications, and energy-efficient, environmentally friendly devices based on materials and design technologies. Furthermore, the group is using its reservoir of technologies to conduct efficient R&D activities concentrating in three strategic areas: IT home electronic appliances; high-speed and large-capacity networks and car electronics.

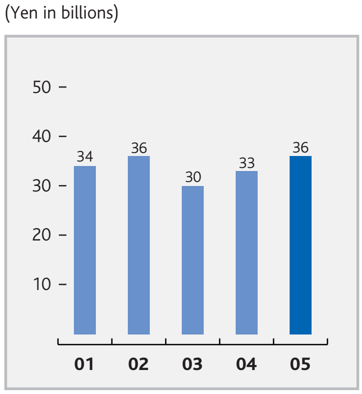
In the electronic materials and components field, development themes include commercialization of optimum ferrite materials for transformers and choke coils that possess both a high saturation magnetic flux density and a low core loss, commercialization of 100Gbpsi GMR heads for HDDs, development of next-generation magnetic recording technology and development of high-frequency-related components for mobile communications applications. In the recording media & systems field, the group has made progress with research on next-generation DVD-related products, including commercialization of Blu-ray discs. Furthermore, in EMC-related areas, which draw on the Company's materials technologies, the Company is working toward the commercialization of products designed for the increasingly higher frequencies used in electronic devices.

R&D at the Company is conducted by the Materials R&D Center, Advanced Process Technology Center, Devices Development Center, Production Engineering Development Center, Materials Analysis Center, Application Center, Silicon System Development Dept., New Business Development Dept. and the R&D functions of each operating group. Each facility is developing new products and technologies in its respective area of responsibility. The Application Center devises the necessary application technologies with the aim of keeping the Company in step with market trends and customer needs. The Materials R&D Center is responsible for research in magnetic and dielectric materials that use powder metallurgy. The Advanced Process Technology Center facilitates the use of cutting-edge process technologies. The Devices Development Center conducts research in next-generation recording and communications technologies as well as new devices.

In terms of overseas R&D activities, the Company is conducting R&D in collaboration with leading universities in the U.S. and U.K., and overseas R&D subsidiaries are making use of local technological resources. In China, where the Company is aiming to establish and develop an operating base capable of supporting growth, R&D activities are being carried out in the area of electronic components and materials. In addition, consolidated subsidiary Headway Technologies, Inc. is developing next-generation HDD heads.

Although the Company has a variety of patents in Japan and other countries, and licenses from other companies,

Research and Development
(Yen in billions)



it believes that expiration of any one of its patents or licenses or related group of patents or licenses would not materially adversely affect its business activities. Total income from patents and licenses was ¥0.5 billion ($5 million) in fiscal 2005, ¥0.1 billion in fiscal 2004 and ¥0.2 billion in fiscal 2003. The Company paid ¥9.3 billion ($87 million) in fiscal 2005, ¥8.1 billion in fiscal 2004 and ¥7.9 billion in fiscal 2003 for patents and licenses, mainly royalties for licenses related to the recording devices business. The Company does not believe that acquisition of new proprietary patents or other companies' patents would have a material effect on operating results in the future.

MARKET RISK MANAGEMENT

MARKET RISK EXPOSURE

The Company is subject to market risk associated with changes in stock prices, interest rates and foreign currency exchange rates. Foreign exchange risk is considered as the primary market risk exposure. The Company has a policy for the procedures and controls to manage market risk sensitive instruments. In order to hedge interest rate risk and foreign currency exchange rate risk, the Company uses derivative financial instruments. The Company does not hold or issue derivative financial instruments for trading purposes.

FOREIGN EXCHANGE AND INTEREST RATE RISK

Forward exchange contracts and currency swap contracts have been entered into to hedge adverse effects of foreign currency exchange rate fluctuations mainly on foreign-currency-denominated trade receivables and foreign-currency-denominated forecasted transactions.

At March 31, 2005 and 2004, the Company and certain of its subsidiaries had forward exchange contracts to sell and buy foreign currencies (principally U.S. dollars and Japanese Yen) and currency option contracts for a contract amount of ¥29.0 billion ($271 million) and ¥35.0 billion, respectively.

The Company and one of its subsidiaries have currency swaps and interest rate and currency swaps with certain financial institutions to limit their exposure to fluctuations in foreign exchange rates and interest rates involved mainly with loans made by the Company to its subsidiaries in a total amount of ¥11.1 billion ($103 million) and ¥12.6 billion at March 31, 2005 and 2004, respectively. These swaps require the Company and the subsidiary to pay principally euros and U.S. dollars and to receive Japanese yen at a specified rate on specific dates. The remaining term of these swaps is one month as of March 31, 2005.

The Company's exposure to market risk related to changes in interest rates relates primarily to its debt securities. The Company has debt securities with fixed rates. The Company, to the extent possible, plans to limit debt securities to short-term debt securities. The Company believes that the fair values of interest rate sensitive instruments as of March 31, 2005 and 2004, and potential, near-term losses affecting future earnings, fair values, and/or cash flows from reasonable near-term changes in interest rates are immaterial.

STOCK PRICE RISK

The Company's exposure to market risk involving changes in stock prices relates only to its equity securities categorized as available-for-sale securities. The Company purchases equity securities for the purpose of acquiring technological information and as part of its sales strategy, and not as a means of investing surplus funds. The aggregate cost and fair value of these equity securities were ¥6.0 billion ($56 million) and ¥7.0 billion ($65 million) as of March 31, 2005, and ¥2.8 billion and ¥3.8 billion as of March 31, 2004, respectively. As of March 31, 2005, these securities mainly represented investments in companies in the transportation, communications and electronic equipment industries, and the cost and fair value of these equity securities were ¥5.6 billion ($53 million) and ¥6.5 billion ($61 million), respectively. As of March 31, 2004, these securities mainly represented investments in companies in the communications and electronic equipment industries, and the cost and fair value of the equity securities were ¥2.4 billion and ¥3.3 billion, respectively.

CRITICAL ACCOUNTING POLICIES

Critical accounting policies are those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

The following is not intended to be a comprehensive list of all of the Company's accounting policies. The Company's significant accounting policies are more fully described in Note 1 to the Consolidated Financial Statements. In many cases, the accounting treatment of a particular transaction is specifically dictated by U.S. generally accepted accounting principles, with no need for management's judgment in their application. There are also areas in which management's judgment in selecting an available alternative would not produce a materially different result.

The Company has identified the following as critical accounting policies: impairment of long-lived assets, valuation of inventories, goodwill and other intangible assets, pension benefit costs, and deferred tax assets.

IMPAIRMENT OF LONG-LIVED ASSETS

As of March 31, 2005 and 2004, the aggregate of the Company's property, plant and equipment and amortized intangible assets was ¥229.6 billion and ¥223.1 billion, which accounted for 28.4% and 29.0% of the total assets, respectively. The Company believes that impairment of long-lived assets are critical to the Company's financial statements because the recoverability of the amounts or lack thereof, could significantly affect its results of operations.

The Company's long-lived assets and certain identifiable intangibles are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. This review is performed using estimates of future cash flows. If the carrying amount of the asset is considered to be impaired, an impairment charge is recorded for the amount by which the carrying value of an asset exceeds its fair value. Management believes that the estimates of future cash flows and fair values are reasonable; however, changes in estimates resulting in lower future cash flows and fair value due to unforeseen changes in business assumptions could negatively affect the valuation of those long-lived assets and significantly affect the Company's financial position and results of operations. These unforeseen changes include a possible further decline in demand and price for optical media products due to a shift in demand from CD-Rs to DVD related products including Blu-ray discs. The Company makes investments with due prudence, taking sufficiently into consideration the future profitability of products and the recoverability of investments.

VALUATION OF INVENTORIES

Inventories are stated at the lower of cost or market, with cost determined on the average cost method. The carrying value of inventory is reduced for estimated obsolescence by the difference between its cost and the estimated market value based upon assumptions about future demand. The Company evaluates the inventory carrying value for potential excess and obsolete inventory exposures by analyzing historical and anticipated demand. In addition, known and anticipated engineering change orders are evaluated against on-hand quantities for their potential obsolescence affects. As fluctuations in estimates, which become a standard in recognizing adjustments in the carrying values of inventory for expected obsolescence, are influential to business results of the Company, we conclude it as a critical accounting policy. If actual demand were to be substantially lower than estimated, additional inventory adjustments for excess or obsolete inventory may be required, which could have a material adverse effect on the Company's business, financial condition and results of operations.

Regarding the appropriateness of estimates in the past, the Company does not take a method to assume various scenarios, but a method to reconsider every quarter by comparing estimate and actual results. For example, in the operation management of product sector with rapid development in technological innovation such as the recording devices sector, the Company revises the estimates of valuation of obsolete inventories arising from the timely response to customers' demands for high-efficiency products on a quarterly basis.

GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets that are determined to have an indefinite life are not amortized and are tested for impairment on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of these assets below their carrying amount. Fair value for these assets is determined using a discounted cash flow analysis, which is based on an authorized business plan. Management believes that the estimates of future cash flows and fair value are reasonable; however, changes in estimates resulting in lower future cash flows and fair value due to unforeseen changes in business assumptions could negatively affect the valuations.

PENSION BENEFIT COSTS

Employee pension benefit costs and obligations are dependent on assumptions used by actuaries in calculating such amounts. These assumptions include discount rates, retirement rates and mortality rates which are based upon current statistical data, as well as salary growth, long-term return on plan assets and other factors. Actual results that differ from the assumptions are accumulated and amortized over future periods and, therefore, generally affect the Company's recognized expense and recorded obligation in future periods. While the Company believes that its assumptions used are appropriate, differences in actual experience or changes in assumptions may affect the Company's benefit obligations and future expense.

In preparing its financial statements for fiscal 2005, the Company established a discount rate of 2.1% and an expected long-term rate of return of 2.2% on plan assets. In estimating the discount rate, the Company uses available information about rates of return on long-term risk free governmental and corporate bonds currently available and expected to be available during the period to the maturity of the pension benefits. The Company established the expected long-term rate of return on plan assets based on management's expectations in respect of the long-term returns of the various plan asset categories in which it invests. Management developed expectations with respect to each plan asset category based on actual historical returns and its current expectations for future returns.

A decrease in the discount rate leads to an increase in actuarial pension benefit obligations that could lead to an increase in net periodic pension cost through amortization of unrecognized actuarial gain or losses. A 50 basis point decrease in the discount rate would increase the projected benefit obligation by approximately 10%.

An increase in the expected return on plan assets may decrease net periodic pension cost in the current year. For fiscal 2005, a 50 basis point decrease in the long-term rate of return would increase net benefit cost by approximately ¥0.7 billion. However, the difference between the expected return and the actual return on those assets could negatively affect net income in future years.

DEFERRED TAX ASSETS

The Company has significant deferred tax assets, which are subject to realizability assessment. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the planned reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes that it is more likely than not that all of the deferred tax assets less valuation allowance, will be realized. However, in the event future projections for income are not realized or are realized in lesser amounts, or in cases where management revises the assessment of the potential for realization of deferred tax assets based on other factors, deferred tax assets may be determined not to be realizable, which then would require the Company to increase a valuation allowance against the deferred tax assets resulting in additional income tax expenses.

New Accounting Standards

In March 2004, the Emerging Issues Task Force reached a consensus on Issue 03-1 ("EITF 03-1"), "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments". EITF 03-1 provides guidance on other-than-temporary impairment models for marketable debt and equity securities accounted for under Statement of Financial Accounting Standards No. 115 ("SFAS 115"), "Accounting for Certain Investments in Debt and Equity Securities", and nonmarketable equity securities accounted for under the cost method. The EITF developed a basic three-step model to evaluate whether an investment is other-than-temporarily impaired. The FASB issued a FASB Staff Position EITF 03-1-1 in September 2004 which delayed the effective date of the recognition and measurement provisions of EITF 03-1. The adoption of EITF 03-1 is not expected to have a material effect on the Company's consolidated results of operations and financial position.

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123 (revised 2004), "Share Based Payment" ("SFAS 123R"). SFAS 123R is a revision of SFAS 123, "Accounting for Stock Based Compensation", and supersedes APB 25. SFAS 123R requires the Company to measure the cost of employee services received in exchange for equity awards based on the grant date fair value of the awards. The cost will be recognized as compensation expense over the vesting period of the awards. In April 2005, the Securities and Exchange Commission deferred the effective date of SFAS 123R to the beginning of the first annual period after June 15, 2005. The Company is currently evaluating the effect that the adoption of SFAS 123R will have on the Company's consolidated financial position and results of operations.

In November 2004, the FASB issued Statement of Financial Accounting Standards No. 151 ("SFAS 151"), "Inventory Costs – an amendment of Accounting Research Bulletin No. 43 ("ARB 43"), Chapter 4". SFAS 151 amends the guidance in ARB 43, Chapter 4, "Inventory Pricing", to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). SFAS 151 requires that items such as idle facility expense, excessive spoilage, double freight and rehandling costs be recognized as current-period charges regardless of whether they meet the criterion of "so abnormal" as stated in ARB 43. In addition, SFAS 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS 151 is effective for inventory costs incurred in fiscal periods beginning after June 15, 2005. The Company does not expect the adoption of SFAS 151 to have a material effect on the Company's consolidated financial position and results of operations.

Forward-Looking Statements

This report contains forward-looking statements, including projections, plans, policies, management strategies, targets, schedules, understandings and evaluations, about the Company and its subsidiaries that are not historical facts. These forward-looking statements are based on current forecasts, estimates, assumptions, plans, beliefs and evaluations in light of information available to management on the date of this report was prepared.

In preparing forecasts and estimates, the Company and its subsidiaries have used as their basis, certain assumptions as necessary, in addition to confirmed historical facts. However, due to their nature, there is no guarantee that these statements and assumptions will prove to be accurate in the future. The Company therefore wishes to caution readers that these statements, facts and certain assumptions contained in this report are subject to a number of risks and uncertainties and may prove to be inaccurate.

The electronics markets in which the Company and its subsidiaries operate are highly susceptible to rapid changes. Furthermore, the Company and its subsidiaries operate not only in Japan, but in many other countries. As such, factors that can have significant effects on its results include, but are not limited to, shifts in technology, demand, prices, competition, economic environments and foreign exchange rates.

SEGMENT INFORMATION

The following industry and geographic segment information is required by the Japanese Securities Exchange Law. Segment information is unaudited.

Industry Segment Information

	Yen (Millions)				U.S. Dollars (Thousands)		
Years ended March 31	**2005**		2004		**2005**		Change (%)
ELECTRONIC MATERIALS AND COMPONENTS							
Net sales							
Unaffiliated customers	**¥545,214**		519,792		**$5,095,458**		4.9
Intersegment	**–**		–		**–**		
Total revenue	**545,214**	**(100.0%)**	519,792	(100.0%)	**5,095,458**	**(100.0%)**	4.9
Operating expenses	**477,694**	**(87.6%)**	461,077	(88.7%)	**4,464,430**	**(87.6%)**	3.6
Operating income	**¥ 67,520**	**(12.4%)**	58,715	(11.3%)	**$ 631,028**	**(12.4%)**	15.0
Identifiable assets	**537,593**		505,178		**5,024,233**		
Depreciation and amortization	**47,409**		46,293		**443,075**		
Capital expenditures	**57,192**		40,084		**534,505**		
RECORDING MEDIA & SYSTEMS							
Net sales							
Unaffiliated customers	**¥112,639**		136,000		**$1,052,701**		–17.2
Intersegment	**–**		–		**–**		
Total revenue	**112,639**	**(100.0%)**	136,000	(100.0%)	**1,052,701**	**(100.0%)**	–17.2
Operating expenses	**120,329**	**(106.8%)**	138,205	(101.6%)	**1,124,570**	**(106.8%)**	–12.9
Operating income (loss)	**¥ (7,690)**	**(–6.8%)**	(2,205)	(–1.6%)	**$ (71,869)**	**(–6.8%)**	–248.8
Identifiable assets	**84,160**		97,186		**786,542**		
Depreciation and amortization	**5,397**		4,433		**50,439**		
Capital expenditures	**3,813**		4,387		**35,635**		
ELIMINATIONS AND CORPORATE							
Corporate assets	**¥186,248**		167,955		**$1,740,636**		
TOTAL							
Net sales							
Unaffiliated customers	**¥657,853**		655,792		**$6,148,159**		0.3
Intersegment	**–**		–		**–**		
Total revenue	**657,853**	**(100.0%)**	655,792	(100.0%)	**6,148,159**	**(100.0%)**	0.3
Operating expenses	**598,023**	**(90.9%)**	599,282	(91.4%)	**5,589,000**	**(90.9%)**	–0.2
Operating income	**¥ 59,830**	**(9.1%)**	56,510	(8.6%)	**$ 559,159**	**(9.1%)**	5.9
Identifiable and corporate assets	**808,001**		770,319		**7,551,411**		
Depreciation and amortization	**52,806**		50,726		**493,514**		
Capital expenditures	**61,005**		44,471		**570,140**		

Note: In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", certain amounts in the segment information do not reflect discontinued operations, fiscal 2004's segment information has been reclassified to conform to the fiscal 2005 presentation.

Geographic Segment Information

Years ended March 31	Yen (Millions) 2005	2004	U.S. Dollars (Thousands) 2005	Change (%)
JAPAN				
Net sales	**¥339,493**	329,782	**$3,172,832**	2.9
Operating income	**26,382**	8,538	**246,561**	209.0
Identifiable assets	**305,717**	316,695	**2,857,168**	–3.5
AMERICAS				
Net sales	**87,594**	100,971	**818,636**	–13.2
Operating income	**5,496**	4,985	**51,364**	10.3
Identifiable assets	**70,844**	65,584	**662,093**	8.0
EUROPE				
Net sales	**71,682**	80,641	**669,925**	–11.1
Operating income (loss)	**(5,125)**	(115)	**(47,897)**	–
Identifiable assets	**44,961**	51,797	**420,196**	–13.2
ASIA AND OTHERS				
Net sales	**400,866**	380,781	**3,746,411**	5.3
Operating income	**33,551**	42,912	**313,561**	–21.8
Identifiable assets	**263,621**	228,058	**2,463,748**	15.6
ELIMINATIONS AND CORPORATE				
Net sales	**241,782**	236,383	**2,259,645**	
Operating income (loss)	**474**	(190)	**4,430**	
Identifiable assets	**122,858**	108,185	**1,148,206**	
TOTAL				
Net sales	**¥657,853**	655,792	**$6,148,159**	0.3
Operating income	**59,830**	56,510	**559,159**	5.9
Identifiable and corporate assets	**808,001**	770,319	**7,551,411**	4.9

Overseas Sales	Yen (Millions) 2005		2004		U.S. Dollars (Thousands) 2005		Change (%)
Americas	**¥ 77,813**	**(11.8%)**	88,734	(13.5%)	**$ 727,224**	**(11.8%)**	–12.3
Europe	**71,702**	**(10.9%)**	80,710	(12.3%)	**670,112**	**(10.9%)**	–11.2
Asia and others	**324,313**	**(49.3%)**	317,725	(48.5%)	**3,030,963**	**(49.3%)**	2.1
Overseas sales total	**¥473,828**	**(72.0%)**	487,169	(74.3%)	**$4,428,299**	**(72.0%)**	–2.7

Note: In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", certain amounts in the segment information do not reflect discontinued operations, fiscal 2004's segment information has been reclassified to conform to the fiscal 2005 presentation.