

August 11, 2003

## ***PALTEK CORPORATION***



### **Summary of Financial Statements for the term ended June 30, 2003 (UNAUDITED)**

NOTES:

All information has been prepared in accordance with generally accepted accounting principles in Japan. Amounts shown in this accounting report and in the attached material have been rounded down to omit fractions less than one thousand yen. This document is an English translation of the Japanese Financial Statement (Kessan Tanshin) which was filed at stock exchanged in Japan on August 11, 2003.

Company Name	: PALTEK CORPORATION	Head Office	: Kanagawa, Japan
Security Code No	: 7587	URL	: <a href="http://www.paltek.co.jp">http://www.paltek.co.jp</a>
Representative	: Tadahito Takahashi, President		
Contact	: Tadashi Ito, Director, General Manager of Operational Service Division and Environment		
Telephone	: +81-45-477-2000		
Date of Board of Directors' Meeting	: August 11, 2003		
US GAAP	: Not adopted		

## Interim Kessan Report for the December 2003 Term (Consolidated)

August 11, 2003

**PALTEK CORPORATION**

Security code number: 7587 (URL <http://www.paltek.co.jp>)  
 Shares traded: JASDAQ  
 Location of headquarters: Kanagawa  
 Name & Executive position of legal representative: Tadahito Takahashi  
 President  
 Please address all communications to: Tadashi Ito, Director, General Manger of  
 Operational Service Division and Environment  
 Phone: (045) 477-2000

Date of Board of Directors' meeting for approval  
 of interim financial results: August 11, 2003  
 Adoption of U.S. accounting standards: None

**1. Consolidated operating results** (From January 1, 2003 to June 30, 2003)**(1) Consolidated financial results**

(In millions of yen, with fractional amounts discarded)

	Net sales		Operating income		Ordinary income	
	(Millions of yen)	%	(Millions of yen)	%	(Millions of yen)	%
June 30, 2003	8,817	39.9	614	162.1	626	82.1
June 30, 2002	6,304	(37.4)	234	(54.8)	343	(24.4)
December 31, 2002	15,614		660		762	

	Net income		Net income per share	Net income per share, fully diluted
	(Millions of yen)	%	(Yen)	(Yen)
June 30, 2003	323	(16.4)	27.34	-
June 30, 2002	386	505.9	32.68	-
December 31, 2002	21		1.83	-

## (Notes)

- Equity in earnings (losses) of associated companies:  
 June 2003 interim term: -  
 December 2002 term: (7) million yen  
 June 2002 interim term: (0) million yen
- Average number of shares outstanding during term (consolidated basis):  
 June 2003 interim term: 11,835,925 shares  
 June 2002 interim term: 11,837,843 shares  
 December 2002 term: 11,837,280 shares
- Changes in accounting policy: None
- The percentages shown next to net sales, operating income, ordinary income and net income represent year-on-year changes.

**(2) Consolidated financial position**

	Total assets	Shareholders' equity	Shareholders' equity ratio	Shareholders' equity per share
	(Millions of yen)	(Millions of yen)	%	(Yen)
June 30, 2003	11,981	8,115	67.7	685.72
June 30, 2002	11,561	8,275	71.6	699.12
December 31, 2002	11,723	7,901	67.4	667.57

(Note) Number of shares issued and outstanding at the end of term (consolidated):  
 June 2003 interim term: 11,835,656 shares      June 2002 interim term: 11,837,126 shares  
 December 2002 term: 11,836,272 shares

**(3) Consolidated cash flows**

	Net cash from operating activities	Net cash from investing activities	Net cash from financing activities	Cash and cash equivalents at end of term
	(Millions of yen)	(Millions of yen)	(Millions of yen)	(Millions of yen)
June 30, 2003	246	(118)	196	1,465
June 30, 2002	759	57	(360)	2,058
December 31, 2002	(343)	94	(211)	1,141

**(4) Scope of consolidation and application of the equity method**

Number of consolidated subsidiaries: 3

Number of non-consolidated subsidiaries accounted for by the equity method: —

Number of associated companies accounted for by the equity method: —

**(5) Changes in scope of consolidation and in application of the equity method**

Consolidation (new): —      (elimination): —

Equity method (new): —      (elimination): 1

**2. Consolidated forecasts for December 2003 term**

(From January 1, 2003 to December 31, 2003)

	Net sales	Operating income	Ordinary income	Net income
	(Millions of yen)	(Millions of yen)	(Millions of yen)	(Millions of yen)
Annual	17,600	1,118	1,095	563

(N.b.) Projected net income per share for fiscal 2003: 47.57 yen

*The above projections represent our estimates based on information available as of the date of publication of these materials, and therefore actual results may differ substantially from the above figures. Please refer to page 12 of the attachment for assumptions and other matters related to the projections.*

## Group organization

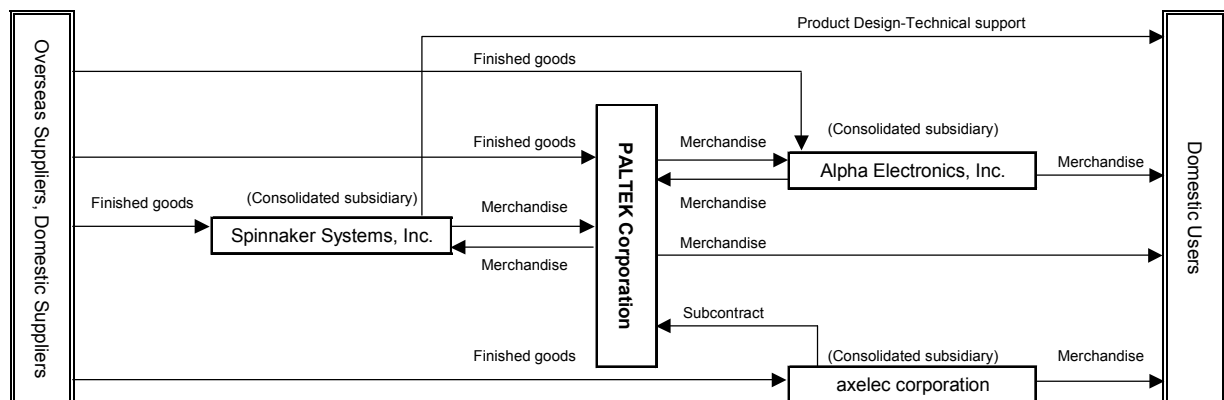
The PALTEK group’s primary business activities are the distribution of semiconductors and design software used in electronics equipment, as well as design support services. The structure of the group and the business relationships among the group companies are illustrated in the diagram below.

In March 2003, PALTEK and MARUBUN Corporation canceled their March 2002 agreement for the joint operation of axelec corporation. PALTEK has since assumed full control of those operations. Separately, HYPER-PALTEK Corporation was disbanded at the end of June 2003 and is being liquidated.

Business segment	Business description	Main companies
Semiconductors and related business	Design, development and sales of semiconductor-related products; design-technology support	PALTEK Corporation (PALTEK) Alpha Electronics Inc. (Alpha Electronics) Spinnaker Systems, Inc. (Spinnaker Systems) axelec corporation (axelec)

(Note)

The “Other” category of business, which appeared in reports through the consolidated fiscal year to December 2002, has been omitted from this interim report because HYPER-PALTEK Corporation, the principal component of this category, has been dissolved and is no longer in business.



(Note) axelec corporation has been a dormant company since April 2003.

## **Management policy and operating results**

### Management policy

#### **1. Basic management policies**

Guided by a philosophy of “symbiosis with diverse partners,” the PALTEK group is seeking to create significant social value for all stakeholders in the Company, including customers, suppliers, employees and shareholders.

To achieve this goal, we believe that the Company’s primary mission must be to provide high-value-added solutions to those involved in developing electronic devices. We are fully confident that, through the skillful application of our own unique marketing methods, our partners will be able to develop devices that are competitive in the global marketplace.

By focusing on high-value-added solutions, we seek to achieve three goals: to position the PALTEK group as a “strategic partner in the development of electronic devices”; to develop into a major player in the networked economy; and to contribute to society across a broad range of areas.

#### **2. Basic policy regarding the distribution of profits**

The PALTEK group recognizes that one of management’s primary concerns is to provide value to shareholders and investors. Accordingly, the Company’s basic policy on dividends will be to continue to make payouts that are appropriate in light of its needs to build a stable operating foundation and to finance future business initiatives. It will do so while endeavoring to enhance its financial performance and profit margins, and while taking steps to sustain profitable operations and to build a strong base of retained earnings.

#### **3. Targeted financial ratios**

Another goal of the PALTEK group will be to provide high-value-added solutions to our customers through a highly efficient operating structure. To assure our ability to achieve this goal, we are aiming to sustain a high ratio of operating income to sales. Over the medium term, our target in this regard is to achieve consolidated sales of 50 billion yen and an operating margin of 10%.

#### **4. Medium- to long-term management strategies**

The PALTEK group’s longer term goals are to transcend the framework of the traditional semiconductor trading company and to provide solutions that rely both on greater versatility and a high level of technological sophistication, which will enable us to support technological development and technology applications. Another focus will be to continue to introduce to Japanese electronic device manufacturers outstanding technologies and products that are being developed by a newly emerging group of venture-capital firms in Japan, in addition to various

technologies and products that are currently unavailable in Japan. In instances where new technologies or markets are not yet established, we will take on a marketing role on behalf of the company with the technology and work to increase product recognition and build a customer base in Japan. Our involvement in these activities has resulted in the creation of a new business model, in which the trading company becomes a participant in technology development. This partnering approach has been a hallmark of the Company since its founding, and is reflected in the motto “solutions supplier” that companies in the group have stressed in their operations. Not only has this approach been greatly appreciated by our customers, but it is also gaining significant support among our suppliers. Therefore, as consumers’ needs grow increasingly complex in the future, we believe that the PALTEK group’s presence will become increasingly vital to both customers and suppliers.

At the same time, our business model must continue to evolve in a rapidly changing market environment. In addition to existing suppliers, we are actively promoting cooperative business arrangements with new partners who own promising new technologies. But anticipating consumer needs and developing new demand in conjunction with business partners will require technological competence. We will therefore continue to invest in the human resources that can provide us with such competence.

Today, the electronic device industry is increasingly shifting its manufacturing and product development base to Asia, which threatens to erode technological capabilities in Japan and create a potentially difficult market environment. In response, customers of the PALTEK group are taking on the challenge of creating new added value through the development of high value-added electronic devices. While continuing to provide solutions to such customers, we will endeavor to develop new customer bases in various growth areas, including broadcasting, consumer electronics and industrial equipment. The group will also construct a new semiconductor-based business model, which will aim at establishing cooperative operations with high-tech venture companies.

## **5. Issues requiring action**

The following concrete issues will require action in light of the foregoing strategies.

During the interim period to June 2003, the Company established a Corporate Marketing Division to deal with these issues and to promote efforts to achieve management targets. The new division creates an ability to integrate information from various sources throughout the organization and to coordinate direction at the operating level, thus strengthening group-wide synergies.

### **(1) Obtaining innovative technologies and expanding and deepening the product line**

The group will need to consider customer requirements from a comprehensive perspective and obtain promising and innovative technologies that are capable of creating new markets. It

will also have to expand and deepen its product line. To achieve these goals, it will be essential that the Company hire or train outstanding researchers and engineers. It will search around the world to identify these researchers and take active steps to hire the required talent.

The PALTEK group entered into four new distributorship agreements during the interim period to June 2003. Its efforts to build the capabilities required to offer total solutions will continue going forward.

(2) Developing creative and high-value-added services and building new business models

The group must also transcend the framework of the traditional trading company and construct new business models. This will require that it provide creative and high value-added solutions. To do so, it must seek out partners from around the world and actively pursue cooperative ventures.

One model for cooperation may lie in applying the Company's unique marketing capabilities to the tasks of selling and marketing products developed by technology-based venture-capital firms. Selling and marketing are a common bottleneck to growth for such companies. In the field of security, the Company entered into an operational alliance with Trinity Security Systems Inc. ("Trinity") in January 2003. This agreement calls for the Company to provide Trinity (the partner *as customer*) with product development support, while the Company also sells products that it procures from Trinity (the partner *as supplier*).

In August 2003, Spinnaker Systems, Inc., one of the subsidiaries of PALTEK, purchased shares in IPFlex, Inc. and entered into a distributorship agreement with that company. PALTEK believes that IPFlex offers potentially large synergies with the technologies and experience that it has accumulated. IPFlex has developed an ultra-high-performance reconfigurable processor technology, based on the brand new concept of instantaneously changing hardware in accordance with application and doing so in a flexible and dynamic way. Compared with existing semiconductors, the IPFlex technology offers more rapid processing speeds and lower power consumption in advanced applications. We believe that this technology will enable users to take the initiative in dealing with today's manufacturing constraints; i.e., the increasing variety of product specifications and standards, the need for production of many varieties in small volumes, and shorter life cycles.

(3) Strengthening the Company's operating foundations and improving management capabilities

The group is endeavoring to strengthen its operating base in order to continue to generate profits amid turbulent change and uncertainty in the market environment. Toward that end, each company in the corporate group is taking steps to increase its operational efficiency and to improve other aspects of managerial capability.

The PALTEK group has designated the first year following its 20<sup>th</sup> anniversary term as a period for reviewing its various operations. During the interim period to June 2003, it revived its founding principles of management and reviewed current operational practices from the perspective of its management philosophy. The group is aiming to integrate everyday activities around a common philosophy and, on this basis, to create more effective and efficient operations.

## **6. Basic philosophy regarding corporate governance and corporate governance-related policies**

(1) The PALTEK group views corporate governance as a managerial control aimed at maximizing corporate value for all stakeholders and at putting its philosophy of symbiosis into practice. Its basic aim for corporate governance is to “respond rapidly to changes in the market environment and to enhance the transparency of management.” In light of this policy, the PALTEK group has established the following system of governance.

### **a. Composition of Board of Directors and Board of Corporate Auditors**

The Company’s Board of Directors is structured with the aim of providing more effective and appropriate solutions to customers. Accordingly, members of the board bring to their jobs not only advanced technical knowledge but also varied perspectives and experiences, which are derived from their varied backgrounds as former customers of the firm or members of other industries. To further enhance transparency and assure greater objectivity in governance, one highly experienced outside director (of a total board of six directors) has been elected to the board.

The Company has adopted a system of corporate auditors. The composition of the board of corporate auditors reflects the importance that has been attached to establishing its independence from the Board of Directors, as three of the board’s four members are highly experienced persons from outside the firm.

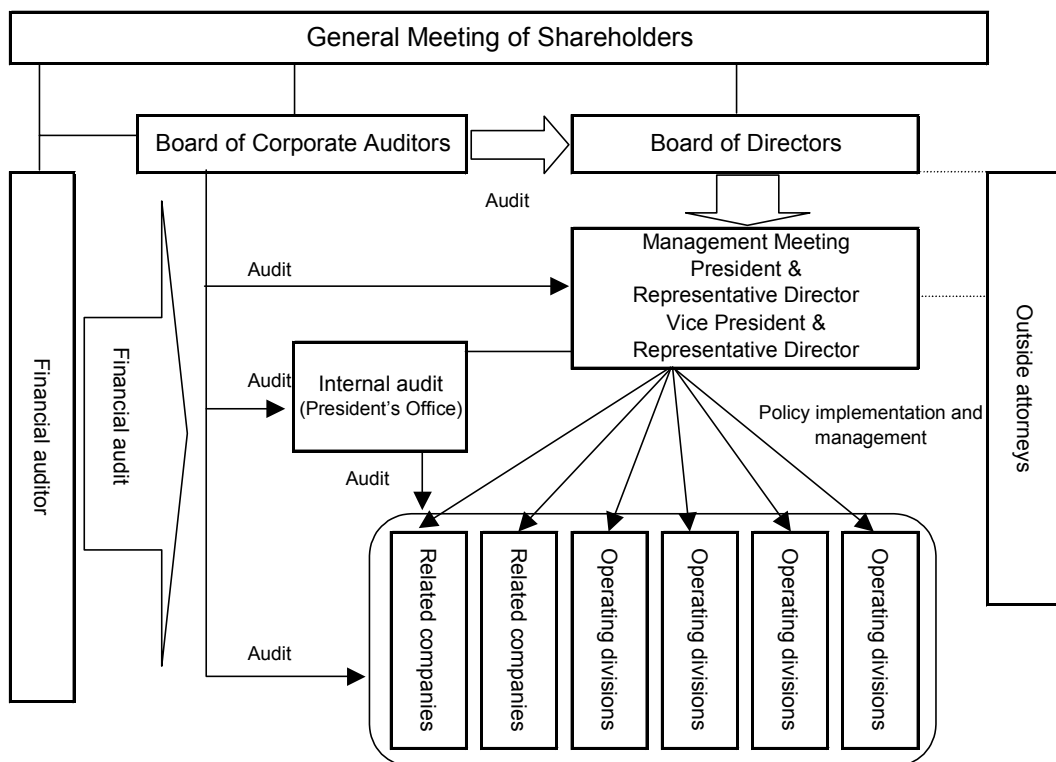
PALTEK is not linked to its outside director or its outside auditors by any special ties, including control over job assignments, financial ties, technology-related ties or business ties.

### **b. Operational execution and oversight**

Each month, the companies in the PALTEK group hold management meetings attended by directors, the heads of the respective divisions, and the chief executives of group companies. The purpose of the meetings is to provide a means for quickly resolving the issues faced by each division and for making management decisions from a more all-embracing standpoint. The meetings are attended by the standing statutory auditor and by outside corporate auditors, who express their opinions and make reports when appropriate. Policy management is used to assure that policies adopted at management

meetings are implemented throughout the organization. And by holding Board of Directors' meetings on the same day as management meetings, the system is set up to encourage rapid judgments on important managerial issues.

In addition to these regularly scheduled meetings, the Company convenes meetings on an ad hoc basis, whenever required. The ability to meet in this way enables the Company to digest information rapidly and to link this information to rapid decision-making and action. In this way, the PALTEK group is endeavoring to respond flexibly to a rapidly and unpredictably changing market situation.



c. Internal controls

To enhance the overall quality of management, the Company has also established a mechanism for internal audits, which are conducted by the staff of the President's Office acting on behalf of the president. Through this mechanism, the Company endeavors to maintain continuous improvement in all of the Company's activities and systems, including general operations. Assessing reasonableness and efficiency, the staff reviews such activities and systems in light of management objectives, and offers evaluations, suggestions and guidance from an impartial standpoint.

d. Involvement of attorneys and CPAs

Attorneys advise the Company on issues of compliance. In addition to biannual financial audits by outside auditing firms, the Company also consults with CPAs at appropriate times on issues of accounting.

(2) Specific actions taken during the past year to improve corporate governance

a. Strengthening adaptability to change and improving crisis management capabilities

In January 2003, Director Hiroyuki Takasaki was elected Vice President and Representative Director. Mr. Takasaki's appointment was designed to enhance the group's ability to make rapid management decisions in response to future changes in the operational environment and to strengthen its crisis management capabilities. In other actions, we enhanced our ability to audit operations from a wider variety of perspectives by electing an additional outside auditor to the four-person Board of Corporate Auditors. The newest appointee, who assumed office from the current term, brings to the board substantial experience in semiconductor manufacturing and in developing related ventures. The appointment also fits in with our long-standing policy of selecting persons to the Board of Auditors who have substantial experience outside the Company.

b. Strengthening a sense of responsibility to shareholders

With respect to General Shareholders' Meetings, a number of steps have been taken to enhance shareholder convenience. Since the General Meeting for the year to December 2001, our shareholders have had the option of exercising their voting rights via the Internet. We have also changed the day of our meetings to Saturdays to facilitate participation by more shareholders from different walks of life. Meeting content has also been a focus of attention. Our approach is not only to run our meetings in accordance with agendas that are appropriate to a consolidated entity, but also to emphasize aggressive information disclosure and feedback from shareholders. Toward this end, we have begun holding company information meetings in conjunction with the shareholder meetings.

We have established a "directors' stock holding system" from the current fiscal year, which is designed to provide performance-based incentives and to instill a sense of responsibility for results.

Our grants of stock options to employees have had as their aim "establishing linkages with shareholder profitability" and "enhancing a sense of participation in management." However, given recent conditions in the equity markets and the level of the Company's share price, and considering the potential impact of options on existing shareholder value, we have concluded that they are not an optimal approach to compensation under current conditions. Consequently, we will be terminating all further grants of options to employees

in the current fiscal year. In place of options, we will be increasing incentives for employees to purchase the Company's stock and endeavoring to realize the foregoing objectives through stock purchasing plans.

(7) Other important issues related to company management

There are no other important issues to report related to the company's management.

## Financial Performance

### 1. Overview of the six-month period to June 30, 2003

(1) Operating results

The Japanese economy produced little that warranted confidence in a strong recovery during the six-month period ended June 30, 2003. Amid global instability caused by the Iraq war and the SARS epidemic, the situation in Japan remained bleak as the government seemed hamstrung in terms of economic policy options, and domestic demand continued to falter. On the other hand, in the data communications sector, the results of the major electrical device manufacturers bottomed out in the fiscal year to March 2003 and showed hints of a recovery. Much of this apparent upswing, however, was due to improvements in corporate finances and it remains to be seen whether a genuine recovery in sales of major product lines is in the offing.

Against this background, the PALTEK group endeavored to expand sales by making proposals in relatively healthy sectors of the industry. By working to establish relationships with new customers and by responding to customer needs by aggressively introducing new products, it endeavored to maintain and expand sales and profits. In terms of specific product areas, sales of its mainstay programmable logic devices to manufacturers of broadcasting equipment for ground station digital broadcasting, and to producers of other industrial equipment, were strong. Rapidly expanding applications for PLDs enabled the group to actively propose the technology to new customers. In the area of analog devices, the group benefited from its close relationships with customers and increased its sales in response to continuing strong demand for portable phones and digital cameras.

Consequently, net sales for the interim period ended June 30, 2003 increased by 39.9% to 8,817 million yen, while ordinary income increased by 82.1% to 626 million yen. Net income for the interim period declined by 16.4% to 323 million yen.

(2) Cash flow

During the six-month period ended June 2003, cash and cash equivalents increased by 324 million yen compared with balances at the end of the fiscal year to December 2002.

Consequently, as of the end of the interim period to June 2003, cash and cash equivalents stood at 1,465 million yen.

The various components of cash flow during the interim period and factors affecting increases or decreases are summarized below.

***(Net cash from operating activities)***

Cash provided by operations amounted to 246 million yen (a decrease of 67.5% year-on-year). This reflected an increase of 617 million yen in interim net profit before taxes and other adjustments, which offset an increase in inventories and a decrease in trade payables.

***(Net cash from investing activities)***

Cash used in investment activities amounted to 118 million yen (compared with 57 million yen cash provided in the year-earlier period). This reflected expenditures for the acquisition of investment and marketable securities and of shares in related companies.

***(Net cash from financing activities)***

Cash provided by financing activities amounted to 196 million yen (compared with 306 million yen in cash used in the year-earlier period). This reflected an increase in borrowings, which offset payments of dividends.

Trends in cash flow-related indices for the corporate group are shown below.

	June 30, 2002	June 30, 2003	December 31, 2002
Equity ratio	71.6%	67.7%	67.4%
Equity ratio based on market prices	58.9%	72.4%	41.6%
Years required to redeem liabilities	0.9 years	3.9 years	-
Interest-coverage ratio	72.4 times	21.3 times	-

*(Notes)*

1. *Equity ratio: Shareholders' equity/total assets*

2. *Equity ratio based on market prices: Market capitalization/total assets*

3. *Years required to redeem liabilities: Interest-bearing liabilities/operating cash flow*

4. *Interest-coverage ratio: Operating cash flow/interest payments*

(1) *Each of the foregoing ratios is calculated on the basis of consolidated financial data.*

(2) *"Market capitalization" is calculated by multiplying the share price on the final day of the fiscal year by the number of shares outstanding on the same day.*

(3) *For "operating cash flow," we use the figure for "cash flow from operations" in the consolidated statement of cash flows. "Interest-bearing liabilities" refers to all liabilities on the consolidated balance sheet on which interest payments are made. For "interest payments," we use the figure for "interest expenses" in the consolidated statement of cash flows.*

(4) *In the 2002 fiscal year, "years required to redeem liabilities" and "interest-coverage ratio" are not shown because cash flow from operations was negative.*

## **2. Outlook for the year ending December 2003**

Although stock prices have recovered rapidly since the beginning of June, it is not yet clear whether the recovery will be strong enough to become an engine for the real economy. On the other hand, in the data communications sector, manufacturers continue to put off capital spending, suggesting that economic recovery may not be imminent.

Given this environment, the PALTEK group will seek to contribute to the development of the PLD business by expanding its customer base in response to widening applications of the technology. At the same time, the group will endeavor to create a new model based on PLD. Additionally, in order to provide a wider range of systems solutions in newly emerging markets that integrate consumer electronics with computers and telecommunications equipment, the group will continue to search for the next new budding technology while it develops the products that were newly acquired in the first half of the fiscal year.

On the basis of these activities, the group is forecasting the following results for the fiscal year to December 2003: net sales of 17.6 billion yen; operating income of 1,118 million yen; ordinary income of 1,095 million yen; and net income of 563 million yen. On a parent company basis, PALTEK is forecasting net sales of 14,313 million yen, operating income of 1,044 million yen, ordinary income of 1,042 million yen, and net income of 549 million yen.

**Consolidated balance sheet**

Thousands of yen	June 30, 2002	%	June 30, 2003	%	December 31, 2002	%
<b>Current assets</b>						
Cash and bank deposits	2,095,115		1,501,927		1,187,549	
Notes and accounts receivable	3,286,623		4,602,611		4,670,434	
Inventories	3,020,790		3,634,428		3,411,841	
Deferred tax assets	719,813		622,850		368,490	
Others	480,846		349,730		584,477	
Allowance for doubtful accounts	(3,036)		(7,920)		(7,382)	
	<u>9,600,153</u>	83.0	<u>10,703,628</u>	89.3	<u>10,215,410</u>	87.1
<b>Fixed assets</b>						
<b>Tangible fixed assets</b>						
	284,891	2.5	204,663	1.7	241,028	2.1
<b>Intangible fixed assets</b>						
Goodwill	672,019		23,725		39,509	
Others	242,100		190,543		212,987	
	<u>914,120</u>	7.9	<u>214,268</u>	1.8	<u>252,496</u>	2.1
<b>Investments and other assets</b>						
Investment securities	181,168		223,553		142,266	
Others	634,129		644,117		937,960	
Allowance for doubtful accounts	(53,302)		(8,346)		(65,868)	
	<u>761,994</u>	6.6	<u>859,324</u>	7.2	<u>1,014,357</u>	8.7
Total fixed assets	<u>1,961,006</u>	17.0	<u>1,278,256</u>	10.7	<u>1,507,883</u>	12.9
<b>Total assets</b>	<u>11,561,159</u>	100.0	<u>11,981,884</u>	100.0	<u>11,723,294</u>	100.0

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Thousands of yen	June 30, 2002	%	June 30, 2003	%	December 31, 2002	%
<b>Current liabilities</b>						
Notes and accounts payable	824,751		929,721		1,292,742	
Short-term bank loans	1,348,332		1,854,216		1,524,572	
Accrued bonuses	52,814		74,942		43,226	
Others	665,445		633,167		606,680	
	<u>2,891,343</u>	25.0	<u>3,492,047</u>	29.2	<u>3,467,221</u>	29.6
<b>Long-term liabilities</b>						
Long-term bank loans	41,669		-		16,670	
Liability for employees' retirement benefits	13,780		13,066		10,603	
Liability for directors' and corporate auditors' retirement benefits	235,157		251,031		248,492	
Others	38,967		59,906		47,475	
	<u>329,574</u>	2.9	<u>324,004</u>	2.7	<u>323,240</u>	2.7
Total liabilities	<u>3,220,917</u>	27.9	<u>3,816,051</u>	31.9	<u>3,790,461</u>	32.3
<b>Minority interests</b>	64,654	0.5	49,844	0.4	31,239	0.3
<b>Shareholders' equity</b>						
Capital stock	1,335,487	11.6	1,335,487	11.1	1,335,487	11.4
Capital surplus	2,694,389	23.3	2,694,389	22.5	2,694,389	23.0
Retained earnings	4,258,581	36.8	4,082,777	34.1	3,891,354	33.2
Unrealized gains or losses on securities	(11,214)	(0.1)	5,679	0.0	(17,570)	(0.2)
Treasury stock	(1,655)	(0.0)	(2,344)	(0.0)	(2,067)	(0.0)
	<u>8,275,587</u>	71.6	<u>8,115,988</u>	67.7	<u>7,901,593</u>	67.4
<b>Total liabilities and shareholders' equity</b>	<u>11,561,159</u>	100.0	<u>11,981,884</u>	100.0	<u>11,723,294</u>	100.0

**Consolidated statement of income**

Thousands of yen	June 30, 2002	%	June 30, 2003	%	December 31, 2002	%
<b>Net sales</b>	6,304,885	100.0	8,817,986	100.0	15,614,300	100.0
<b>Cost of sales</b>	4,452,538	70.6	6,669,746	75.6	11,530,872	73.8
Gross profit on sales	1,852,346	29.4	2,148,240	24.4	4,083,427	26.2
<b>Selling, general and administrative expenses</b>						
Provision for doubtful accounts	-		579		9,595	
Salary	480,511		442,386		979,239	
Provision for bonuses	49,179		65,012		59,631	
Provision for directors' and corporate auditors' retirement benefits	5,264		15,770		18,598	
Rental expenses	225,703		210,904		460,886	
Others	857,427		799,510		1,895,080	
	1,618,086	25.7	1,534,163	17.4	3,423,031	21.9
Operating income	234,259	3.7	614,076	7.0	660,395	4.3
<b>Nonoperating income</b>						
Interest income	865		723		1,121	
Dividend income	114		104		261	
Foreign exchange gain	166,658		40,793		179,795	
Gain on sale of investment securities	4,486		2,822		4,289	
Others	19,443		4,063		44,057	
	191,569	3.0	48,507	0.5	229,526	1.4
<b>Nonoperating expenses</b>						
Interest expenses	10,499		11,606		22,176	
Equity in loss of associated companies	991		-		7,947	
Provision for doubtful accounts	53,302		-		57,522	
Commissions paid	-		13,942		14,000	
Others	17,159		10,972		25,607	
	81,953	1.3	36,521	0.4	127,253	0.8
Ordinary income	343,875	5.4	626,061	7.1	762,667	4.9
<b>Extraordinary income</b>						
Gain on sales of fixed assets	4		478		4	
Reversal of allowance for doubtful accounts	3,288		-		-	
Gain on reversal of expenses for dissolution of joint venture	-		39,883		-	
	3,292	0.1	40,362	0.5	4	0.0
<b>Extraordinary losses</b>						
Loss on devaluation of fixed assets	-		8,725		22,585	
Loss on disposal of fixed assets	4,444		5,609		10,632	
Loss on devaluation of investment securities	-		28,181		24,753	
Amortization of goodwill	-		-		508,674	
Loss on liquidation of subsidiaries and associated companies	392,378		6,341		386,307	
	396,822	6.3	48,856	0.6	952,953	6.1

PALTEK CORPORATION

Thousands of yen	June 30, 2002	%	June 30, 2003	%	December 31, 2002	%
Income (loss) before income taxes and minority interests	(49,654)	(0.8)	617,566	7.0	(190,281)	(1.2)
Income taxes - current	204,066		267,183		474,436	
Income taxes - deferred	(632,241)		(12,106)		(661,451)	
	(428,175)	(6.8)	255,077	2.9	(187,015)	(1.2)
Minority interests in income (loss) of consolidated subsidiaries	(8,344)	(0.1)	38,928	0.4	(24,947)	(0.2)
Net income	386,866	6.1	323,560	3.7	21,681	0.2

**Consolidated statement of retained earnings**

Thousands of yen	June 30, 2002	June 30, 2003	December 31, 2002
Retained earnings, beginning of term	3,990,100	-	-
Reduction in retained earnings			
Dividends	118,384	-	-
	<u>118,384</u>	-	-
Net income	386,866	-	-
Retained earnings, end of term	4,258,581	-	-
<b>Capital surplus</b>			
Capital reserves, beginning of term	-	2,694,389	2,694,389
Capital reserves, end of term	-	2,694,389	2,694,389
<b>Retained earnings</b>			
Balance, beginning of term	-	3,891,354	3,990,100
Increase			
Net income	-	323,560	21,681
	-	<u>323,560</u>	<u>21,681</u>
Decrease			
Cash dividends	-	118,362	118,384
Directors' bonuses	-	13,775	2,042
	-	<u>132,138</u>	<u>120,427</u>
Balance, end of term	-	4,082,777	3,891,354

**Consolidated statement of cash flows**

Thousands of yen	June 30, 2002	June 30, 2003	December 31, 2002
<b>Net cash from operating activities</b>			
Income (loss) before taxes and minority interests	(49,654)	617,566	(190,281)
Depreciation	74,897	67,586	155,365
Amortization of goodwill	118,045	15,711	744,207
Equity in losses of associated companies	991	-	7,947
Loss on devaluation of fixed assets	-	8,725	22,585
Loss on devaluation of investment securities	-	28,181	24,753
Increase in allowance for doubtful accounts	37,265	538	54,177
Increase (decrease) in accrued bonuses	9,179	31,715	(408)
Increase (decrease) in liability for employees' retirement benefits	246	2,463	(2,930)
Increase in liability for directors' and corporate auditors' retirement benefits	5,264	2,539	18,598
Interest and dividends income	(980)	(827)	(1,382)
Interest expenses	10,499	11,606	22,176
Gain on sales of investment securities	(4,486)	(2,822)	(4,289)
Loss (gain) on sales of investment securities	1,512	-	83
Gain on sales of tangible fixed assets	(4)	(478)	(4)
Loss on disposal of tangible fixed assets	4,444	5,569	8,309
Gain on reversal of expenses for dissolution of joint venture	-	(39,883)	-
Loss on liquidation of subsidiaries and associated companies	321,302	6,341	322,614
Decrease (increase) in accounts receivable - trade	593,444	69,423	(802,605)
Decrease (increase) in inventories	(149,602)	(223,699)	(542,784)
Increase (decrease) in payables - trade	(255,737)	(363,020)	212,253
Decrease (increase) in advance payments	112,101	73,323	176,519
Increase in accounts payable - other	-	85,768	-
Increase (decrease) in advances	-	(104,041)	-
Decrease (increase) in consumption tax receivable	100,283	97,183	(80,085)
Bonus paid to directors and corporate auditors	-	(14,010)	(2,400)
Others	133,472	48,183	109,153
	1,062,485	423,645	251,572
Interest and dividends received	788	37	70
Interest paid	(10,779)	(11,388)	(22,369)
Proceeds from reversal of previously budgeted for dissolution of joint venture	-	39,883	-
Payments on liquidation of subsidiaries and associated companies	(267,085)	(6,341)	(273,755)
Income tax paid	(25,717)	(199,112)	(298,743)
	759,691	246,723	(343,225)

PALTEK CORPORATION

Thousands of yen	June 30, 2002	June 30, 2003	December 31, 2002
<b>Net cash from investing activities</b>			
Increase in time deposits	(34,031)	(20,000)	(43,033)
Decrease in time deposits	20,000	30,033	20,000
Purchases of investment securities	(42)	(71,000)	(98)
Proceeds from sales of investment securities	99,916	3,919	99,916
Payments for acquisition of affiliate's equity	-	(20,000)	(11,246)
Purchases of tangible fixed assets	(22,256)	(17,093)	(43,534)
Proceeds from sales of tangible fixed assets	9,282	16,421	9,282
Purchases of intangible fixed assets	(12,777)	(22,194)	(30,717)
Proceeds from sale of investment to partnership	8,054	3,097	8,054
Payments for loans	-	(61,500)	-
Proceeds from collection of loans	5,720	61,562	5,845
Proceeds from surrender of insurance policy	-	-	120,435
Increase in other investments	(42,843)	(21,937)	(57,068)
Decrease in other investments	26,090	-	16,604
	57,112	(118,691)	94,442
<b>Net cash from financing activities</b>			
Net increase (decrease) in short-term bank loans	(241,643)	332,040	(90,402)
Proceeds from long-term bank loans	4,140	-	4,140
Repayment of long-term bank loans	(25,490)	(19,066)	(25,490)
Purchases of treasury stock	(921)	(277)	(1,332)
Proceeds from issuance of common stock	20,000	-	20,000
Cash dividends paid to minority shareholders	-	(166)	(665)
Cash dividends	(116,463)	(116,162)	(117,610)
	(360,377)	196,368	(211,359)
Effect of exchange rate changes on cash and cash equivalents	(7,140)	11	(7,138)
	449,285	324,411	(467,281)
Increase (decrease) in cash and cash equivalents	449,285	324,411	(467,281)
Cash and cash equivalents at beginning of term	1,652,477	1,141,516	1,652,477
Decrease in cash and cash equivalents due to decrease in consolidated subsidiaries	(43,679)	-	(43,679)
Cash and cash equivalents, end of term	2,058,083	1,465,927	1,141,516