



To Our Stakeholders
PALTEK REPORT
Year Ended December 31, 2002

To our Stakeholders:



PALTEK Corporation
Tadahito Takahashi,
 President

Year 2002 marked the 21st year for PALTEK and it was a tough and challenging year for PALTEK as the technology industry suffered the sharp decline.

To begin with, I would like to express my sincere regret that our earnings and stock price posed serious concerns among our shareholders.

PALTEK celebrated the 20th anniversary in October last year since the formation of the company. Looking back over this period, we can divide those 20 years into three distinct growth phases:

1. >>> | 1982 ~ 1987 ... Early development
2. >>> | 1988 ~ 1998 ... Growth as a private company
3. >>> | 1999 ~ 2001 ... Growth as a public company

(For PALTEK's corporate history, please refer to page 8)

In the 5th year as a public company, we acknowledge that PALTEK is now faced with the arduous period and we are being tested in many ways. Our mission in this period is to go through with the period as quickly as possible while preparing ourselves to reemerge from it as a stronger and more cohesive organization.

2002 was also a remarkable year when "Paradigm Shift" took place more rapidly than we anticipated. "Paradigm Shift" is a concept, which I have always kept in my mind in observation of natural phenomenon as well as in business since I started the company. I have often talked about this

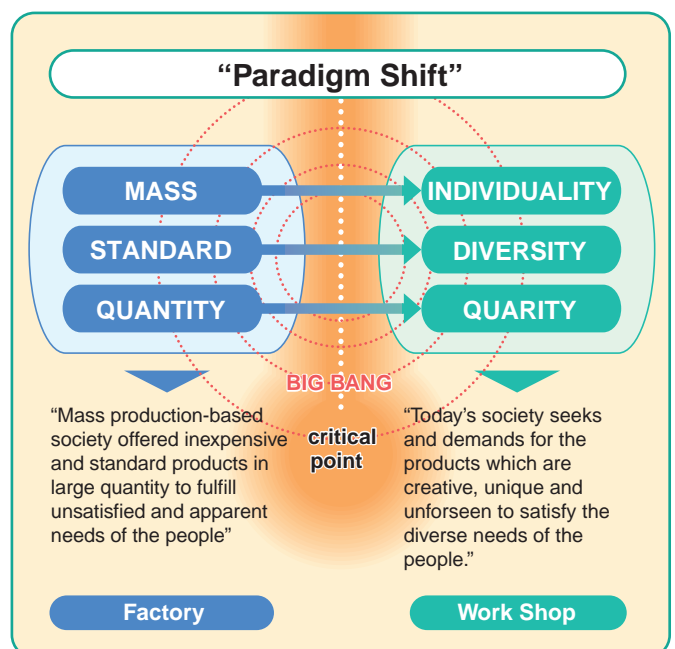
concept both within the company and with the people outside of the company.

Our assumption is that Japanese society, in its many aspects, experience the fundamental transitions. Such transitions occur in every layer of life. For example, "individuality" is valued rather than "mass" while "diversity" replaces "standard." "Quality" comes first before "quantity." Looking at recent and current changes and phenomenon in Japan as a whole, we can safely say our assumption is largely proved right by the facts. I can say that some of our early success at PALTEK is largely credited to this assumption. However, as we entered 2002, the pace of change picked up far beyond our expectations.

The challenge facing us, therefore, is to accelerate the speed in order to keep up with this pace of changes. To achieve the speed we need, we had to deal with some of the burdens, which were holding us back. By taking following actions, we believe we have made ourselves more agile and fitter.

First, we decided to take a lump-sum amortization of goodwill respect to Spinnaker Systems, Inc. one of our subsidiaries. Spinnaker is involved mainly in marketing EDA tools, which are software tools used in planning and designing of semiconductors. Its main clients are Japanese semiconductor designers. With the global downturn in the semiconductor industry, Japanese semiconductor companies have cut back so sharply on their capital investments as to bring them to a virtual halt. With that market situation in mind, we made the decision to amortize the company's goodwill in a single lump-sum.

Next, in order to lay a solid foundation for a major leap forward in 2003, we have evaluated our business portfolio and, based on such assessment, we have taken several measures. One such measure is to streamline our product line. We terminated the distribution agreement with Infineon Technologies Japan K.K. Other additional measures we took were to liquidate HYPER-PALTEK Corporation while dissolving the joint venture with Marubun Corporation.



The New Beginning

We set Year 2003 as a new starting point for the next growth phase for PALTEK. Already we are busy making preparations in several areas.

First, in the area of Altera's programmable logic devices (PLD), which is our mainstay business, we are making aggressive moves in promoting the new PLD product families. Altera's unique technologies have enabled them to introduce large-density, highly cost-efficient PLD products to the market, which no other existing products could match. Thanks to these new technologies and a number of new products being currently deployed, we started to see PLDs used in more applications. We expect these new products will further expand the market to the fields, where PLDs have been rarely used.

Next, in view of the convergence taking place among household applications and information/communications applications, we intend to expand our business by offering systems solutions based on new strategies and business propositions, which we have been offering as a network solution.

Moreover, we intend to develop new and untapped markets by working together with high-tech venture companies that are being born and springing up throughout Japan. As I mentioned earlier, Japanese society is making a transition to the new society, and one of such effects can be seen among some engineers, who have been spun off from major electronics or semiconductor companies and who are now starting venture companies. For the past several years, we have nurtured our contacts with these kinds of start-up venture companies. In particular, we have been working closely with Nippon Technology Venture Partners Ltd., (Kazutaka Muraguchi, General Partner) as well as with other venture capital firms, so that in the future we can discover and develop other venture companies that could become our customers or partners. These efforts have already been paid off and we have started to see some specific business potentials. As the first achievement in 2003, we have started the new kind of security services by teaming up with Trinity Security Systems Inc. The security business, as we see it, will become a key requirement as the broadband era gets underway, and we see a tremendous opportunity in this market.

Lastly, I would like to inform you that we have appointed Hiroyuki Takasaki to serve as the executive vice president of the company effective January 1, 2003. His appointment is intended to facilitate timely management decisions as well as to strengthen our risk management capability. Mr. Takasaki brings many years of experiences in semiconductor industry to PALTEK, having worked for a US-based major semiconductor manufacturer, and ultimately served as the president of the Japanese subsidiary of a major American semiconductor company before joining PALTEK. We are confident that his outstanding wealth of experience brings new opportunities and growth to PALTEK.

Looking toward Year 2003, we are committed that all PALTEK people, the management team and all employees alike, strive to meet the expectations of our shareholders, customers and suppliers, based on our corporate philosophy of "kyo-sei" ("Cooperative Growth.")

A Message from Mr. Hiroyuki Takasaki, Executive Vice President

I joined PALTEK as I was deeply moved by Mr. Takahashi's philosophy of "kyo-sei." ("cooperative growth.") Over the last two and a half years I have been in charge of Altera's PLD business at PALTEK. I was recently appointed as an executive Vice president and a representative director of PALTEK Corporation. In accepting the appointment, I am determined to fully dedicate myself to the success and development of PALTEK Corporation.

Over the last few years our focus has been placed on strengthening the basic yet very important functions as a distributor of semi-conductor products. Namely, we have deployed the new sales management information systems while we enhanced our proprietary customer database system. Additionally, we installed a new business process management system, and introduced a new inventory management system based on advanced statistical method. By deploying these aggressive measures, we were able to install more efficient sales and management operations, and we have started to see some tangible results. We have also increased the number of engineering staff in order to enhance our capability as a solution provider. We pride ourselves that our engineering capacity exceeds the norm of a semiconductor distributor in both number and quality.

In addition to augmenting our fundamental capabilities, we will keep addressing the questions and missions we set forward for ourselves. Such questions are: what kind of values we can offer to the Japanese society which is going through drastic "Paradigm Shift," what are the roles that we have to play in order to remain as an indispensable strategic partner for our customers as well as for our suppliers, what is the ultimate image of the company as a leading originator of new business models, and what is our *raison d'être*.

Thank you for your continued support.

Sincerely,

Hiroyuki Takasaki,

Managing Director and Vice President



The future of PALTEK Group

The PALTEK Group sets up a goal to become a group of companies with an annual revenue of ¥50 billion with an operating profit margin of 10% by Year 2005, With these goals in mind, we will be focusing on the following three areas in Year 2003:

1. Strengthening the PLD business

Our PLD (Programmable Logic Device) business has been strong since Year 2002, in particular, due to the deployment of such new product families like Stratix and Cyclone by our supplier, Altera Corporation.

Altera continues to be a leader and an early adopter of leading-edge technologies. For many years Altera has been able to provide the PLD products which are outstanding in every way: density, speed and cost-performance. At the same time, by creating a rich variety of standard IPs (Intellectual Properties), it has made it very easy for the logic designers to build sophisticated systems into PLDs in a very short time. This has brought the system design significantly closer to realizing the SOPC (system-on-a-programmable-chip) technology that Altera has long been advocating.

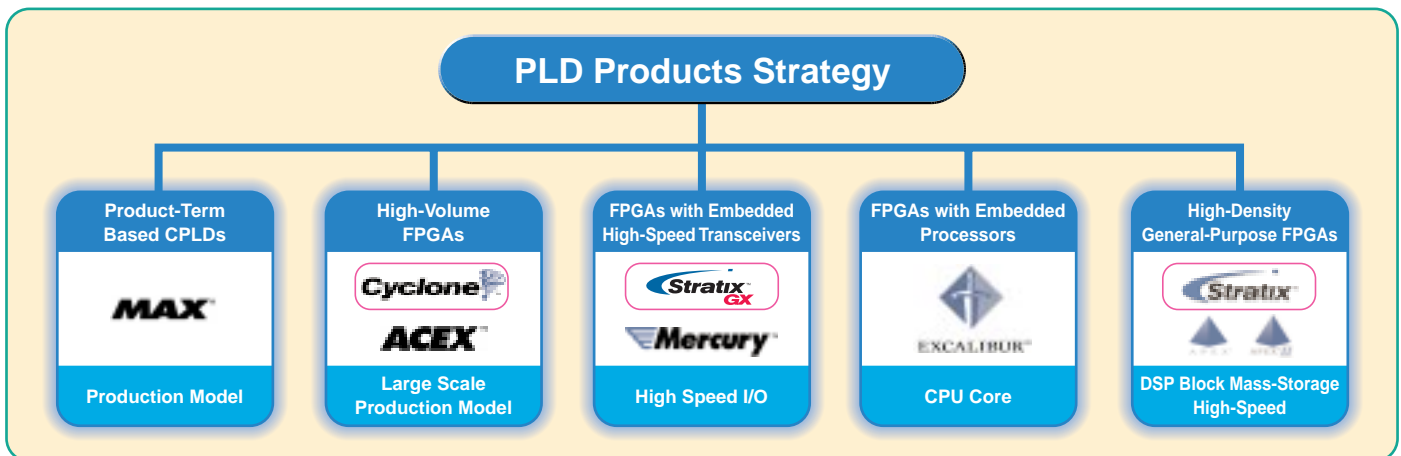
Given the current market conditions, we will be pursuing the following strategies to expand our PLD business:

1. Strengthening technical services

As in the past, we are trying to offer a kind of sophisticated technical solutions, that go beyond what traditional semiconductor distributors usually offer. To make PLDs into SOPCs, we need to have technical knowledge of our customers' end-products. To achieve this, we continue to invest in our human resources.

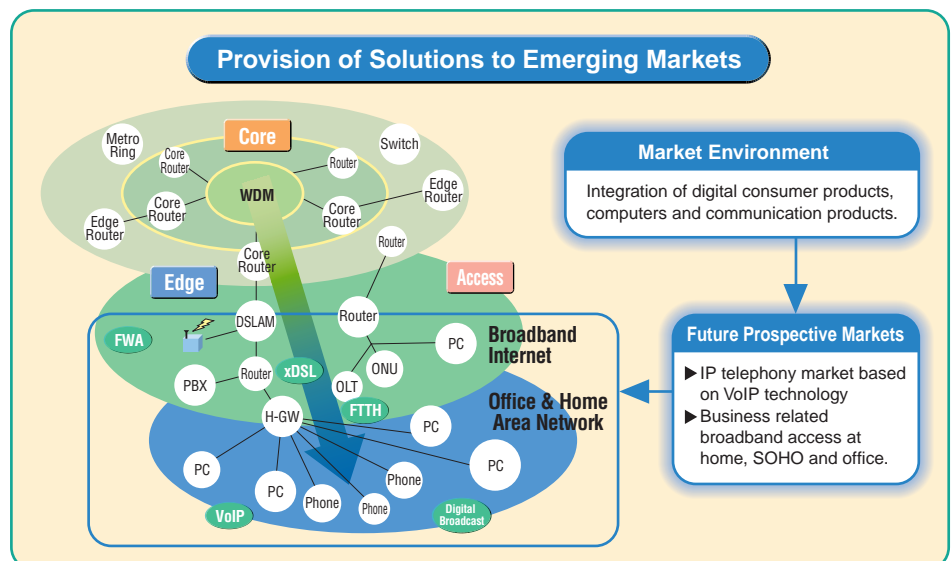
2. Expanding our customer base

As PLD are more widely used and accepted in a variety of applications and customers, we are expanding our customer base. Moreover, some high-tech venture businesses, which are being born throughout Japan, appear to be good partners to team up in order to promote and further advance PLD business.



2. Providing system solutions to the emerging markets

Investments in communications infrastructure have been significant in recent years and it is our observation that not much investment can be expected in this segment at least in the near future. On the other hand, as digital consumer products, computers and telecommunication products are more closely linked, we believe that the following markets described below will present strong growth opportunities, and we intend to exploit and expand our product offerings in these directions. Our strategy is to promote our product offering not only in semiconductor products but also in the forms of module or board, or even system, which will help us to expand our sales opportunities.



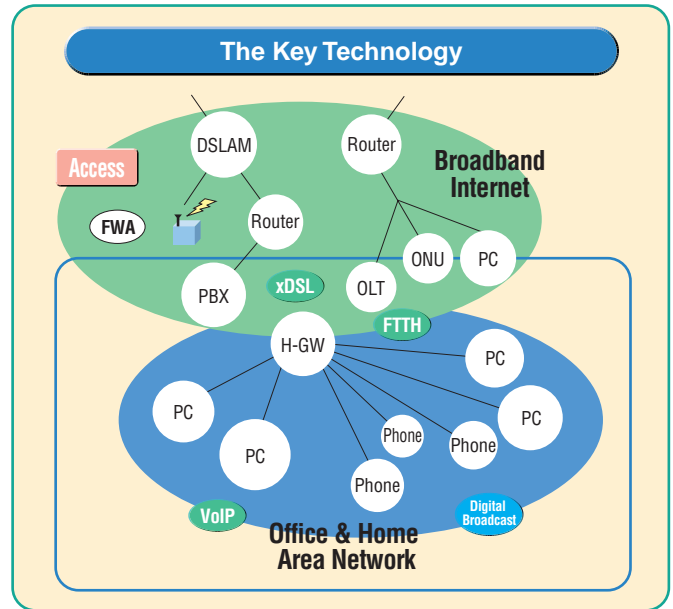
1: IP Telephony market based on VoIP technology

Product promotion and technical support to such applications like IP-PBX (Private Branch exchange), CTI (Computer Telephony Integration), and IAD (Integration Access Devices) targeted all types of markets such as carriers, enterprises, and individuals.



2: Broadband access related market

Product promotion and technical support to such broadband access related markets like individual homes, SOHO, and enterprises.



3: Deployment of security business with Trinity Security Systems

The internet is finally approaching the broadband era, as expressed in the marketing slogans like “ubiquitous society” and “e-Japan plan.”

At the same time, the increasing proliferation of hacker attacks and computer viruses is becoming a serious hazard for the progress of the internet society.

In reality, today’s security measures have not kept pace with the accelerating expansion and advancement of broadband access in the world of internet.

We take this situation as a great business opportunity for PALTEK. To capture and exploit this opportunity, we teamed up with Trinity Security Systems Inc., an expert in the security

field, with a wealth of experience in encryption technology and protection of confidential data.

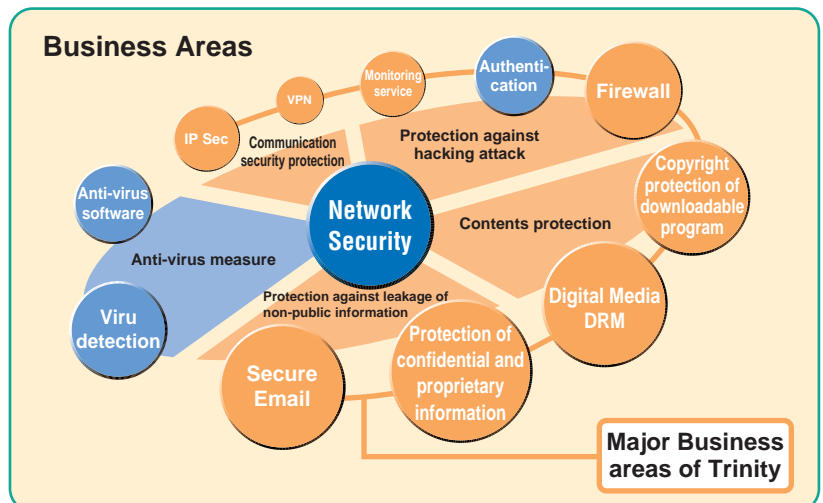
Security business has strong connection and needs to our customers in the broadband market and applications. With our experiences and knowledge in this field, we can better address the needs of our customers.

By flexibly combining PALTEK knowledge and experience in the broadband market with Trinity Security Systems’ security technology, we are confident that PALTEK can establish a solid position as a leading company, which can provide total solutions in the security business market.



TRINITY SECURITY SYSTEMS

Headquarters: 8-3-13 Nishigotanda, Shinagawa-ku, Tokyo, 141-0031, Japan
 Representative: Motonori Hayashi, President & CEO
 Employees: 31(as of January 2003)
 Established: November 1, 1999
 Capital: ¥304 million (as of January 2003)
 Business: Development, sales and systems integration of network security-related software, hardware, middleware.



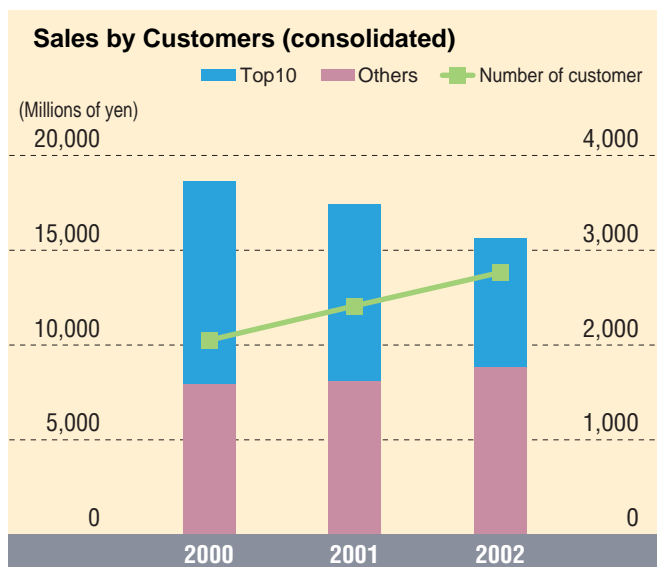
Risk factors

In addition to all the information about our strategies and expectations of the PALTEK Group in the future, the following factors could affect our actual results.

(1) Risk factor #1

First of all, a large portion of our revenue is consisted of revenues from a relatively small number of customers.

However, we have already introduced and working on the countermeasures. We are expanding our customer base through broadening the application fields of existing products while developing entirely new markets through alliance with high-tech start-up companies.

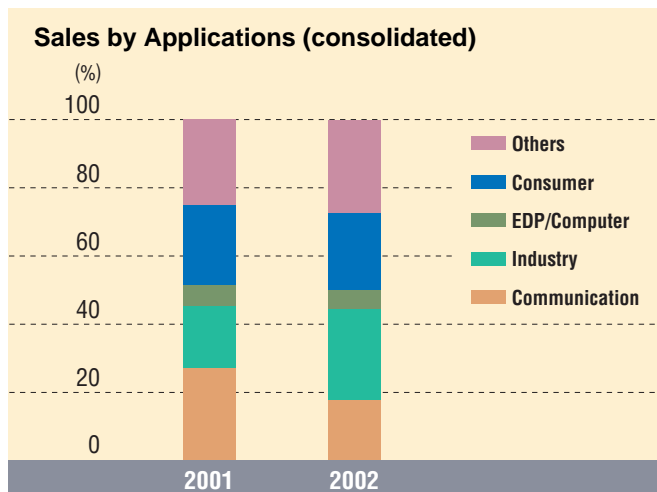


(2) Risk factor #2





Secondly, the areas of application of the products handled by PALTEK were traditionally concentrated in the information and communications-related segments (Communication).

This factor is now being solved by the advantage of our major product offering, PLDs. PLD market has really opened up to embrace a wide variety of applications, including industrial equipment such as broadcasting equipment, measuring equipment, medical diagnostic systems, and large display panels (Industry), as well as Electronic Data Processing equipment (EDP/Computer), DVDs and all kinds of digital consumer goods (Consumer).

What we call "user configurability" has become the important key concept for a logic designer, where a user or a logic designer can alter a design as it becomes necessary, at hand and any time.



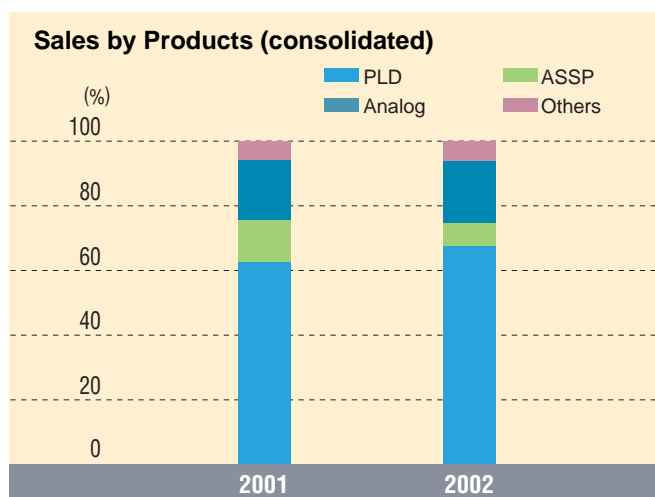
Definitions of Applications

Communication	Industry	EDP/Computer	Consumer
Applications for communication infrastructure and Broadband Switching, Terminal, Gateway, Routing/IP, Wireless Access	Applications for digital broadcasting equipment, medical equipment and measurement equipment	Applications for computer peripheral equipment, storage and imaging equipment (FAX, Copy machine)	Applications for mobile phones, DSCs, audios and game equipment
			

(3) Risk factor #3

The third factor is represented by the skewed product sales.

As discussed earlier in connection with the future business plans, we continue to search and incorporate innovative new products and technologies centering around existing products in order to provide high-value-added products and services that are unique to PALTEK. In year 2002, we have concluded distribution agreement with three companies (see pages 9 and 10) and have already started marketing their products.

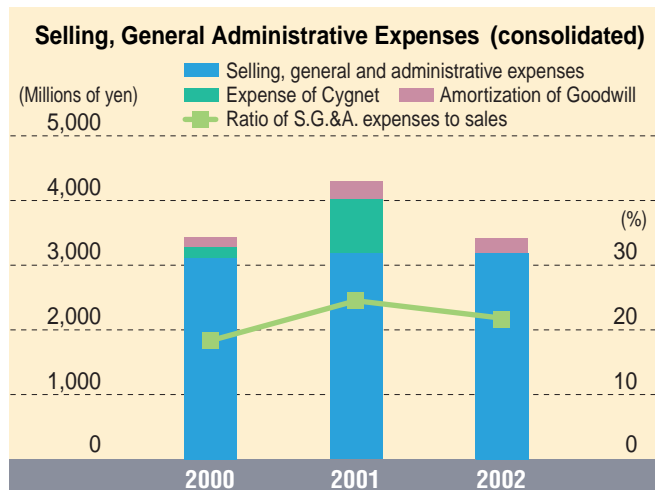
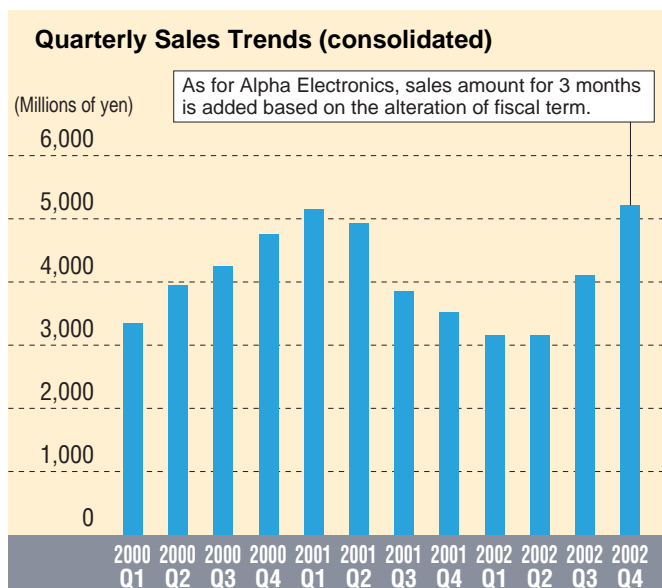
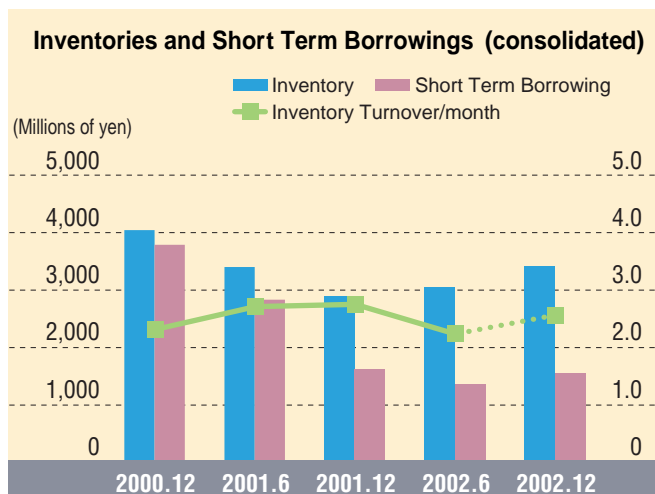


(4) Risk factor #4

Lastly, the impact of the past year's economic slowdown was large, and we anticipate that the situation is likely to continue in foreseeable future.

To strengthen our financial standing and to better-prepare for the challenges of the new environment, PALTEK has already taken several measures as we discussed in the previous pages. The subsidiaries of PALTEK are also making efforts to improve their operations.

As noted from our quarterly sales trends below, we think we hit the bottom around the first and second quarter of 2002.



*Please note that the Quarter Results are unaudited financial statements.

PALTEK Corporation : Profiles of Directors

PALTEK is a young and vibrant company with energetic corporate officers and employees. The company was established 20 years ago, and some 80% of the employees are younger than 40 years old. Following are the profiles of the directors.

President

Tadahito Takahashi

October 24, 1948

Oct. 1982 Established PALTEK Corporation as President
 Dec. 1999 Chairman of the Board of Alpha Electronics, Inc.
 Jun. 2001 Appointed Director of axelec corporation



Managing Director and Vice President,
 General Manager of PLD Business Division

Hiroyuki Takasaki

September 25, 1946

Sep. 1971 Joined Texas Instruments Japan Ltd.
 Aug. 1997 Appointed President & Representative Director, XILINX K.K.
 Jun. 2000 Joined PALTEK Corporation
 Mar. 2001 Became a member of the Board
 Jan. 2002 Appointed Director of Spinnaker Systems, Inc.
 Jun. 2003 Appointed as Managing Director and Vice President



Director,
 General Manager of System
 Solution Division

Masanori Kanamori

April 18, 1947

Mar. 1979 Joined Texas Instruments Japan Ltd.
 Jul. 1997 Appointed General Manager of MOS Memory Business Division, Semiconductor Business Headquarters
 Nov. 1998 Joined PALTEK Corporation
 Mar. 1999 Became a member of the Board

Director,
 General Manager of Solution
 Development
 Division

Yoshio Sakurai

December 14, 1946

Apr. 1967 Joined NEC Corporation
 Jul. 1995 Deputy General Manager of Switching Division
 Nov. 1995 Appointed General Manager of Access System Development Division
 Jul. 1998 Seconded to NEC Communication Systems, Ltd. as General Manager of Engineering Division
 Jun. 1999 Seconded to NEC Communication Systems Kyushu, Ltd. as Director
 Apr. 2001 Joined PALTEK Corporation
 Jun. 2001 Appointed President & Representative Director of axelec Corporation
 Mar. 2002 Became a member of the Board



Director,
 General Manager of
 Operational Service Division,
 and Environment

Tadashi Ito

October 5, 1949

Apr. 1973 Joined Japan Automobile Research Institute
 July. 1982 Joined Texas Instruments Japan Ltd.
 July. 1990 Appointed Accounting Manager, ASP Business Department.
 Mar. 1995 Appointed Contoller, ASP Business Dept.
 Nov. 1998 Joined Vivid Semiconductor Co., Ltd. as Manager of Japan Office
 Apr. 2000 Joined Mattson Technology Center Inc. as Administration Manager
 June.2001 Joined PALTEK Corporation
 Jan. 2002 Appointed Manager of Finance & Legal Group, Operational Service Division



Outside Director

Masahiko Hirata

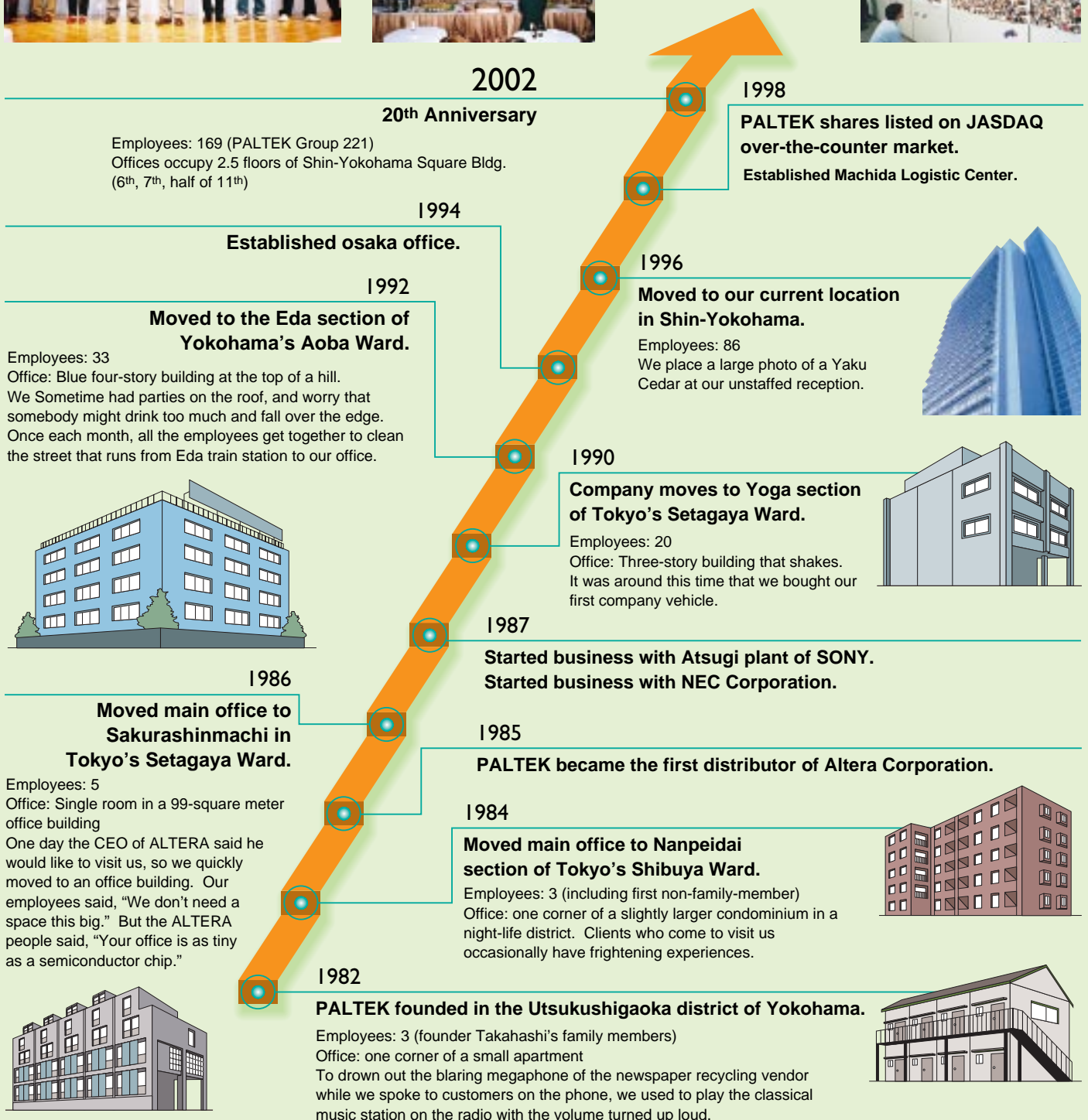
February 1, 1931

Apr. 1954 Joined Matsushita Electric Industrial Co., Ltd.
 Nov. 1970 Appointed Director of Victor Company of Japan, Ltd.
 Jun. 1980 Appointed Senior Managing Director
 Feb. 1985 Appointed Director of Matsushita Electric Industrial Co., Ltd.
 Jun. 1988 Appointed Executive Vice President
 Jun. 1993 Appointed Senior Corporate Auditor
 Mar. 2001 Became a member of the Board of PALTEK Corporation

PALTEK - 20 Years of History

Twenty years have passed since PALTEK was founded at Yokohama in Kanagawa Prefecture. I would like to give you a brief outline of the company's history.

•Pictures from the 20th Anniversary party•



TOPICS

Strategic move for entering future potential markets

Enter Into Distribution Agreement with BRECIS Communications Corporation.



BRECIS is the world's first company to succeed in offering one-chip solutions, using their unique System-on-a-Chip (SoC) technology. This technology enable them to combine the function of several chips, such as voice processing, security engines and packet processors, in one piece of silicon.

The outstanding features of BRECIS products are their single-chip designs including security features with rapid processing speed of over 40 Mbps. The key advantages of appliances that use BRECIS's products architecture are small-footprint, low price, and high performance.

Through our distribution agreement with BRECIS, we can map out our strategy for entering the security market, which is widely seen as a market with strong growth potential.



About Metalink Ltd.



Metalink utilizes the industry's highest-level SHDSL and VDSL technology to develop and market high-performance broadband access chip-sets focused on video-streaming and Voice Over DSL applications. Metalink's broadband solutions realize high-speed video streaming and data communications at low-cost in the network throughout the world.

PALTEK hopes to strengthen and expand its solutions for the access network market by offering Metalink's products.



TRINITY SECURITY SYSTEMS

Business Alliance with Trinity Security Systems Inc.

As the spread of broadband network gains momentum, interest in data security is rising year by year. Based on the wealth of technical expertise we have built up over the years, and aiming to build a new business centered around our core product line of programmable logic devices, we reached the decision to form a business alliance with Trinity Security Systems, Inc. Trinity is an innovative company with substantial intellectual property assets in the security field. It already holds and has outstanding applications for a number of patents. Through this alliance, we hope to expand into new businesses and realize synergies with our existing business lines.

Reorganization and preparation for the next leap

Lump-sum amortization of goodwill related to Spinnaker Systems, Inc.

Responding to poor earnings results at wholly owned subsidiary Spinnaker Systems, which has been suffering from prolonged capital investment cutbacks among Japanese chip manufacturers, the PALTEK Group has readjusted the term of amortization, and decided additional ¥500 million as the lump-sum amortization of goodwill in addition to the previously scheduled amount of ¥200 million.

Dissolution of HYPER-PALTEK Corporation

HYPER-PALTEK Corporation was established as a joint venture between California-based HYPER CORPORATION and PALTEK Corporation on January 31, 2001 and the company provided the Bluetooth qualification services. A decision has been reached to dissolve HYPER-PALTEK, however, in view of the limited prospects that the business would develop beyond current levels, and limited synergies with the business of PALTEK and of HYPER CORPORATION.

Enter Into Distribution Agreement with TransChip Inc. a leading developer of single chip camera solutions for mobile communication devices



TransChip is the leading company founded by industry leading experts in the fields of imaging and semiconductor technologies.

Furthermore, it is the first company in the world to develop a product family of integrated digital camera solutions for the capture, processing and compression of digital images on a single-chip, significantly reducing time to market by offering handset manufacturers a complete shrink wrap solution.

TransChip's products can be mounted in a wide array of applications such as mobile phones and PDAs. Furthermore, it enables customers to cut product development cost by reducing the number of microchips in the imaging system compared to current CCD camera chipsets. TransChip is engaged in an ongoing development of functionality including mega pixel resolution and MPEG-4.

By distributing TransChip's solution that takes into account the designs and space limitations of camera-equipped mobile phones, PALTEK spread out its solutions for the hand-held device market, in which fast time-to-market is a critical success factor.



Enter Into Distribution Agreement with Ashley Laurent, Inc. regarding security software necessary in broadband networks



As the growing popularity of ADSL and VoIP is rapidly increasing, the number of terminals that are directly connected to broadband networks are also increasing. In the enterprise and SOHO markets, great emphasis is being placed on security functionality and processing speed.

The outstanding features of Ashley Laurent's software is that encrypting data at more than double previous speeds and making high-speed access to broadband networks possible from any terminal.

We believe that, by combining Ashley Laurent's BroadWay™ software family with our existing products, we are able to offer more market-competitive product development proposals.

Termination of distribution agreement with Infineon Technologies Japan K.K.

PALTEK has decided to terminate its domestic distribution agreement with Infineon Technologies Japan, effective Jan. 31, 2003, due to changes in PALTEK's product line and in Infineon's support services.

Termination of Joint Venture Agreement with MARUBUN Corporation

PALTEK and MARUBUN Corporation have worked together to create a new semiconductor distribution business model since March 2002 through axelec corporation.

Under the prolonged stagnation of information technology market, however, 2 parties discussed the prospects of business at axelec and decided to terminate this joint venture.

Pursuant to the agreement, axelec Corporation will remain and stay in business as PALTEK's wholly owned subsidiary.

Business Overview

Operating results

In the current fiscal year, the Japanese economy showed a healthy recovery in the first half, led by expanding exports of electronic products and automobiles to the U.S. and Asian countries. In the second half and after, however, the Japanese economy has shifted again as stock price declines kicked off by suspicions of window dressing by U.S. companies, and uncertainties about the global political situation. As a result, exports have languished, and the future outlook has grown cloudy.

At the same time, it is too soon to blow away the clouds of uncertainty as we continue to experience contraction in capital spending in information and communications-related industries triggered by the slowdown in other industries.

In this market environment, some capital investment and production may be restarted after a long period of restraint, but few people expect the trend to continue over the long-term, and IT equipment makers' earnings have been greatly affected. For the PALTEK Group, the global slump in the IT sector, and the absence of any outstanding IT products to fuel growth in the semiconductor market has meant an extremely harsh business environment. But the company has focused its efforts on selling semiconductors in relatively healthy fields such as broadcasting equipment, consumer electronics and industrial equipment. It has also focused on achieving growth in other ways, by developing new customers, launching new products, and responding to customer needs.

As a result, net sales for the consolidated accounting period under review totaled ¥15,614 million (down 10.5% year-on-year). Ordinary income amounted to ¥762 million (up 218.2% year-on-year) due mainly to the reduction in R&D and other expenditures, as a result of the liquidation of an overseas subsidiary, Cygnet Technologies, Inc. Reflecting the lump-sum amortization of goodwill in relation to the purchase of the shares of Spinnaker Systems, Inc., liquidation expense incurred in relation to the liquidation of Cygnet Technologies, Inc., and recognition of a tax effect in an amount equal to the loss incurred by Cygnet

Technologies, Inc., net income for fiscal 2002 is ¥21 million (vs. ¥459 million net loss for the previous year).

Broken down by business segment, our results were as follows:

<Semiconductors and related businesses>

PALTEK Corporation, Alpha Electronics, Inc. Spinnaker Systems, Inc. and axelec corporation are active in semiconductor related businesses.

In the fiscal year just ended, the global IT slump has meant the absence of attractive IT equipment products that could drive the semiconductor market, creating an extremely harsh business environment for PALTEK. In this environment, PALTEK has been making efforts to maintain earnings and achieve growth by increasing semiconductor sales in relatively healthy sectors such as broadcasting equipment and industrial equipment, and by discovering new customers, launching new products, and responding to customer needs. In the market for PLDs (Programmable Logic Devices), applications have been growing day by day, and PALTEK has been actively pursuing sales growth to new customers. As a result, sales totaled ¥15,613 million (down 10.0% year-on-year).

Alpha Electronics founded a new subsidiary in China, in response to customers' shifts of production operations to that country. The company achieved ISO9001 certification, which should strengthen its relationship with key clients. In this environment, the company managed to maintain business with key clients in line with projected levels, and made a positive contribution to group earnings. Alpha Electronics changed the fiscal Year end month from September to December in order to align with PALTEK's fiscal year. As a result, a period of 15 months is accounted in this fiscal year.

Spinnaker Systems' main clients are communications equipment makers and electronics equipment makers. It is active in EDA software sales and intellectual property licensing. In view of the deteriorated performance during the fiscal year 2002, we have conducted an overall review of

its future business plans. As a result of the review, it was determined that consolidation goodwill with respect to Spinnaker Systems was impaired. In accordance with this assessment, we expensed the entire amount of the goodwill and recognized ¥508 million as an extraordinary loss.

MARUBUN and PALTEK have worked together to create a new semiconductor distribution business model since March 2002 through axelec corporation. However, 2 parties discussed the prospects of business at axelec and decided to terminate this joint venture. Pursuant to the agreement, axelec corporation will remain and stay in business as PALTEK's wholly owned subsidiary. The business did not make a positive contribution to the group earnings due to its start-up phase starts during fiscal year 2002.

<Other>

About HYPER-PALTEK Corporation, joint venture between California-based HYPER CORPORATION and PALTEK Corporation, it was decided to dissolve and liquidate by discussing 2 parties.

Outlook for fiscal year 2003

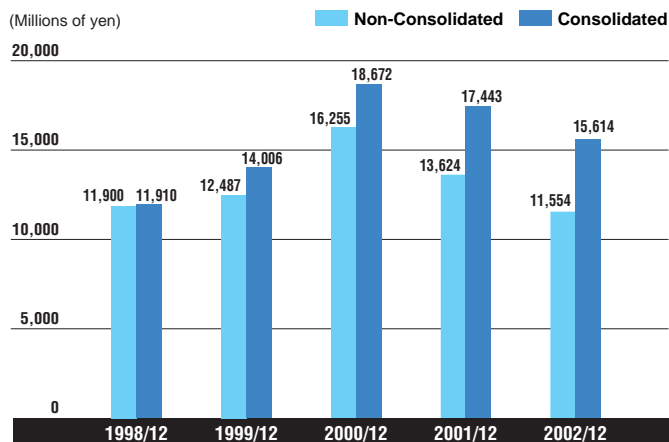
Regarding the future outlook for the business environment, the Japanese economy remains in a deflationary spiral, with future prospects clouded with uncertainty. However, in view of the fact that manufacturers' inventories are at extremely low levels, the U.S. economy seems to be able to fend off a renewed contraction, and given the expectations of a rebound in Japan's domestic demand, we believe the chance of renewed contraction is limited. On the other hand, in the area of information technology, it is too soon to blow away the clouds of uncertainty, as the outlook for fresh capital investment remains weak due to weakness in other industries. The major structural transition from the conventional telephone network to an IP-based network has already begun, and major PALTEK customers continue to restructure. The transfer of production and development of electronic devices to overseas countries is accelerating, and the destruction of Japan's future technological strength is

becoming a major concern for everyone.

We believe, however, that demand may recover in 2003, due to the prospective emergence of attractive new IT devices and consumer electronics products, new business opportunities stemming from the unification of broadcasting and communications through the start of terrestrial digital broadcasting, and expanded product development as electronic equipment makers have completed a round of inventory reduction. In these circumstances, the PALTEK Group will focus not just on IT equipment, but on growing areas such as broadcasting, consumer electronics, and industrial equipment, aiming for growth through expansion of its customer base. We aim to provide total solutions, evolving away from the conventional sales-centered model of semiconductor designing support services, and toward a more creative, highly-value-added model of development support services. With restructuring of the group companies already behind us, we anticipate a reduction in SG&A expenses including amortization of goodwill.

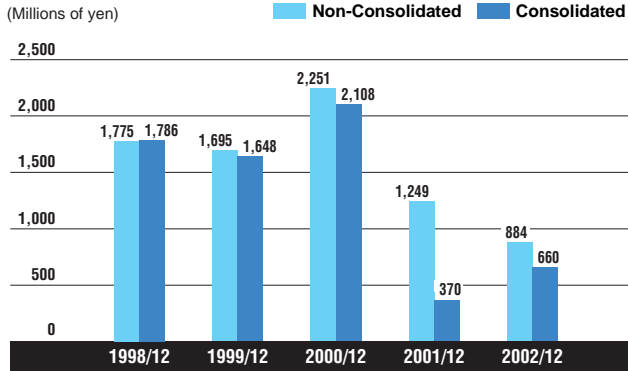
In fiscal year 2003, we aim to achieve, on a consolidated basis, total group sales of ¥16,436 million, operating income of ¥884 million, ordinary income of ¥834 million and net income of ¥467 million. On a non-consolidated basis, our projections call for net sales of ¥13,500 million, operating income of ¥888 million, ordinary income of ¥838 million and net income of ¥486 million.

Net Sales

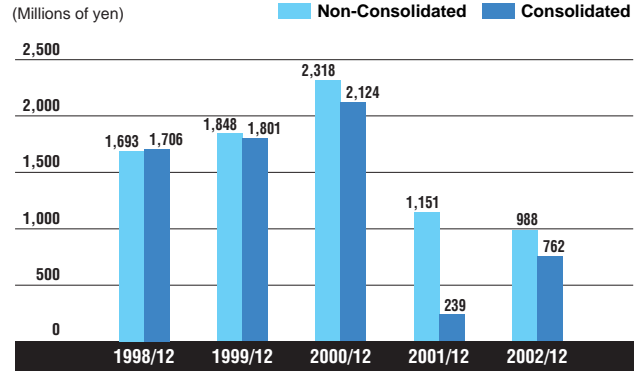


Financial Highlights

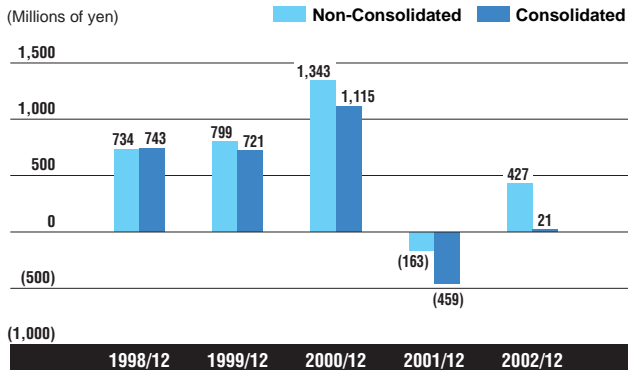
Operating income



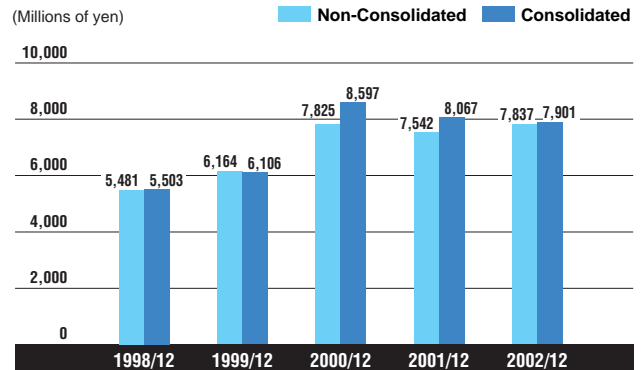
Ordinary income



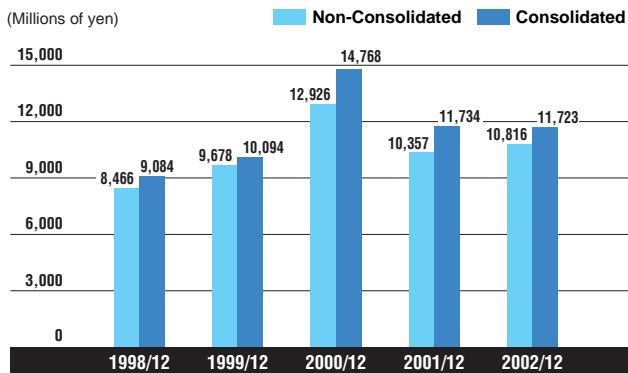
Net income (loss)



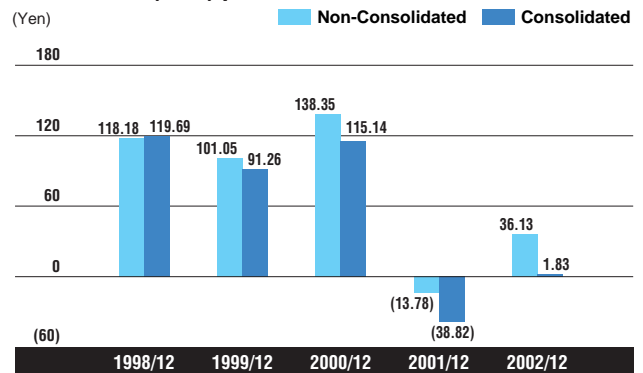
Shareholders' equity



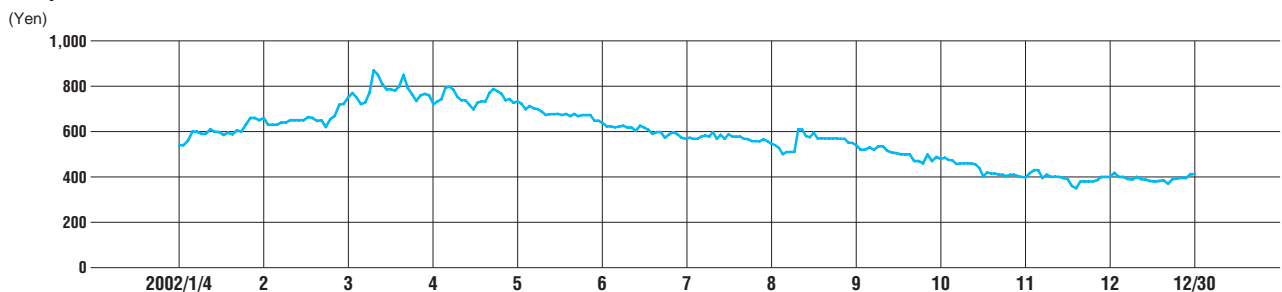
Total assets



Net income (loss) per share



Stock quotes



Consolidated Balance Sheets

(Thousands of yen)

	As of December 31, 2000	As of December 31, 2001	As of December 31, 2002
(Assets)			
Current assets			
Cash and bank deposits	1,578,800	1,675,477	1,187,549
Notes and accounts receivable	6,041,082	3,870,829	4,670,434
Marketable securities	172,969	—	—
Inventories	4,042,014	2,881,429	3,411,841
1 Deferred tax assets	98,810	106,568	368,490
Other current assets	380,841	817,637	584,477
Allowance for doubtful accounts	(40,637)	(4,467)	(7,382)
Total current assets	12,273,882	9,347,474	10,215,410
Fixed assets			
Tangible fixed assets			
2 Buildings	166,865	172,113	161,714
Accumulated depreciation	(52,318)	(67,800)	(77,169)
Vehicle equipment	5,995	1,884	1,884
Accumulated depreciation	(4,706)	(1,603)	(1,719)
Furniture and fixtures	414,122	513,403	377,949
Accumulated depreciation	(189,763)	(276,118)	(258,860)
Land	57,466	57,466	37,228
Total tangible fixed assets	397,662	399,344	241,028
Intangible fixed assets			
3 Goodwill	1,177,668	790,145	39,509
Other intangible assets	213,847	301,458	212,987
Total intangible fixed assets	1,391,516	1,091,603	252,496
Investments and other assets			
Investment securities	179,500	285,181	142,266
Long-term loans receivable	508	59,211	53,365
Deferred tax assets	120,310	116,760	524,845
Other	408,878	449,877	359,749
Allowance for doubtful accounts	(3,280)	(14,605)	(65,868)
Total investments and other assets	705,917	896,425	1,014,357
Total fixed assets	2,495,096	2,387,373	1,507,883
Total Assets	14,768,979	11,734,848	11,723,294
(Liabilities)			
Current liabilities			
Notes and accounts payable	788,203	1,096,911	1,292,742
Short term bank loans	3,785,019	1,604,924	1,524,572
Income taxes payable	565,424	58,915	201,017
Accrued bonuses	51,973	43,635	43,226
Other current liabilities	581,663	411,101	405,663
Total current liabilities	5,772,284	3,215,488	3,467,221
Long-term liabilities			
Long-term bank loans	74,656	96,992	16,670
Liability to employees' retirement benefits	12,635	—	—
Liability for employees' retirement benefits	—	13,533	10,603
Liability for directors' and corporate auditors' retirement benefits	224,945	229,893	248,492
Other long-term liabilities	30,269	58,684	47,475
Total long-term liabilities	342,507	399,104	323,240
Foreign currency translation adjustments	8,622	—	—
Total liabilities	6,123,415	3,614,592	3,790,461
(Minority interests)			
Minority interests	48,552	52,823	31,239
(Shareholders' equity)			
Capital stock	1,335,487	1,335,487	1,335,487
Capital surplus	2,694,389	2,694,389	2,694,389
Retained earnings	4,567,519	3,990,100	3,891,354
Net- unrealized loss on securities	—	(5,550)	(17,570)
Foreign currency translation adjustments	—	53,740	—
Treasury stock	(384)	(734)	(2,067)
Total shareholders' equity	8,597,011	8,067,432	7,901,593
Total liabilities, minority interests and shareholders' equity	14,768,979	11,734,848	11,723,294

The explanation of points

- The point picked up below is all about the consolidated and non-consolidated results of fiscal year 2002.
- In order to focus our management resources in more profitable businesses going forward, we have implemented a wide-ranging reorganization of our corporate structure, including the shrinking and restructuring businesses, and the decision to liquidate two companies in our group. The impacts of these actions are outlined below (please refer to points 1,3,4,5,6,9,10 and 18).

POINT 1

- The increase in deferred tax assets caused largely by recognition of the tax effect, related to the initiation of liquidation proceedings for a subsidiary.

POINT 2

- The decrease in buildings and land mainly caused by the devaluation of ¥22 million for fixed assets planned to sales whose book values have substantially declined against current values.

POINT 3

- The decrease in Goodwill primarily reflects our decision to amortize the entire amount of unamortized balance (¥508 million), as of the end of this accounting period, recognized at the time of the acquisition of Spinnaker Systems, Inc.'s shares by PALTEK. This amount was fully expensed and recognized as an extraordinary loss on the income statements. In addition, normal depreciation of ¥235 million for the period was recorded as related to Spinnaker Systems and Alpha Electronics in S.G.&A. expenses.

Consolidated Statements of Income

(Thousands of yen)

	January 1, 2000- December 31, 2000	January 1, 2001- December 31, 2001	January 1, 2002- December 31, 2002
Net Sales	18,672,185	17,443,098	15,614,300
Cost of sales	13,125,438	12,779,491	11,530,872
Gross profit	5,546,746	4,663,607	4,083,427
4 Selling, general and administrative expenses	3,437,921	4,292,732	3,423,031
Provision for doubtful accounts	—	—	9,595
Salary	961,840	1,386,597	979,239
Provision for bonuses	51,049	51,851	59,631
Provision for directors' and corporate auditors' retirement benefits	19,592	21,254	18,598
Rent expense	368,273	495,096	460,886
5 Amortization of goodwill	149,777	274,237	235,612
Other	1,887,387	2,063,696	1,659,468
Operating income	2,108,825	370,874	660,395
Non-operating income	127,959	51,866	229,526
Interest income	3,610	3,813	1,121
Dividend income	209	224	261
Foreign exchange gain	110,528	—	179,795
Gain on sale of investment securities	14	13,999	4,289
Equity in earnings of associated companies	—	3,047	—
Amortization of negative goodwill	—	—	79
Other	13,596	30,781	43,977
Non-operating expenses	111,904	183,045	127,253
Interest expense	55,777	69,629	22,176
Provision for doubtful accounts	—	—	57,522
Foreign exchange loss	—	58,082	—
6 Equity in losses of associated companies	25,521	—	7,947
7 Loss on surrender of insurance policy	—	8,867	14,094
8 Commissions paid	—	3,742	14,000
Other	30,604	42,723	11,512
Ordinary income	2,124,880	239,695	762,667
Extraordinary income	49,857	30,255	4
Previous year adjustment income	49,799	—	—
Gain on sales of fixed assets	57	—	4
Gain on reversal of foreign currency translation adjustments due to decrease in consolidated subsidiaries	—	7,762	—
Reversal of allowance for doubtful accounts	—	22,492	—
Extraordinary losses	15,979	218,900	952,953
Loss on sales of fixed assets	2,817	—	—
Loss on devaluation of fixed assets	—	—	22,585
Loss on disposal of fixed assets	252	1,313	10,632
Loss on sales of investment securities	—	39,920	—
Loss on devaluation of investment securities	12,909	14,844	24,753
Amortization of goodwill	—	156,521	508,674
9 Loss on liquidation of subsidiaries	—	—	386,307
Charge for full amount of transitional obligation for employees retirement benefits	—	6,300	—
Income (loss) before income taxes and minority interests	2,158,758	51,049	(190,281)
Income taxes-current	1,070,410	551,136	474,436
10 Income taxes-deferred	(14,524)	36	(661,451)
Minority interests in net loss of consolidated subsidiaries	12,990	40,539	24,947
Net income (loss)	1,115,862	(459,583)	21,681

POINT **4**

- The decrease in S.G.&A. expenses reflects the decrease in R&D expenses and labor cost that resulted from the initiation of liquidation proceedings for Cygnet Technologies, Inc. In the previous reporting period, Cygnet Technologies-related S.G.&A. expenses were ¥828 million.

POINT **5**

- Amortization of goodwill that are expensed in S.G.&A. expenses consist of ¥203 million related to Spinnaker Systems and ¥32 million related to Alpha Electronics, Inc. In addition, Amortization of goodwill expensed in extraordinary losses reflects our decision to amortize the entire amount of unamortized balance related to Spinnaker Systems Inc. (¥508 million).

POINT **6**

- Equity in losses of associated companies is the losses for HYPER-PALTEK, of which dissolution and liquidation was decided.

POINT **7**

- Loss on surrender of insurance policy reflects cancellation of life insurance as a result of reviewing investment activities.

POINT **8**

- Commissions paid represent fees paid for committed lines of credit. Currently, the Company has ¥4,000 million committed lines of credit.

POINT **9**

- Loss on liquidation of subsidiaries is largely expenses for the liquidation of Cygnet Technologies, Inc.

POINT **10**

- Income taxes-deferred reflect the tax effects of the recognition of losses related to the liquidation of Cygnet Technologies, Inc.

Consolidated Statements of Cash Flows

(Thousands of yen)

	Year ended December 31, 2000	Year ended December 31, 2001	Year ended December 31, 2002
Cash flows from operating activities:			
Income (loss) before taxes and minority interests	2,158,758	51,049	(190,281)
Depreciation	120,692	195,282	155,365
Amortization of goodwill	149,777	430,758	744,207
Equity in net (gains) losses of associated companies	(25,521)	(3,047)	7,947
Loss on devaluation of fixed assets	—	—	22,585
Loss on devaluation of investment securities	12,909	14,844	24,753
Gain on reversal of foreign currency translation adjustments due to decrease in consolidated subsidiaries	—	(7,762)	—
Increase (decrease) in allowance for doubtful accounts	2,589	(24,844)	54,177
Increase (decrease) in accrued bonuses	6,528	(8,337)	(408)
Decrease in liability for employee's retirement benefits	(2,366)	(12,635)	—
Increase (decrease) in liability for employees' retirement benefits	—	13,533	(2,930)
Increase in liability for directors' and corporate auditors' retirement benefits	(55,096)	4,947	18,598
Interest and dividends income	(3,819)	(4,038)	(1,382)
Interest expense	55,777	69,629	22,176
Foreign exchange gain	—	(12,724)	(476)
Gain on sales of investment securities	—	(13,999)	(4,289)
Loss on sales of investment securities	—	39,920	83
Gain on sales of tangible fixed assets	—	—	(4)
Loss on sales of tangible fixed assets	2,817	—	—
Loss on disposal of tangible fixed assets	252	1,313	8,309
Loss on disposal of intangible fixed assets	—	—	2,322
Loss on liquidation of subsidiaries	—	—	322,614
11 (Increase) decrease in accounts receivable-trade	(1,483,140)	2,159,876	(802,605)
(Increase) decrease in inventories	(1,857,809)	1,160,316	(542,784)
Decrease (increase) in accounts payable-trade	(31,292)	306,312	212,253
Increase in consumption tax receivable	—	—	(80,085)
(Increase) decrease in advance payments	—	(207,972)	176,519
Bonus paid to directors and corporate auditors	(4,950)	(20,150)	(2,400)
Other	(43,299)	(212,349)	107,307
Sub total	(946,147)	3,919,923	251,572
Interest and dividends received	3,080	2,567	70
Interest paid	(56,772)	(70,122)	(22,369)
Payments on liquidation of subsidiaries	—	—	(273,755)
Income taxes paid	(1,096,606)	(1,089,172)	(298,743)
Other	—	(26,553)	—
Net cash (used in) provided by operating activities	(2,096,446)	2,736,642	(343,225)
Cash flows from investing activities:			
Increase in time deposits	(258,400)	(24,820)	(43,033)
Decrease in time deposits	582,000	49,185	20,000
Purchases of marketable securities	(100,241)	—	—
Proceeds from sales of marketable securities	100,050	—	—
Purchases of investment securities	—	(4,990)	(98)
12 Proceeds from sales of investment securities	—	18,873	99,916
Payments for acquisition of subsidiary's equity	—	—	(11,246)
Payment for acquisition of Cygnet Technologies, Inc.	(45,393)	—	—
Proceeds from acquisition of Spinnaker Systems, Inc.	270,387	—	—
Purchases of tangible fixed assets	(143,372)	(178,083)	(43,534)
Proceeds from sales of tangible fixed assets	68	—	9,282
Purchases of intangible fixed assets	(169,336)	(205,732)	(30,717)
Proceeds from sales of intangible fixed assets	—	50	—
Increase in investment in partnership	—	—	(10,749)
Proceeds from sales of investment to partnership	—	—	8,054
Proceeds from collections of loans	271	4,697	5,845
Increase in loans	(16,035)	(63,400)	—
Proceeds from surrender of insurance policy	—	32,392	120,435
Increase in other investments	(73,320)	(52,563)	(46,319)
Decrease in other investments	16,501	1,212	16,604
Net cash provided by (used in) investing activities	163,178	(423,179)	94,442
Cash flows from financing activities:			
Net increase (decrease) in short term bank loans	1,920,000	(2,188,606)	(90,402)
Proceeds from long term bank loans	61,765	141,200	4,140
Repayment of long term bank loans	(50,390)	(112,784)	(25,490)
Purchases of treasury stock	(74,181)	(7,061)	(1,332)
Proceeds from sales of treasury stock	76,904	7,111	—
Proceeds from issuance of common stock	—	—	20,000
Cash dividends paid to minority shareholders	(935)	(935)	(665)
Cash dividends paid	(78,964)	(98,139)	(117,610)
Other	(5,015)	23	—
Net cash provided by (used in) financing activities	1,849,183	(2,259,191)	(211,359)
Effect of exchange rate changes on cash and cash equivalents	10,250	66,967	(7,138)
Net (decrease) increase in cash and cash equivalents	(73,834)	121,238	(467,281)
Cash and cash equivalents at beginning of period	1,605,270	1,531,436	1,652,477
Decrease in cash and cash equivalents due to decrease in consolidated subsidiaries	—	(197)	(43,679)
Cash and cash equivalents at end of period	1,531,436	1,652,477	1,141,516

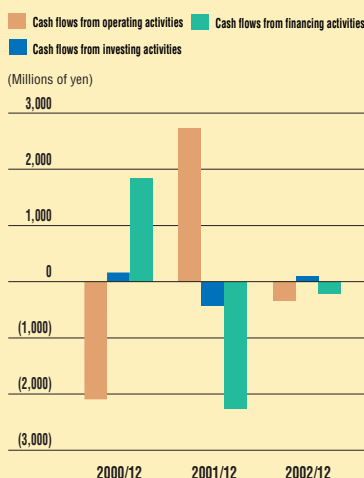
POINT 11

- The increase in account receivables and inventories is mainly the result of improved sales and increase in orders during the period.

POINT 12

- Proceeds from sales of investment securities reflects the redemption of investment trust beneficiary certificates.

Cash flows



Notes to consolidated financial statements (January 1, 2002 - December 31, 2002)

Material information regarding preparation of consolidated financial statements

1. Scope of consolidation

- (1) Number of consolidated subsidiaries: 3

Names of consolidated subsidiaries:

Alpha Electronics, Inc.
Spinnaker Systems, Inc.
axelec corporation

Cygnat Technologies, Inc., treated as a consolidated subsidiary in the previous year, was excluded from consolidation results starting with the second half of this year as liquidation procedures have progressed and the company became insignificant for the purpose of consolidation.

- (2) Names of unconsolidated subsidiaries:

Cygnat Technologies, Inc.
AlphaMetric, Inc.
Alpha Electron (HK) Co. Ltd.

(Reasons for exclusion from consolidation)

Scale of operations of these unconsolidated subsidiaries are small and their total assets, revenues, net income (as calculated by the equity method) and retained earnings (as calculated by the equity method) have no significant impact on the consolidated financial statements. Alpha Electron (HK) Co. Ltd. was established during this consolidated accounting period.

2. Application of the equity method

- (1) Number of associated companies to which the equity method is applicable: 1

Name of the associated company to which the equity method is applicable:

HYPER-PALTEK Corporation

- (2) Name of non-consolidated subsidiary to which the equity method is not applicable:

Alpha Electron (HK) Co. Ltd.

(Reasons for exclusion from consolidation)

Non-consolidated subsidiaries to which the equity method is not applicable have no significant impact on the consolidated net income and consolidated retained earnings.

In addition, non-consolidated subsidiaries all combined do not have a significant impact on the consolidated results.

3. Accounting period of consolidated subsidiaries

Until the previous accounting period, Alpha Electronics, Inc., one of the Company's consolidated subsidiaries, had its annual accounting period ending on September 30. Effective this consolidated accounting period, Alpha Electronics, Inc. changed its accounting period to end on December 31. The balance sheet as of December 31, 2002, income statement and cash flow statement for the 15-month period between October 1, 2001 and December 31, 2002 were used for consolidation.

4. Significant accounting policies

- (1) Valuation of material assets

(A) Securities:

Available-for-sale securities:

Available-for-sale securities with market values:
Stated at fair market value as of the balance sheet date.
(Unrealized gains and losses are reported in the shareholders' equity section of the consolidated balance sheet. Sales cost is calculated using the moving average method)

Available-for-sale securities without market values:

Stated at moving average cost.

(B) Derivatives:

As a principle, derivatives are stated at fair market value.

(C) Inventories:

(a) Merchandise:

Stated by moving average cost (last purchased price method used by some of the consolidated subsidiaries)

(b) Supplies:

Stated by last purchased price method

- (2) Depreciation of fixed assets

(A) Tangible fixed assets:

Declining balance method (Note: Buildings, excluding ancillary facilities, acquired on or after April 1, 1998 are depreciated based on the straight line method)

Useful lives are as follows:

Buildings 10 – 45 years
Vehicle equipment 6 years
Furniture and fixtures 5 – 15 years

(B) Intangible fixed assets

The straight line method.

Useful life of the software for internal use is 5 years.

- (3) Allowances

(A) Allowance for doubtful accounts:

An allowance for doubtful accounts is provided to cover possible losses from bad debts. The allowance with respect to non-classified loans/receivables is calculated based on historical default rates. For classified loans/receivables, the Company and its domestic consolidated subsidiaries states an amount deemed to be unrecoverable based on the prospect of recovery of individual loans/receivables.

(B) Accrued bonuses:

Reserves are provided to cover the estimated amount of bonuses payable to employees.

(C) Liability for employees' retirement benefits:

The amount estimated to represent the potential liability, as of the end of this consolidated accounting period, is calculated by taking retirement benefit liabilities and the estimated value of pension assets into consideration.

(D) Liability for directors' and corporate auditors' retirement benefits:

An allowance is provided by the Company and a domestic subsidiary to cover the estimated amount of retirement benefits payable to directors and corporate auditors.

- (4) Translation of foreign currency denominated assets and liabilities into Japanese yen

Foreign currency denominated monetary rights and obligations are translated into Japanese yen using the prevailing spot exchange rate as of the consolidated balance sheet date. Translation differences are recognized as foreign exchange gains or losses. Foreign currency denominated monetary obligations that are subject to hedging by forward foreign exchange contracts are translated into Japanese yen using the actual contracted exchange rate.

- (5) Lease transactions

Finance leases for which ownership does not transfer to the lessees are not capitalized, and are accounted for in the same manner as operating leases.

- (6) Hedge accounting

(A) Hedge accounting method:

The Company adopts deferred hedge accounting. Derivatives that meet the criteria for hedging accounting are accounted for using deferral hedge accounting, which requires unrealized gains or losses to be deferred as liabilities or assets. Forward foreign exchange contracts that are effective hedges are accounted for using the allocation method, which requires recognized foreign currency receivables or payables to be translated using the corresponding foreign exchange contract rates.

(B) Hedging instruments and targets:

Hedging instruments:

Forward foreign exchange contract

Hedging targets:

Foreign currency denominated monetary liabilities and transactions scheduled to be denominated in a foreign currency.

(C) Hedging policies:

Derivative transactions are used only by the Company. Eligible hedging instruments are approved at the Board of Directors Meeting at the time of the preparation of the import plan.

(D) Method for assessing effectiveness of hedges:

Accumulated changes in the cash flow of hedged items are compared to the accumulated changes in the cash flow of hedging instruments on a semi-annual basis. The effectiveness of hedging is evaluated by taking the degree of changes in cash flows of the hedged item and hedging transaction into consideration.

(7) Other

Treatment of consumption tax:

Transactions subject to consumption tax are recorded at amounts exclusive of consumption taxes.

5. Valuation of assets and liabilities of consolidated subsidiaries

The assets and liabilities of the subsidiaries are evaluated using the fair value at the time the respective subsidiaries were initially consolidated.

6. Amortization of goodwill

Goodwill is amortized in equal amounts over a five year period. In the event that the amount is minimal, the amount is expensed in the year in which the adjustment is made.

With regard to the goodwill recognized at the time of the acquisition of Spinnaker Systems, Inc. shares by the Company, the entire amount of unamortized balance as of the close of this accounting period was fully expensed and recognized as an extraordinary loss.

7. Consolidated statement of retained earnings

The Consolidated statement of retained earnings is based on the officially confirmed appropriation schedules of the consolidated subsidiaries for the year.

8. Cash and cash equivalents

Included in "cash and cash equivalents" in the statements of cash flows are cash in hand, demand deposits, and short-term investments with maturities arriving in three months from the date of acquisition that are readily convertible to cash and are subject to minimum risk of price fluctuations.

Additional information

(Presentation of consolidated balance sheets and consolidated statements of retained earnings)

The shareholders' equity section of the consolidated balance sheets and consolidated statements of retained earnings are presented in a manner consistent with the Regulations Concerning Consolidated Financial Statements as revised in accordance with the provisions of the second paragraph of the Supplementary Provision to the "The Cabinet Office Ordinance Regarding Partial Revision of the Regulations Concerning Terminology, Forms and Preparation of Consolidated Financial Statements (The Cabinet Office Ordinance No. 11 on March 26, 2002)."

(Treasury stock and reversal of legal reserves)

Effective this consolidated accounting period, the Company has adopted the "Accounting Standard for Treasury Stock and Reduction of Legal Reserves" (Financial Accounting Standards No. 1.) The change on the consolidated operating results for the consolidated accounting period under review has no effect.

Notes

(Consolidated balance sheets)

(Thousands of yen)

- Amount of notes receivable discounted : ¥126,842
- Amount of accounts receivable-trade offered as collateral : ¥797,649
- Investment in non-consolidated subsidiaries : ¥1,794

(Consolidated statements of income)

(Thousands of yen)

- Breakdown of gains on sale of fixed assets:

Furniture and fixtures	¥4
------------------------	----
- Breakdown of loss on devaluation of planned sales of fixed assets whose book values have substantially declined:

Buildings	¥2,347
Land	¥20,238
- Breakdown of loss on disposal of fixed assets:

Buildings	¥4,141
Furniture and fixtures	¥4,168
Software	¥2,322
- Breakdown of loss on liquidation of subsidiaries:

Loss on sale of fixed assets	¥2,589
Loss on devaluation of fixed assets	¥112,300
Loss on devaluation of inventories	¥71,322
Other liquidation expenses	¥223,663
Reversal of foreign exchange translation adjustment	(¥23,569)

(Consolidated statements of cash flows)

(Thousands of yen)

"Cash and bank deposits" on the consolidated balance sheet and "cash and cash equivalents" on the consolidated statement of cash flows are reconciled as follows:

	As of December 31, 2002
Cash and deposits	¥1,187,549
Time deposits with maturities longer than 3 months	(¥46,033)
Cash and cash equivalents	<u>¥1,141,516</u>

(Lease transactions)

(Thousands of yen)

Finance leases where ownership does not transfer to the lessee:

- Acquisition cost equivalent, accumulated depreciation equivalent and book value equivalent of leased properties as of the end of this consolidated accounting period.

	Acquisition cost equivalent	Accumulated depreciation equivalent	Book value equivalent
Furniture and fixtures	28,000	9,333	18,666
Software	560,391	266,143	294,248
Total	588,391	275,476	312,915

- Future minimum lease payments:

Within one year	¥118,350
Over one year	¥201,066
Total	¥319,416

- Lease expenses and pro forma data as to depreciation expenses and interest expenses are summarized as follows:

Lease payments	¥123,190
Depreciation equivalent	¥117,678
Interest expense equivalent	¥6,967

- Calculation of depreciation equivalent:

Depreciation is based on the straight line method over the lease term of the leased assets with no residual value.

- Calculation of interest expense equivalent:

The interest expense equivalent is calculated by taking the difference between the total amount of lease payment and acquisition cost equivalent of the leased property, and amortizing it over the lease period based on the interest method.

(Securities)

Securities as of the term ended December 31, 2002

1. Available-for-sale securities with market values

(Thousands of yen)

	Type of securities	Acquisition cost	Book value	Difference
Fair market value exceeds acquisition cost	(1) Stocks	13,370	16,909	3,538
	(2) Bonds			
	JGB, Local government bonds	—	—	—
	Corporate bonds	—	—	—
	Other	—	—	—
	(3) Other	27,785	28,759	974
	Sub-total	41,156	45,669	4,512
Fair market value does not exceed acquisition cost	(1) Stocks	9,977	8,209	(1,767)
	(2) Bonds			
	JGB, Local government bonds	—	—	—
	Corporate bonds	—	—	—
	Other	—	—	—
	(3) Other	82,429	47,142	(35,286)
	Sub-total	92,406	55,352	(37,053)
	Total	133,563	101,022	(32,541)

Note: During the term ended December 31, 2002, an impairment loss in the amount of ¥3,665 thousand was recognized for available-for-sale securities with market values.

2. Available-for-sale securities sold during the period

(Thousands of yen)

Amount sold	Total gain on sales	Total loss on sales
109,720	4,289	83

3. Major components of debt and equity securities without market values

(Thousands of yen)

	Amount stated in consolidated B/S
Available-for sale securities	
Unlisted securities (excluding OTC-traded stocks)	39,450
Total	39,450

(Derivative transactions)

1. Matters related to condition of transactions

(1) Types of derivatives used by the Group:

Forward foreign exchange contracts are the only derivative instruments used by the Group. Among the Group companies, the Company is the only user of derivative instruments. The following information therefore relates to transactions engaged by the Company.

(2) Transaction policy and purpose of use:

Derivative instruments are used by the Company in the normal course of its business in order to effectively manage the risk arising from fluctuations in foreign exchange rates.

Forward foreign exchange contracts are used to hedge the risk of foreign exchange fluctuations with respect to future scheduled transactions denominated in foreign currencies as well as foreign currency denominated obligations. Forward foreign exchange contracts are not used for speculative purposes or for the purpose of realizing short-term trading gains.

Derivative transactions are accounted for using hedge accounting. Details with respect to the method of hedge accounting is provided in "Material information regarding preparation of consolidated financial statements" (Section 4. "Significant accounting policies", Paragraph (6) "Hedge accounting")

(3) Risks associated with derivative transactions:

Derivative instruments used by the Company involve credit risk and market risk. Credit risk refers to the risk of default by the counter party of the derivative transaction concerned. Market risk refers to potential loss that may be realized by the fluctuations in foreign exchange rates. The Company believes that credit risk associated

with the transactions entered into by the Company is minimal as counter parties are all highly rated domestic financial institutions. The forward foreign exchange contracts entered into by the Company are exposed to future fluctuations in foreign exchange rates. However, it should be noted that these forward exchange contracts are engaged for the purpose of hedging the foreign currency denominated obligations on the Company's balance sheets, and that changes in the value of derivatives offset the changes in the value of hedged obligations.

(4) Risk management:

Hedging policies are determined at the Board of Directors' Meeting at the time of the formulation of the import schedule. Transactions are executed by the Finance Team, Finance/Legal Group, Operational Service Division based on the policies determined by the Board with specific transactional approval by the director in charge of the Division. The Finance Team prepares a position report in order to monitor and analyze outstanding transactions and to report to the director in charge.

2. Matters related to estimated fair value of transactions

No details are provided herein as these transactions are for hedging purpose only.

(Retirement benefits)

1. The retirement benefit program adopted

The Company has an employees' pension fund and a tax-qualified pension plan, both of which are defined benefit plans. Our domestic consolidated subsidiaries have lump-sum retirement payment plans and mutual funds for retirement allowances for medium and small companies.

The company has joined the welfare pension fund for the computer industry association, a jointly established contributory plan, which is prescribed in the article 33 of the Accounting Standards for Retirement Benefits.

Total amount of the plan assets for the Company as of December 31, 2002 was ¥179,995 thousand.

2. Retirement benefit obligations

(Thousands of yen)

	As of December 31, 2002
(1) Projected benefit obligations	(89,695)
(2) Fair value of plan assets	86,674
(3) Net amount stated in the consolidated B/S ((1) + (2))	(3,021)
(4) Prepaid pension cost	7,581
Liability for employees' retirement benefits ((3) – (4))	(10,603)

3. Pension and severance costs

(Thousands of yen)

	January 1, 2002-December 31, 2002
Retirement benefit costs	
(1) Service cost	14,915
(2) Amortization of net transition obligation	—
Subtotal	14,915
(3) Contribution to the jointly established welfare pension fund	20,756
(4) Contribution to the mutual funds for retirement allowances for medium and small companies	2,463
(5) Special retirement benefit	8,878
Retirement benefit costs	47,014

4. Assumptions used in the accounting for retirement benefit obligations

Method of computation of projected benefit obligation

The simplified method is used in calculating the projected benefit obligation.

(Tax effect accounting)

(Thousands of yen)

1. A breakdown of deferred tax assets and liabilities are noted below:

Deferred tax assets:

Loss on valuation of inventories	27,893
Allowance for bad debts in excess of tax limit	27,091
Liability for retirement benefits to directors' and corporate auditors'	104,068
Loss on devaluation of investment securities	15,586
Revaluation loss on investment securities	15,563
Loss on liquidation of subsidiaries and associated companies	660,950
Loss carry forward	34,641
Accrued enterprise tax	17,862
Other	45,493
Subtotal	949,152
Valuation allowance	(38,927)
Total deferred tax assets	910,224

Deferred tax liabilities:

Revaluation gain on investment securities	(2,764)
Other	(14,124)
Total deferred tax liabilities	(16,888)
Net deferred tax assets	893,335

2. Reconciliation between the statutory tax rate and the effective tax rate:

(%)

Statutory tax rate	42.00
(Decrease) increase in taxes resulting from:	
Entertainment expenses, etc. non deductible portion	(5.62)
Amortization of goodwill	(164.27)
Inhabitants tax	(3.33)
Effect of applying equity method	(1.75)
Loss on liquidation of subsidiaries	23.74
Effect of the increase in valuation allowances	205.80
Other	1.71
Effective income tax rate	98.28

(Segment information)

1. Business segment information

Information by business segment is omitted as the semi-conductor-related business accounts for more than 90% of the total consolidated sales, operating income and total assets.

2. Geographic segment information

Information by geographic segment is omitted as the domestic business accounts for more than 90% of the total consolidated sales and total assets.

3. Overseas sales

Overseas sales information is omitted as it accounts for less than 10% of the total consolidated sales.

(Related party transactions)

Not available

4. Purchases, Orders Received and Sales

(1) Purchases

Purchases made during the term ended December 31, 2002 are as follows:

(Thousands of yen)

Business Segment	January 1, 2001-December 31, 2001		January 1, 2002-December 31, 2002		Change from the previous year (%)	
	Amount	Ratio (%)	Amount	Ratio (%)	Amount	Change (%)
Semiconductor business	11,394,258	99.6	12,046,785	100.0	652,527	5.7
Communications equipment business	48,781	0.4	416	0.0	(48,365)	(99.2)
Total	11,443,039	100.0	12,047,201	100.0	604,162	5.3

Note: Consumption tax is not included in the above figures.

(2) Orders received

Orders received during the term ended December 31, 2002 as follows:

(Thousands of yen)

Business Segment	January 1, 2001-December 31, 2001		January 1, 2002-December 31, 2002		Change from the previous year (%)	
	Orders received	Backlog	Orders received	Backlog	Orders received	Backlog
Semiconductor business	15,317,609	805,728	16,446,698	1,730,974	1,129,088	925,245
Communications equipment business	187,447	92,366	480	—	(186,967)	(92,366)
Total	15,505,057	898,095	16,447,178	1,730,974	974,121	832,878

Note: Consumption tax is not included in the above figures.

(3) Sales

Sales during the term ended December 31, 2002 as follows:

(Thousands of yen)

Business Segment	January 1, 2001-December 31, 2001		January 1, 2002-December 31, 2002		Change from the previous year (%)	
	Amount	Ratio (%)	Amount	Ratio (%)	Amount	Change (%)
Semiconductor business	17,348,017	99.5	15,613,820	100.0	(1,734,197)	(10.0)
Communications equipment business	95,080	0.5	480	0.0	(94,600)	(99.5)
Total	17,443,098	100.0	15,614,300	100.0	(1,828,798)	(10.5)

Note: 1. Consumption tax is not included in the above figures.

2. Sales by major customers and the ratio to total sales for the last two accounting periods are as follows:

Clients	January 1, 2001-December 31, 2001		January 1, 2002-December 31, 2002	
	Amount	Ratio (%)	Amount	Ratio (%)
NEC Corporation	3,951,547	22.7	2,406,727	15.4

Note: Consumption tax is not included in the above figures.

Non-consolidated Balance Sheets

(Thousands of yen)

	As of December 31, 2000	As of December 31, 2001	As of December 31, 2002	
(Assets)				
Current assets				
13	Cash and bank deposits	862,988	1,323,375	746,779
	Notes receivable	1,422,061	911,163	1,077,930
	Accounts receivable	4,056,379	2,264,511	2,834,474
	Marketable securities	172,969	—	—
	Merchandise	3,696,244	2,505,379	3,072,386
	Supplies	8,518	8,052	5,674
	Prepaid expenses	115,503	117,570	117,852
	Deferred tax assets	89,102	259,554	364,173
	Other accounts receivable	183,298	152,283	19,708
	Consumption tax receivable	—	230,781	340,476
	Treasury stock	384	—	—
	Other current assets	502	15,268	1,375
	Allowance for doubtful accounts	(35,330)	(2,924)	(6,712)
	Total current assets	10,572,622	7,785,015	8,574,119
Fixed assets				
Tangible fixed assets				
14	Buildings	156,550	160,107	155,105
	Accumulated depreciation	(49,741)	(64,712)	(73,959)
	Furniture and fixtures	348,338	357,931	353,228
	Accumulated depreciation	(171,743)	(231,030)	(241,357)
	Land	56,868	56,868	36,629
	Total tangible fixed assets	340,271	279,164	229,646
Intangible fixed assets				
	Telephone rights	2,577	2,577	2,577
	Trade marks	500	400	300
	Software	176,987	253,626	201,124
	Total intangible fixed assets	180,064	256,603	204,001
Investments and other assets				
15	Investment securities	130,614	245,160	109,315
	Investments in subsidiaries and associated companies	1,335,890	909,142	903,707
	Investments in partnerships	63,934	66,496	61,400
	Long-term loans receivable	—	58,461	53,302
	Long-term loans to employees	508	749	62
	Claims in bankruptcy	—	13,518	12,565
	Long-term prepaid expenses	3,251	19,040	8,861
	Deferred tax assets	88,845	497,207	509,538
	Fixed leasehold deposits	132,616	132,026	131,110
	Other	110,156	108,775	84,740
	Allowance for investment losses	(32,000)	—	—
	Allowance for doubtful accounts	(113)	(13,518)	(65,868)
	Total investments and other assets	1,833,703	2,037,060	1,808,736
	Total fixed assets	2,354,038	2,572,828	2,242,384
	Total Assets	12,926,661	10,357,844	10,816,504
(Liabilities)				
Current liabilities				
	Accounts payable	499,353	758,400	1,082,716
	Short-term bank loans	3,450,000	1,150,000	1,150,000
	Other payables	347,438	182,731	206,841
	Accrued expenses	34,986	30,343	28,228
	Income taxes payable	497,000	3,045	197,000
	Deposits received	19,284	17,087	17,508
	Accrued bonuses	35,673	25,192	34,424
	Reserve for operating losses of subsidiaries	—	403,745	12,482
	Other current liabilities	125	1,918	646
	Total current liabilities	4,883,860	2,572,463	2,729,847
Long-term liabilities				
	Liabilities for directors' and corporate auditors' retirement benefits	187,257	183,712	201,698
	Other long-term liabilities	30,269	58,684	47,475
	Total long-term liabilities	217,526	242,397	249,173
	Total Liabilities	5,101,387	2,814,861	2,979,021
(Shareholders' equity)				
Capital stock				
	Capital surplus	1,335,487	1,335,487	1,335,487
	Capital reserve	1,674,375	1,674,375	1,674,375
	Total capital surplus	1,674,375	1,674,375	1,674,375
Retained earnings				
	Legal reserve	34,100	46,100	46,100
	Voluntary reserve	2,996,512	4,343,036	4,318,560
	Reserve for the development of domestic market for imported goods	96,512	43,036	18,560
	General reserve	2,900,000	4,300,000	4,300,000
	Unappropriated retained earnings	1,784,798	148,296	482,060
	Total retained earnings	4,815,410	4,537,432	4,846,720
	Net unrealized loss on securities	—	(3,577)	(17,032)
	Treasury stock	—	(734)	(2,067)
	Total shareholders' equity	7,825,274	7,542,983	7,837,483
	Total liabilities and shareholders' equity	12,926,661	10,357,844	10,816,504

POINT 13

- The increase in notes receivable, accounts receivable and merchandise is mainly the result of improved sales and increase in orders during the period.

POINT 14

- The decrease in buildings and land mainly caused by the devaluation of ¥22 million for fixed assets planned to sales whose book values have substantially declined against current values.

POINT 15

- The decrease in investment securities reflects the redemption of investment trust beneficiary certificates.

Non-Consolidated Statements of Income

Non-consolidated Statements of Income

(Thousands of yen)

	January 1, 2000- December 31, 2000	January 1, 2001- December 31, 2001	January 1, 2002- December 31, 2002
Net sales	16,255,560	13,624,685	11,554,934
Cost of sales	11,348,032	9,852,062	8,310,670
Gross profit	4,907,528	3,772,623	3,244,263
16 Selling, general and administrative expenses	2,656,080	2,523,032	2,359,646
Provision for doubtful accounts	2,475	—	11,296
Salary	741,921	721,943	693,287
Bonuses	206,065	165,342	187,409
Provision for bonuses	33,174	24,241	34,021
Provision for directors' and corporate auditors' retirement benefits	14,766	12,260	17,985
Rent expense	315,823	395,019	386,361
Depreciation	103,060	141,375	135,032
Commissions paid	186,406	204,983	183,790
Other	1,052,385	857,865	710,460
Operating income	2,251,448	1,249,590	884,617
Non-operating income	130,117	36,428	210,307
Interest income	1,521	1,490	501
Interest income on securities	1,535	—	—
Dividend income	5,065	5,068	5,338
Foreign exchange gain	110,215	—	174,530
Gain on sale of investment securities	14	13,999	4,289
Rent revenue	—	4,453	10,964
Other	11,764	11,416	14,682
Non-operating expenses	63,466	134,029	106,872
Interest expense	45,111	47,581	16,524
Provision for doubtful accounts	—	—	57,522
Foreign exchange loss	—	56,763	—
Loss on surrender of insurance policy	—	8,867	14,094
Commissions paid	—	3,742	14,000
Other	18,354	17,074	4,730
Ordinary income	2,318,100	1,151,989	988,053
Extraordinary income	47,168	19,000	—
Previous year adjustment income	47,168	—	—
Reversal of allowance for doubtful accounts	—	19,000	—
Extraordinary losses	34,817	1,436,343	232,521
Loss on sales of fixed assets	2,817	—	—
17 Loss on disposal of fixed assets	—	—	22,585
Loss on devaluation of fixed assets	—	—	8,225
Loss on devaluation of investment in subsidiaries	—	986,377	20,000
Provision for Investment losses	32,000	—	—
Allowance for operating losses of subsidiaries	—	403,745	12,482
Loss on sale of investment securities	—	39,920	—
Loss on devaluation of investment securities	—	—	25,988
18 Loss on liquidation of subsidiaries	—	—	143,240
Charge for full amount of transitional obligation for employees' retirement benefits	—	6,300	—
Income (Loss) before income taxes	2,330,451	(265,353)	755,531
Income taxes-current	1,006,842	474,038	435,066
Income taxes-deferred	(19,794)	(576,223)	(107,206)
Net income (loss)	1,343,403	(163,168)	427,672
Retained earnings at the beginning of period	213,354	311,464	54,387
Adjustment on tax effect accounting at previous year	158,153	—	—
Reversal of reserve for development of domestic market for imported goods adopting tax effect accounting	69,888	—	—
Unappropriated retained earnings	1,784,798	148,296	482,060

POINT

16

- The decrease in S.G.&A. expenses is the result of lower selling costs, mainly advertising and sales promotion fee which including in other account.

POINT

17

- Loss on disposal of fixed assets reflects the devaluation for fixed assets planned to sales whose book values have substantially declined against current values.

POINT

18

- Loss on liquidation of subsidiaries mainly reflects those losses incurred this current period for the liquidation of Cygnet Technologies, Inc.

Appropriation Statements

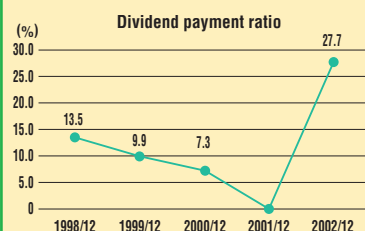
Statements of Retained Earnings

(Thousands of yen)

	As of December 31, 2000	As of December 31, 2001	As of December 31, 2002
Unappropriated retained earnings	1,784,798	148,296	482,060
Reversal of voluntary reserve	53,476	24,476	18,560
Reversal of reserve for development of domestic market for imported goods	53,476	24,476	18,560
Total	1,838,274	172,772	500,620
Appropriations	1,526,810	118,384	230,772
Legal reserve	12,000	—	—
Dividends	98,660	118,384	118,362
Bonuses paid to directors and corporate auditors	16,150	—	12,410
(Bonuses for corporate auditors)	(4,025)	(—)	(1,830)
Voluntary reserve	—	—	—
General reserve	1,400,000	—	100,000
Unappropriated retained earnings carried forward	311,464	54,387	269,847

Profit Distribution

Our dividend policy reflects our recognition of the importance of returning profit to our shareholders and investors. We intend to maintain an appropriate level of profit distributions by working to continuously improve our business performance and profit margins while strengthening our internal reserves. Accordingly, our dividend policy reflects these considerations.



*In fiscal 2001, dividend of ¥10 per share was declared. As a net loss was recorded for the period, the dividend payout ratio was not calculated.

Notes to non-consolidated financial statements (January 1, 2002 - December 31, 2002)

Summary of significant accounting policies

1. Valuation of securities

- (1) Securities of subsidiaries and associated companies:
Stated at moving average cost
- (2) Available-for-sale securities:
Available-for-sale securities with market values:
Stated at fair market value as of balance sheet date (Unrealized gains and losses are reported in the shareholders' equity section of the non-consolidated balance sheet. Sales cost is calculated using the moving average method.)
Available-for-sale securities without market values:
Stated at moving average cost.

2. Valuation of derivative instruments, etc.

- Derivatives:
As a principle, derivatives are stated at fair market value.

3. Valuation of inventories

- (1) Merchandise:
Stated by moving average cost.
- (2) Supplies:
Stated by last purchased price method.

4. Depreciation of fixed assets

- (1) Tangible fixed assets:
Declining balance method (Note: Buildings, excluding ancillary facilities, acquired on or after April 1, 1998 are depreciated based on the straight line method.)
Useful lives are as follows:
Buildings 10 – 45 years
Furniture and fixtures 5 – 15 years
- (2) Intangible fixed assets:
The straight line method
Useful life of the software for internal use is 5 years.

5. Translation of foreign currency denominated assets and liabilities into Japanese yen

Foreign currency denominated monetary rights and obligations are translated into Japanese yen using the prevailing spot exchange rate as of the balance sheet date. Translation differences are recognized as foreign exchange gains or losses.
Foreign currency denominated monetary obligations that are subject to hedging by forward foreign exchange contracts are translated into Japanese yen using the actual contracted exchange rate.

6. Allowances

- (1) Allowance for doubtful accounts:
An allowance for doubtful accounts is provided to cover possible losses from bad debts. The allowance with respect to non-classified loans/receivables is calculated based on historical default rates. For classified loans/receivables, the Company states an amount deemed to be unrecoverable based on the prospect of recovery of individual loans/receivables.
- (2) Accrued bonuses:
Reserves are provided to cover the estimated amount of bonuses payable to employees.
- (3) Liability for employees' retirement benefits:

The amount estimated to represent the potential liability as of the end of fiscal year is calculated by taking retirement benefit liabilities and the estimated value of pension assets into consideration.

For the current fiscal year, prepaid pension cost in the amount of ¥7,581 thousand is recognized and included in the long-term prepaid expense account, as the plan assets exceeded the amount of retirement benefit obligations as of the end of the fiscal year.

- (4) Liability for directors' and corporate auditors' retirement benefits:
An allowance is provided to cover the estimated amount of retirement benefits payable to directors and corporate auditors.
- (5) Allowance for operating losses of subsidiaries:
An allowance is provided to cover potential losses related to business failure of subsidiaries by estimating the amount of loss incurred by the Company over and above the amount of investment.

7. Lease transactions

Finance leases for which ownership does not transfer to the lessee are not capitalized, and are accounted for in the same manner as operating leases.

8. Hedge accounting

- (1) Hedge accounting method:
The Company adopts deferred hedge accounting. Derivatives that meet the criteria for hedging accounting are accounted for using deferral hedge accounting, which requires unrealized gains or losses to be deferred as liabilities or assets. Foreign exchange contracts that are effective hedges are accounted for using the allocation method, which requires recognized foreign currency receivables or payables to be translated using the corresponding foreign exchange contract rates.
- (2) Hedge instruments and targets:
Hedging instruments:
Forward foreign exchange contract.
Hedging targets:
Foreign currency denominated monetary liabilities and transactions scheduled to be denominated in a foreign currency.
- (3) Hedging policies:
Eligible hedging instruments are approved at the Board of Directors Meeting at the time of the preparation of the import plan.

- (4) Method of assessing effectiveness of hedges:
Accumulated changes in the cash flow of hedged items are compared to the accumulated changes in the cash flow of hedging instruments on a semi-annual basis. The effectiveness of hedging is evaluated by taking the degree of changes in cash flows of the hedged item and hedging transaction into consideration.

9. Other

Treatment of consumption tax:
Transactions subject to consumption tax are recorded at amounts exclusive of consumption taxes.

Additional information

(Presentation of balance sheet)

The shareholders' equity section of the balance sheets are presented in a manner consistent with the Regulations Concerning Financial Statements as revised in accordance with the provisions of the second paragraph of the Supplementary Provision to the "The Cabinet Office Ordinance Regarding Partial Revision of the Regulations Concerning Terminology, Forms and Preparation of Financial Statements (The Cabinet Office Ordinance No. 11 on March 26, 2002)".

(Treasury stock and reversal of legal reserves)

Effective this fiscal year, the Company has adopted the "Accounting Standard for Treasury Stock and Reduction of Legal Reserves" (Financial Accounting Standards No. 1.) The change on the operating results for this fiscal year under review has no effect.

Notes

(Balance Sheet)

(Thousands of yen)

1. Total number of authorized shares : 23,562,000 shares
Total number of shares issued : 11,839,399 shares

2. Contingent liabilities (Thousands of yen)

(1) Guarantee of subsidiaries' borrowings from financial institutions:

Alpha Electronics, Inc.	¥270,002
axelec corporation	¥10,517
Total	¥280,519

(2) Guarantee of a subsidiary's accounts payable:

Alpha Electronics, Inc.	¥136,283
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(3) Guarantee of a subsidiary's obligations under discounted promissory notes:

Alpha Electronics, Inc.	¥57,390
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The above amounts represent net amounts of contingent liabilities after deducting the amount provided in the allowance for operating losses of a subsidiaries in the total amount of ¥12,482 thousand.

(Income statement)

(Thousands of yen)

1. Costs associated with programming, inspection and sorting of merchandise purchased.

Labor cost	¥20,774
Outsourcing cost	¥29,308
Depreciation	¥3,019
Other	¥22,162
Total	¥75,263

2. "Transfers to other accounts" represents the amount transferred from the merchandise account to the advertising expense account.

3. Breakdown of loss on disposal of fixed assets:

Buildings	¥2,197
Furniture and fixtures	¥3,705
Software	¥2,322

4. Breakdown of loss on devaluation of planned sales of fixed assets whose book values have substantially declined:

Buildings	¥2,347
Land	¥20,238

5. Breakdown of loss on liquidation of subsidiaries:

Cygnet Technologies, Inc.	¥137,421
AlphaMetric, Inc.	¥5,818

(Lease transactions)

(Thousands of yen)

Finance leases where ownership does not transfer to the lessee:

(1) Acquisition cost equivalent, accumulated depreciation equivalent and book value equivalent of leased properties as of the end of fiscal year.

	Acquisition cost equivalent	Accumulated depreciation equivalent	Book value equivalent
Software	560,391	266,143	294,248
Total	560,391	266,143	294,248

(2) Future minimum lease payments:

Within one year	¥112,791
Over one year	¥187,634
Total	¥300,426

(3) Lease expenses and pro forma data as to depreciation expenses and interest expenses are summarized as follows:

Lease payments	¥117,287
Depreciation equivalent	¥112,078
Interest expense equivalent	¥6,508

(4) Calculation of depreciation equivalent:

Depreciation is based on the straight line method over the lease term of the leased assets with no residual value.

(5) Calculation of interest expense equivalent:

The interest expense equivalent is calculated by taking the difference between the total amount of lease payments and acquisition cost equivalent of the leased property, and amortizing it over the lease period based on the interest method.

(Securities)

The Company held no securities with market values issued by subsidiaries and associated companies.

(Tax effect accounting)

(Thousands of yen)

1. A breakdown of deferred tax assets and liabilities are noted below:

Deferred tax assets:	
Loss on valuation of inventories	17,131
Liability for retirement benefits to directors' and corporate auditors'	84,713
Allowance for bad debts in excess of tax limit	27,091
Loss on devaluation of investment securities	14,068
Loss on liquidation of subsidiaries	231,173
Loss on valuation of investment in subsidiaries	438,176
Accrued enterprise tax	17,671
Other	49,481
Total deferred tax assets	879,508

Deferred tax liabilities:

Reserve for the development of domestic market for imported goods	(3,184)
Revaluation gain on investment securities	(2,611)
Total deferred tax liabilities	(5,796)
Net deferred tax assets	873,712

2. Reconciliation between the statutory tax rate and the effective tax rate is not provided as the difference between the two was insignificant.

Company Profile

(as of December 31, 2002)

- **Company Name** PALTEK Corporation
- **President** Tadahito Takahashi
- **Directors** 6
- **Corporate Auditors** 3
- **Employees** 169
- **Capital** 1,335,487,300 yen
- **Subsidiaries** Alpha Electoronics, Inc.,
Spinnaker Systems, Inc., axelec corporation,
Alpha Electron (HK), Inc.
- **Main Banks** Sumitomo Mitsui Banking Corporation,
UFJ Bank Limited., Mizuho Bank, Ltd.,
The Bank of Tokyo-Mitsubishi, Ltd.,
UFJ Trust Bank Limited.
- **Main Customers** NEC Corporation, Anritsu Corporation,
Sony Corporation,
Oki Electric Industry Co., Ltd.
- **Main Suppliers** Altera Corporation (U.S.A.)
Ashley Laurent, Inc. (U.S.A.)
AudioCodes Ltd. (ISRAEL)
BRECIS Communications Corp. (U.S.A.)
GSI Technology, Inc. (U.S.A.)
Metalink Ltd. (ISRAEL)
TransChip Inc. (ISRAEL)

(as of March 31, 2003)

- **Directors and Corporate Auditors**

President	Tadahito Takahashi
Managing Director and Vice President	Hiroyuki Takasaki
Director	Masanori Kanamori
Director	Yoshio Sakurai
Director	Tadashi Ito
Director	Masahiko Hirata
Standing Corporate Auditor	Yukio Miura
Corporate Auditor	Takashi Nakagami
Corporate Auditor	Kazutaka Muraguchi
Corporate Auditor	Tatsuo Kawasaki
- **Offices**
 - **Head Office**
Shin-Yokohama Square BLDG,
2-3-12 Shin-Yokohama, Kouhoku-ku, Yokohama
222-0033, Kanagawa, Japan
TEL : 045-477-2000
FAX : 045-477-2010
 - **Osaka Branch**
Omachi BLDG, 1-14-33 Esaka-cho, Suita, Osaka
564-0063, Japan
TEL : 06-6369-4070
FAX : 06-6369-4071
 - **Machida Logistics Center**
3F Tenko BLDG,17
687-1 Tsuruma, Machida, Tokyo 194-0004, Japan
(Logistics Center)
TEL : 042-788-5560
(Programming Center)
TEL : 042-788-5561 FAX : 042-788-5562

Stock Information

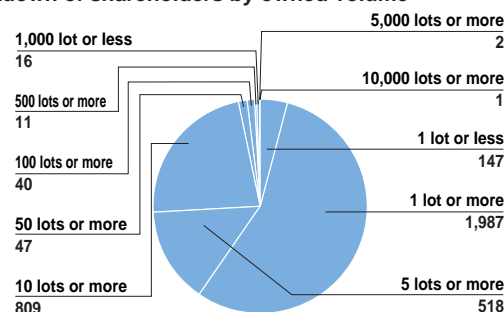
Stock Information (as of December 31, 2002)

- **Total number of authorized shares** 23,562,000 share
- **Total number of shares issued** 11,839,399 shares
- **Number of shares per lot** 100 shares
- **Number of shareholders** 3,578
- **Principal Shareholders**

Name	Number of shares held (thousand)	Equity Ownership (%)
Tadahito Takahashi	2,640.0	22.29
Dave Brauer	798.2	6.74
Trust & Custody Services Bank, Ltd.	665.0	5.61
Endeavor Corporation	593.2	5.01
UFJ Trust Bank Ltd.	435.7	3.68
Sadahiro Horiko	423.1	3.57
Japan Trustee Services Bank, Ltd.	410.3	3.46
The Master Trust Bank of Japan, Ltd.	342.1	2.88
Credit Agricole Indosuez Luxembourg S.A.	298.0	2.51
Keiko Takahashi	222.8	1.88

Note: This ranking shows real possession situation.

Breakdown of shareholders by owned volume



Breakdown of Ownership by shareholders type

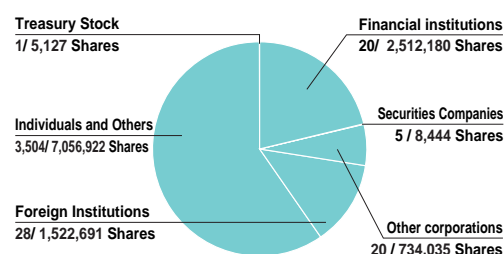


Photo on Cover Page [The infant tree of cedars]

Life is passed from the old trees to the seeds, and to the baby trees. This cycle of life reminds us the wealth of the forest and what is really important in our lives, and the true meaning of “wealth.”

Photographer: Hiroaki Yamashita

Hiroaki Yamashita was born in Kagoshima, the southern part of Kyushu in 1955. Since his early childhood, he has grown to love and developed a true passion for hiking in the mountains. During his university days, he developed a deep attraction to the beauty and nature of Yakushima Island. To this day, he spends a majority part of each year visiting and taking photographs of this spectacular Island.

I n f o r m a t i o n

Adoption of Online voting system

For your convenience, PALTEK has deployed an online voting system for our shareholders to exercise their voting rights. We have also prepared the English translation of the agenda of the General meeting of Shareholders. We sincerely hope that these measures will make it easy for our shareholders in overseas to communicate and participate in the stockholders meeting. Please access the website from the following URL address.

Web site for online voting : <http://www.koushi.ufjtrustbank.co.jp>

English documents : <http://agendabrief.ufjtrustbank.co.jp/>

Audio streaming on our Web site

Since last year, we have been offering audio streaming on our Web site and slides related to various announcements of interest to investors. We are trying to make these materials available as close to “real time” as possible, and we hope you find them useful.

URL: <http://www.paltek.co.jp/ir/Index.htm>



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<http://www.paltek.co.jp>