Consolidated Balance Sheets

March 31, 1998 and 1997

ASSETS	Millions of yen		Thousands of U.S. dollars (Note 1)
	1998	1997	**1998**
Current assets:			
Cash and cash equivalents (Notes 2-b and 5):			
Cash	**¥ 46,137**	¥ 62,026	**$ 349,523**
Time deposits	**94,535**	153,820	**716,174**
Marketable securities (Note 3)	**5,464**	8,765	**41,394**
Receivables:			
Trade notes	**5,908**	8,398	**44,758**
Trade accounts	**47,312**	62,517	**358,424**
Allowance for doubtful receivables	**(2,050)**	(1,457)	**(15,530)**
Inventories (Note 4)	**273,104**	320,536	**2,068,970**
Prepaid expenses and other current assets	**9,852**	11,248	**74,636**
Total current assets	**480,262**	625,853	**3,638,349**
Property, plant and equipment:			
Land	**156,989**	155,238	**1,189,311**
Buildings and structures	**255,477**	249,017	**1,935,432**
Machinery and equipment	**45,787**	43,395	**346,871**
Furniture and fixtures	**28,533**	27,247	**216,159**
Construction in progress	**16,886**	9,137	**127,924**
Total	**503,672**	484,034	**3,815,697**
Accumulated depreciation	**(157,129)**	(145,868)	**(1,190,371)**
Net property, plant and equipment	**346,543**	338,166	**2,625,326**
Investments and other assets:			
Investment securities (Note 3)	**62,359**	64,061	**472,417**
Investments in and advances to associated companies (Note 3)	**52,205**	49,971	**395,492**
Long-term loans	**23,671**	23,673	**179,326**
Lease deposits and other assets	**48,331**	44,480	**366,143**
Allowance for doubtful accounts	**(1,095)**	(848)	**(8,295)**
Total investments and other assets	**185,471**	181,337	**1,405,083**
Translation adjustments	**796**	588	**6,030**
Total	**¥1,013,072**	¥1,145,944	**$7,674,788**

See notes to consolidated financial statements.

LIABILITIES AND SHAREHOLDERS' EQUITY

	Millions of yen		Thousands of U.S. dollars (Note 1)
	1998	1997	1998
Current liabilities:			
Short-term bank loans (Note 5)	**¥ 38,315**	¥ 37,687	**$ 290,265**
Commercial paper (Note 5)	**30,000**		**227,273**
Current portion of long-term debt (Note 5)	**448**	109,571	**3,394**
Payables:			
Trade notes	**60,809**	84,346	**460,674**
Trade accounts	**52,003**	72,043	**393,962**
Construction	**7,839**	4,461	**59,386**
Deposits received (Note 6)	**50,949**	75,191	**385,978**
Income taxes payable	**11,062**	20,042	**83,803**
Accrued expenses and other current liabilities (Note 5)	**28,025**	33,547	**212,311**
Total current liabilities	**279,450**	436,888	**2,117,046**
Long-term liabilities:			
Long-term debt (Note 5)	**2,843**	3,236	**21,538**
Employees' retirement benefits (Note 7)	**17,130**	16,076	**129,773**
Long-term deposits received (Note 6)	**118,016**	105,326	**894,061**
Other long-term liabilities	**204**	261	**1,545**
Total long-term liabilities	**138,193**	124,899	**1,046,917**
Commitments and contingencies (Notes 12, 13 and 14)			
Shareholders' equity (Notes 5, 8 and 15)**:**			
Common stock, ¥50 par value — authorized, 1,900,000,000 shares; issued and outstanding, 523,893,045 shares in 1998 and 523,891,198 shares in 1997	**108,781**	108,780	**824,098**
Additional paid-in capital	**122,041**	122,040	**924,553**
Legal reserve	**12,718**	11,800	**96,348**
Retained earnings	**351,891**	341,538	**2,665,841**
Total	**595,431**	584,158	**4,510,840**
Treasury stock — at cost	**(2)**	(1)	**(15)**
Total shareholders' equity	**595,429**	584,157	**4,510,825**
Total	**¥1,013,072**	¥1,145,944	**$7,674,788**

Consolidated Statements of Income

Years ended March 31, 1998, 1997 and 1996

	Millions of yen			Thousands of U.S. dollars (Note 1)
	1998	1997	1996	**1998**
Net sales:				
Construction	**¥ 850,265**	¥ 960,226	¥ 877,343	**$6,441,402**
Real estate	**142,432**	155,828	128,143	**1,079,030**
Other	**77,092**	72,241	60,732	**584,030**
Total net sales	**1,069,789**	1,188,295	1,066,218	**8,104,462**
Cost of sales:				
Construction	**651,346**	736,300	674,751	**4,934,439**
Real estate	**126,747**	138,098	112,357	**982,932**
Other	**53,314**	47,989	40,895	**403,894**
Total cost of sales	**834,407**	922,387	828,003	**6,321,265**
Gross profit	**235,382**	265,908	238,215	**1,783,197**
Selling, general and administrative expenses	**186,932**	182,019	162,148	**1,416,152**
Operating income	**48,450**	83,889	76,067	**367,045**
Other income (expenses):				
Interest and dividends	**2,513**	2,509	3,106	**19,038**
Interest expense (Note 5)	**(1,160)**	(1,621)	(2,927)	**(8,788)**
Other — net (Notes 5 and 10)	**(1,160)**	(220)	702	**(8,788)**
Other income — net	**193**	668	881	**1,462**
Income before income taxes and translation adjustment	**48,643**	84,557	76,948	**368,507**
Income taxes (Note 11)	**28,270**	42,105	37,955	**214,166**
Translation adjustment			(1)	
Net income	**¥ 20,373**	¥ 42,452	¥ 38,992	**$ 154,341**

	Yen			U.S. dollars
Per share of common stock (Note 2-n)**:**				
Net income	**¥38.89**	¥82.76	¥80.91	**$0.29**
Diluted net income	**37.91**	79.89	77.66	**0.29**
Cash dividends applicable to the year	**17.00**	17.00	17.00	**0.13**

See notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

Years ended March 31, 1998, 1997 and 1996

	Thousands	Millions of yen			
	Outstanding number of shares of common stock	Common stock	Additional paid-in capital	Legal reserve	Retained earnings
Balance, April 1, 1995	478,608	¥ 76,900	¥ 90,163	¥ 10,084	¥ 278,811
Net income					38,992
Cash dividends, ¥17.0 per share					(8,136)
Bonuses to directors and corporate auditors					(191)
Transfer to legal reserve				842	(842)
Shares issued on conversion of convertible bonds	32	1	1		
Shares issued on exercise of warrants	20,650	14,559	14,558		
Translation adjustment					3
Balance, March 31, 1996	499,290	91,460	104,722	10,926	308,637
Net income					42,452
Cash dividends, ¥17.0 per share					(8,487)
Bonuses to directors and corporate auditors					(190)
Transfer to legal reserve				874	(874)
Shares issued on conversion of convertible bonds	9	7	7		
Shares issued on exercise of warrants	24,592	17,313	17,311		
Balance, March 31, 1997	523,891	108,780	122,040	11,800	341,538
Net income					**20,373**
Cash dividends, ¥17.0 per share					**(8,906)**
Bonuses to directors and corporate auditors					**(196)**
Transfer to legal reserve				**918**	**(918)**
Shares issued on conversion of convertible bonds	**2**	**1**	**1**		
Balance, March 31, 1998	**523,893**	**¥108,781**	**¥122,041**	**¥12,718**	**¥351,891**

	Thousands of U.S. dollars (Note 1)			
	Common stock	Additional paid-in capital	Legal reserve	Retained earnings
Balance, March 31, 1997	$824,090	$924,545	$89,393	$2,587,409
Net income				**154,341**
Cash dividends, $0.13 per share				**(67,469)**
Bonuses to directors and corporate auditors				**(1,485)**
Transfer to legal reserve			**6,955**	**(6,955)**
Shares issued on conversion of convertible bonds	**8**	**8**		
Balance, March 31, 1998	**$824,098**	**$924,553**	**$96,348**	**$2,665,841**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Years ended March 31, 1998, 1997 and 1996

	Millions of yen			Thousands of U.S. dollars (Note 1)
	1998	1997	1996	**1998**
Operating activities:				
Net income	**¥ 20,373**	¥ 42,452	¥ 38,992	**$ 154,341**
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	**18,710**	19,961	21,060	**141,742**
Loss (gain) on sales of marketable and investment securities	**(114)**	431	651	**(864)**
Write-down of marketable and investment securities	**555**	268		**4,205**
Provision for doubtful receivables and accounts	**998**	670	57	**7,561**
Loss on sales and disposal of property, plant and equipment	**2,055**	1,664	3,651	**15,568**
Equity in earnings of associated companies, less dividends	**306**	(849)	(1,955)	**2,318**
Gain resulting from associated company's public offering of stock (Note 10)			(615)	
Provision for employees' retirement benefits, net of payments	**1,054**	1,216	1,038	**7,985**
Amortization of deferred exchange gains		(2,455)	(4,914)	
Changes in certain assets and liabilities:				
Decrease (increase) in receivables	**17,540**	50,651	(6,561)	**132,879**
Decrease (increase) in inventories	**44,756**	(6,235)	(37,031)	**339,061**
Decrease (increase) in prepaid expenses and other current assets	**1,396**	2,319	(1,632)	**10,576**
Increase (decrease) in payables — trade	**(43,577)**	(35,660)	52,888	**(330,129)**
Increase (decrease) in current deposits received	**(24,242)**	6,662	22,179	**(183,652)**
Increase (decrease) in income taxes payable	**(8,980)**	(8,847)	6,249	**(68,030)**
Increase (decrease) in accrued expenses and other current liabilities	**(5,516)**	(196)	2,083	**(41,788)**
Other — net	**(509)**	638	(547)	**(3,856)**
Total adjustments	**4,432**	30,238	56,601	**33,576**
Net cash provided by operating activities	**24,805**	72,690	95,593	**187,917**
Investing activities:				
Capital expenditures	**(28,700)**	(34,133)	(20,640)	**(217,424)**
Purchases of marketable and investment securities	**(25,724)**	(43,761)	(54,731)	**(194,879)**
Net increase in lease deposits and other assets	**(4,785)**	(9,023)	(4,156)	**(36,250)**
Increase in investments in and advances to associated companies	**(2,497)**	(2,494)	(654)	**(18,916)**
Increase in long-term loans			(25)	
Proceeds from sales of marketable and investment securities	**30,279**	48,591	54,815	**229,386**
Proceeds from sales of property, plant and equipment	**6,546**	1,757	583	**49,591**
Decrease in investments in and advances to associated companies	**46**	92	317	**348**
Decrease in long-term loans	**2**	59	3,882	**15**
Net cash used in investing activities	**(24,833)**	(38,912)	(20,609)	**(188,129)**
Financing activities:				
Net increase in commercial paper	**30,000**			**227,273**
Net increase in long-term deposits received	**12,690**	9,521	6,866	**96,136**
Net increase (decrease) in short-term bank loans	**628**	(13)	454	**4,757**
Proceeds from long-term debt	**13**			**98**
Shares issued on exercise of warrants		34,624	29,117	
Repayments of long-term debt	**(109,571)**	(130,730)	(293)	**(830,083)**
Dividends paid	**(8,906)**	(8,487)	(8,136)	**(67,469)**
Net cash provided by (used in) financing activities	**(75,146)**	(95,085)	28,008	**(569,288)**
Net increase (decrease) in cash and cash equivalents	**(75,174)**	(61,307)	102,992	**(569,500)**
Cash and cash equivalents, beginning of year	**215,846**	277,153	174,161	**1,635,197**
Cash and cash equivalents, end of year	**¥140,672**	¥215,846	¥277,153	**$1,065,697**
Additional cash flow information:				
Interest paid	**¥ 1,934**	¥ 6,592	¥ 6,863	**$ 14,652**
Income taxes paid	**37,250**	50,952	31,706	**282,197**
Noncash financing activities:				
Convertible bonds converted into common stock	**2**	14	2	**16**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared from the consolidated financial statements issued for domestic reporting purposes in accordance with the provisions set forth in the Japanese Securities and Exchange Law. Daiwa House Industry Co., Ltd. (the "Company") and its domestic subsidiaries maintain their accounts and records in accordance with the provisions set forth in the Japanese Commercial Code (the "Code") and in conformity with accounting principles and practices generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Accounting Standards, and its foreign subsidiaries in conformity with those of each country of their domicile. The consolidated statements of cash flows are not required as a part of the basic consolidated financial statements in Japan but are presented herein as additional information.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, the notes to the consolidated financial statements include information which is not required under accounting principles generally accepted in Japan but is presented herein as additional information.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which the Company is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥132 to $1, the approximate rate of exchange at March 31, 1998. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

2. Summary of Significant Accounting Policies

a. Consolidation

The consolidated financial statements include the accounts of the Company and all subsidiaries (together the "Companies"). All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Companies is eliminated.

Investments in significant associated companies (20% - 50% ownership) are accounted for by the equity method.

The differences between the cost and underlying net equity of investments in subsidiaries and associated companies at acquisition are amortized over five years.

b. Cash and cash equivalents

For purposes of the statements of cash flows, the Companies consider all time deposits to be cash equivalents. Time deposits have original maturities of one year or less and are withdrawable on demand with no diminution of principal.

Time deposits pledged as collateral as substitutes of deposits for certain construction contracts were ¥20 million ($152 thousand) at both March 31, 1998 and 1997.

c. Marketable and investment securities

Marketable and investment securities are stated at cost determined by the average method. However, appropriate write-downs are recorded for securities with values considered to have been permanently or substantially impaired.

d. Inventories

Inventories are stated at cost. Inventories of land, residential homes and condominiums, and construction projects in progress include all costs of land, land development and construction. The cost of construction materials and supplies is determined by the average method.

e. Property, plant and equipment

Property, plant and equipment are stated at cost. Depreciation is computed by the declining-balance method at rates based on the estimated useful lives of the assets. The range of useful lives is principally from 15 to 47 years for buildings and structures, from 10 to 13 years for machinery and equipment and from 5 to 15 years for furniture and fixtures.

f. Leases

All leases are accounted for as operating leases. Under Japanese accounting standards for leases, finance leases that are deemed to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain “as if capitalized” information is disclosed in the notes to the lessee’s financial statements. The disclosure requirements of these standards are being applied on a step-by-step basis beginning with fiscal years starting on or after April 1, 1996, with full implementation required for fiscal years starting on or after April 1, 1998.

g. Retirement and pension plans

The Company and its domestic subsidiaries provide for employees’ retirement benefits based on Japanese tax regulations. The liability balances represented 40% of the amounts which would have been required if all employees voluntarily terminated at each balance sheet date. Retirement benefits to directors and corporate auditors are subject to the approval of the shareholders and are charged to expense when paid.

In addition, the Company and certain subsidiaries have a trusteed pension plan for which the policy is to fund and charge to expense, normal costs as accrued on the basis of an accepted actuarial method.

h. Revenue and profit recognition

Sales and related profits are generally recorded when sales contracts are closed and customers have satisfied the down payment and other requirements stipulated by the contracts. Land and land development costs are allocated to units sold based upon relative area. Payments received from customers prior to the recording of a sale are accounted for as current deposits received (see Note 6).

i. Income taxes

Income taxes are provided for amounts currently payable for each year. The tax effect of temporary differences between tax and financial reporting purposes is not recorded.

j. Appropriations of retained earnings

Appropriations of retained earnings at each year end are reflected in the financial statements of the following year after shareholders’ approval has been obtained.

k. Foreign currency transactions

Short-term receivables and payables denominated in foreign currencies are translated into Japanese yen at the current exchange rates at each balance sheet date. Long-term receivables and payables denominated in foreign currencies are translated into Japanese yen at historical exchange rates except for short- and long-term receivables and payables which are translated using the exchange rates set forth in the applicable forward exchange contracts.

In the case where there is significant fluctuation of currencies with possible exchange losses, long-term receivables or payables denominated in foreign currencies are translated at the current exchange rates in effect at the balance sheet date.

The exchange gains arising from forward exchange contracts are deferred and recognized as income ratably over the term of the contract period. Other exchange gains and losses are recognized in the fiscal periods in which they occur.

l. Foreign currency financial statements

Effective for the year ended March 31, 1997, the balance sheet accounts of the overseas subsidiaries and associated companies are translated into Japanese yen at current exchange rates as of the balance sheet date except for shareholders’ equity, which is translated at historical exchange rates. Differences arising from such translation are shown as “Translation adjustments” in the accompanying consolidated balance sheets. Revenue and expense accounts of the overseas subsidiaries and associated companies are translated into Japanese yen at the current exchange rates.

In 1996, financial statements of overseas subsidiaries and associated companies were translated into Japanese yen at year-end-rates for monetary current assets and liabilities and retained earnings, and at historical rates for other balance sheet accounts. The average rate for each year was used for translation of income and expenses, except that certain costs and expenses relating mainly to inventories and depreciable assets were translated at historical rates, and net income or loss was translated at year-end rates. Adjustments due to the translation were included in the respective financial statements.

m. Reclassifications

Certain reclassifications have been made to the 1997 and 1996 financial statements to conform to the classifications used in 1998.

n. Per share information

The computation of net income per share is based on the weighted average number of shares of common stock outstanding during each year. The average number of common shares used in the computation was 523,891 thousand shares for 1998, 512,975 thousand shares for 1997 and 481,926 thousand shares for 1996.

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

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years including dividends to be paid after the end of the year.

3. Marketable and Investment Securities

Carrying amounts and aggregate market values of current and non-current marketable securities at March 31, 1998 and 1997 were as follows:

	Millions of yen				Thousands of U.S. dollars	
	1998		1997		**1998**	
	Carrying amount	Aggregate market value	Carrying amount	Aggregate market value	Carrying amount	Aggregate market value
Current:						
Marketable securities	**¥ 5,464**	**¥ 4,997**	¥ 8,755	¥ 10,214	**$ 41,394**	**$ 37,856**
Treasury stock	**2**	**2**	1	1	**15**	**15**
Non-current:						
Investment securities	**61,264**	**53,058**	63,050	68,852	**464,121**	**401,955**
Investments in associated companies	**41,861**	**34,711**	42,077	58,787	**317,129**	**262,962**
Total	**¥108,591**	**¥92,768**	¥113,883	¥137,854	**$822,659**	**$702,788**

The difference between the above carrying amounts and the amounts shown in the balance sheets with respect to marketable securities, investment securities and investments in associated companies consisted of unlisted securities, for which market value amounts are not available.

4. Inventories

Inventories at March 31, 1998 and 1997 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	1998	1997	**1998**
Finished residential homes and condominiums	**¥ 30,560**	¥ 22,454	**$ 231,515**
Construction projects in progress	**29,176**	58,171	**221,031**
Residential homes and condominiums in process	**9,228**	24,118	**69,909**
Land held:			
For resale	**154,057**	163,346	**1,167,099**
Under development	**20,445**	15,777	**154,886**
Undeveloped	**20,742**	26,350	**157,136**
Construction materials and supplies	**8,896**	10,320	**67,394**
Total	**¥273,104**	¥320,536	**$2,068,970**

The Companies engage in two principal business activities. They manufacture and construct prefabricated houses and structures and also engage in various contracted construction projects, primarily for the construction of large-scale commercial and residential buildings. To further such business, the Companies purchase land for development and resale.

5. Short-term Bank Loans, Commercial Paper and Long-term Debt

Short-term bank loans at March 31, 1998 and 1997 consisted principally of bank overdrafts. The annual interest rates for the short-term bank loans ranged from 0.9% to 1.6% at March 31, 1998 and 1997, respectively. The annual interest rates for commercial paper ranged from 0.8% to 0.9% at March 31, 1998.

Long-term debt at March 31, 1998 and 1997 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	1998	1997	**1998**
Bonds with detachable stock purchase warrants —			
1.0% U.S. dollar bonds due 1998		¥ 79,571	
Convertible bonds:			
0.8% convertible bonds due 1998		30,000	
2.0% convertible bonds due 1999	**¥ 448**	448	**$ 3,394**
2.0% convertible bonds due 2002	**2,450**	2,453	**18,561**
Unsecured loans from banks	**393**	335	**2,977**
Total	**3,291**	112,807	**24,932**
Less current portion	**448**	109,571	**3,394**
Long-term debt, net of current portion	**¥2,843**	¥ 3,236	**$21,538**

Annual maturities of long-term debt at March 31, 1998 were as follows:

Year ending March 31:	Millions of yen	Thousands of U.S. dollars
1999	¥ 448	$ 3,394
2000	393	2,977
2002	2,450	18,561
Total	¥3,291	$24,932

As is customary in Japan, the Companies maintain deposit balances with banks with which they have borrowings. Such deposit balances are not legally or contractually restricted as to withdrawal.

General agreements with the respective banks provide, as is customary in Japan, that collateral must be provided under certain circumstances if requested by such banks and that certain banks have the right to offset cash deposited with them against any short-term or long-term debt or obligation that becomes due and, in case of default and certain other specified events, against all other debt payable to the banks. The Companies have never been requested to provide any additional collateral.

All outstanding 1.0% U.S. dollar bonds with warrants due in 1998 were redeemed during the fiscal year ended March 31, 1998. As the Company had purchased forward exchange contracts for these bonds with warrants at the time of issuance, the remaining unamortized portions of the related exchange gains which were recorded as “Accrued expenses and other current liabilities” have been fully recognized in the consolidated statement of income for the year ended March 31, 1998. The amortization of deferred exchange gains was credited to interest expense related to these bonds and remaining portions were recorded as exchange gains or offset with exchange losses in “Other income (expenses): Other — net” in the consolidated statements of income (see Note 10).

All outstanding convertible bonds of the Company at March 31, 1998 were convertible into 1,785 thousand shares of the Company’s common stock. The convertible bonds may be redeemed prior to maturity in whole or in part at prices ranging from 104% to 100% of the principal amounts. The conversion prices of the convertible bonds at March 31, 1998 were as follows, subject to anti-dilutive provisions:

	Conversion price
2.0% convertible bonds due 1999	¥1,623.4
2.0% convertible bonds due 2002	1,623.4

The agreements for certain convertible bonds contain restrictions with respect to the payment of cash dividends and other matters. The amount of retained earnings free from such restrictions was ¥325,390 million ($2,465,076 thousand) at March 31, 1998 (see Note 8).

6. Current and Long-term Deposits Received

Current deposits received at March 31, 1998 and 1997 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	1998	1997	**1998**
Advances from customers on signed or future sales contracts	**¥37,522**	¥56,392	**$284,258**
Deposits from customers, primarily for incidental costs such as registration fees, etc.	**12,015**	17,049	**91,023**
Other	**1,412**	1,750	**10,697**
Total	**¥50,949**	¥75,191	**$385,978**

Long-term deposits received at March 31, 1998 and 1997 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	1998	1997	**1998**
Deposits from the Company's club members	**¥ 80,158**	¥ 71,279	**$607,258**
Deposits from members of golf courses	**8,810**	9,482	**66,742**
Deposits from sales agents and subcontractors	**8,626**	8,435	**65,349**
Deposits from lessee	**20,360**	16,067	**154,242**
Other	**62**	63	**470**
Total	**¥118,016**	¥105,326	**$894,061**

The Companies operate resort complexes that include hotels with adjacent golf courses, vacation homes and other resort facilities. Members of the "Daiwa Royal Members Club" pay non-interest bearing refundable deposits to the Company and in return have certain rights in relation to the use of all the Company's resort hotels.

7. Retirement and Pension Plans

Under the unfunded retirement benefit plan, employees terminating their employment are entitled, in most circumstances, to lump-sum severance payments determined by reference to wage rates at the time of termination, years of service and certain other factors. In addition, the Company, Daiwa Housing Co., Ltd., Daiwa Resort Co., Ltd., Royal Home Center Co., Ltd. and Daiwa Living Co., Ltd. have adopted a trusteed pension plan covering most employees of the Company and the aforementioned subsidiaries. At March 31, 1997 and 1996 (the most recent available valuation dates), the assets of the plan amounted to ¥87,936 million ($666,182 thousand) and ¥79,208 million, respectively. Prior service cost is being amortized over 20 years.

Total charges to expense for the retirement and pension plans were ¥5,487 million ($41,568 thousand), ¥5,843 million and ¥4,767 million for the years ended March 31, 1998, 1997 and 1996, respectively.

8. Shareholders' Equity

The Code requires at least 50% of the issue price of new shares, with a minimum of the par value thereof, to be designated as stated capital as determined by resolution of the Board of Directors. Proceeds in excess of amounts designated as stated capital are credited to additional paid-in capital.

The Code also requires companies to appropriate from retained earnings to a legal reserve an amount at least equal to 10% of all cash payments which are made as an appropriation of retained earnings until such reserve equals 25% of the stated capital. This reserve is not available for dividends but may be used to reduce a deficit by resolution of the shareholders.

The Company may transfer portions of additional paid-in capital and legal reserve to stated capital by resolution of the Board of Directors. The Company may also transfer portions of unappropriated retained earnings, available for dividends, to stated capital by resolution of the shareholders.

Under the Code, the Company may issue new common shares to existing shareholders without consideration as a stock split pursuant to resolution of the Board of Directors. The Company may make such a stock split to the extent the aggregate par value of the shares outstanding after the stock split does not exceed the stated capital. However, the amount calculated by dividing the total amount of shareholders' equity by the number of outstanding shares after the stock split shall not be less than ¥50.

At March 31, 1998, retained earnings recorded on the books included ¥323,413 million ($2,450,098 thousand) designated as general reserves but available for future dividends and bonuses to directors and corporate auditors subject to approval by the shareholders and legal reserve requirements (see Note 5 with respect to restrictions under convertible debt agreements).

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

9. Segment Information

Information about operations in different industry segments of the Companies for the years ended March 31, 1998, 1997 and 1996 is as follows:

Sales and operating income

	Millions of yen					
	1998					
	Residential	Commercial	Resort	Other	Eliminations	Consolidated
Sales to customers	**¥729,305**	**¥259,161**	**¥41,593**	**¥39,730**		**¥1,069,789**
Intersegment sales		**1,361**	**705**	**768**	**¥ (2,834)**	
Total sales	**729,305**	**260,522**	**42,298**	**40,498**	**(2,834)**	**1,069,789**
Operating expenses	**684,906**	**242,875**	**48,191**	**42,097**	**9,414**	**1,027,483**
Operating income (loss) before adjustment of enterprise tax	**¥ 44,399**	**¥ 17,647**	**¥(5,893)**	**¥(1,599)**	**¥(12,248)**	**42,306**
Enterprise tax (income tax) included in operating expenses						**(6,144)**
Operating income						**¥ 48,450**

	Thousands of U.S. dollars					
	1998					
	Residential	Commercial	Resort	Other	Eliminations	Consolidated
Sales to customers	**$5,525,038**	**$1,963,341**	**$315,098**	**$300,985**		**$8,104,462**
Intersegment sales		**10,311**	**5,341**	**5,818**	**$(21,470)**	
Total sales	**5,525,038**	**1,973,652**	**320,439**	**306,803**	**(21,470)**	**8,104,462**
Operating expenses	**5,188,682**	**1,839,962**	**365,083**	**318,917**	**71,318**	**7,783,962**
Operating income (loss) before adjustment of enterprise tax	**$ 336,356**	**$ 133,690**	**$(44,644)**	**$(12,114)**	**$(92,788)**	**320,500**
Enterprise tax (income tax) included in operating expenses						**(46,545)**
Operating income						**$ 367,045**

	Millions of yen					
	1997					
	Residential	Commercial	Resort	Other	Eliminations	Consolidated
Sales to customers	¥835,112	¥276,990	¥42,072	¥34,121		¥1,188,295
Intersegment sales		864	563	681	¥ (2,108)	
Total sales	835,112	277,854	42,635	34,802	(2,108)	1,188,295
Operating expenses	754,939	261,278	49,146	37,016	11,012	1,113,391
Operating income (loss) before adjustment of enterprise tax	¥ 80,173	¥ 16,576	¥(6,511)	¥(2,214)	¥(13,120)	74,904
Enterprise tax (income tax) included in operating expenses						(8,985)
Operating income						¥ 83,889

	Millions of yen					
	1996					
	Residential	Commercial	Resort	Other	Eliminations	Consolidated
Sales to customers	¥739,563	¥260,167	¥40,591	¥25,897		¥ 1,066,218
Intersegment sales		851	513	626	¥ (1,990)	
Total sales	739,563	261,018	41,104	26,523	(1,990)	1,066,218
Operating expenses	667,756	243,272	48,874	28,022	10,166	998,090
Operating income (loss) before adjustment of enterprise tax	¥ 71,807	¥ 17,746	¥(7,770)	¥(1,499)	¥(12,156)	68,128
Enterprise tax (income tax) included in operating expenses						(7,939)
Operating income						¥ 76,067

Assets, depreciation and capital investments

	Millions of yen					
	1998					
	Residential	Commercial	Resort	Other	Corporate	Consolidated
Assets	**¥363,580**	**¥105,191**	**¥186,569**	**¥70,088**	**¥287,644**	**¥1,013,072**
Depreciation	**5,628**	**1,907**	**9,029**	**1,191**	**101**	**17,856**
Capital investments	**6,746**	**6,761**	**12,226**	**958**	**7,371**	**34,062**

	Thousands of U.S. dollars					
	1998					
	Residential	Commercial	Resort	Other	Corporate	Consolidated
Assets	**$2,754,394**	**$ 796,901**	**$1,413,402**	**$530,970**	**$2,179,121**	**$7,674,788**
Depreciation	**42,636**	**14,447**	**68,402**	**9,023**	**765**	**135,273**
Capital investments	**51,106**	**51,220**	**92,621**	**7,257**	**55,841**	**258,045**

	Millions of yen					
	1997					
	Residential	Commercial	Resort	Other	Corporate	Consolidated
Assets	¥422,653	¥129,466	¥182,646	¥69,918	¥341,262	¥1,145,945
Depreciation	6,278	2,125	9,587	806	120	18,916
Capital investments	9,366	10,455	10,085	2,633	8,497	41,036

	Millions of yen					
	1996					
	Residential	Commercial	Resort	Other	Corporate	Consolidated
Assets	¥441,559	¥142,725	¥181,400	¥67,936	¥407,597	¥1,241,217
Depreciation	6,940	2,200	10,031	560	240	19,971
Capital investments	13,471	3,880	7,628	1,683	8,110	34,772

The industry segments consisted of the following:

Components of net sales in the consolidated statements of income	Industry Segment			
	Residential	Commercial	Resort	Other
Construction	Construction of single/multi-family homes and condominiums	Construction of commercial buildings		Construction of resort villas
Real estate	Sales of real estate for residential use	Sales and rental of real estate for commercial use		Sales of land lots for resort villas
	Real estate commissions			
	Rental of residential complexes			
Other			Operations of hotels and golf courses	Operations of "do-it-yourself" hardware centers

Eliminations include unallocated operating expenses, principally consisting of general corporate expenses incurred by the administration headquarters of the Company.

Corporate assets are principally cash and cash equivalents, marketable securities and investment securities.

10. Other Income (Expenses): Other — Net

"Other income (expenses): Other — net" for the years ended March 31, 1998, 1997 and 1996 consisted of the following:

	Millions of yen			Thousands of U.S. dollars
	1998	1997	1996	**1998**
Equity in earnings of associated companies	**¥ 449**	¥1,516	¥2,627	**$ 3,401**
Exchange gains (see Note 5)	**1,047**	466	826	**7,932**
Gain resulting from associated company's public offering of stock			615	
Loss on sales and disposal of property, plant and equipment	**(2,055)**	(1,664)	(3,651)	**(15,568)**
Gain (loss) on sales of marketable and investment securities	**114**	(431)	(651)	**864**
Real estate acquisition tax and other taxes	**(414)**	(718)	(513)	**(3,136)**
Write-down of marketable and investment securities	**(555)**	(268)		**(4,205)**
Other — net	**254**	879	1,449	**1,924**
Total	**¥(1,160)**	¥ (220)	¥ 702	**$ (8,788)**

Daiwa Logistics Co., Ltd. ("DLC"), an associated company, made a public offering of 1 million shares in September 1995. The Company did not subscribe to any shares and as a result of the offering the Companies' ownership in DLC decreased from 47.2% to 40.4%. However, the Companies' interest in DLC's net assets increased because of the proceeds from shares issued to the public. The gain from the increase in the Companies' investment in DLC is presented as "Gain resulting from associated company's public offering of stock" separate from "Equity in earnings of associated companies" as shown above.

11. Income Taxes

The Companies are subject to a number of taxes based on income. The effective income tax rates of the Companies for the years ended March 31, 1998, 1997 and 1996 differ from the normal statutory rates for the following reasons:

	1998	1997	1996
Normal statutory income tax rates	**51.2%**	51.2%	51.2%
Increase (decrease) in tax rates due to:			
Permanently non-deductible expenses	**2.4**	1.4	1.5
Temporary differences	**1.8**	(0.3)	(1.9)
Equity in earnings of associated companies, less dividends	**0.3**	(0.5)	(1.3)
Gain resulting from associated company's public offering of stock			(0.4)
Other — net	**2.4**	(2.0)	0.2
Effective income tax rates	**58.1%**	49.8%	49.3%

12. Leases

Total lease payments under finance leases that are not deemed to transfer ownership of the leased property to the lessee were ¥5,713 million ($43,280 thousand) and ¥3,937 million for the years ended March 31, 1998 and 1997, respectively.

Obligations under such finance leases as of March 31, 1998 are as follows:

	Millions of yen	Thousands of U.S. dollars
Due within one year	¥ 5,854	$ 44,349
Due after one year	9,666	73,227
Total	¥15,520	$117,576

The amount of obligations under finance leases includes the imputed interest expense portion.

Obligations and future rental income under non-cancellable operating leases as of March 31, 1998 are as follows:

Lessee	Millions of yen	Thousands of U.S. dollars
Due within one year	¥ 11,980	$ 90,757
Due after one year	130,558	989,076
Total	¥142,538	$1,079,833

Lessor	Millions of yen	Thousands of U.S. dollars
Due within one year	¥ 5,436	$ 41,182
Due after one year	69,562	526,985
Total	¥74,998	$568,167

13. Derivatives

The Company has entered into foreign exchange forward contracts to hedge market risk from the changes in foreign exchange rates associated with liabilities denominated in foreign currencies.

It is the Company's policy to use derivatives only for the purpose of reducing market risks associated with liabilities.

The execution and control of derivatives are controlled by the Finance Department. Each derivative transaction is reported to management and the Accounting Department monthly.

As of March 31, 1998, the Company did not have any forward exchange contracts. As of March 31, 1997, the total forward exchange contracted amount which was not reflected on the balance sheet was as follows:

1997	Contract amount (in thousands)	Millions of yen: Amount in equivalent of yen valued at forward exchange rate	Millions of yen: Amount in equivalent of yen valued at spot rate as of March 31, 1997
Buying U.S. dollars forward	US$7,909	¥853	¥982

	Thousands of U.S. dollars: Amount in equivalent of yen valued at forward exchange rate	Thousands of U.S. dollars: Amount in equivalent of yen valued at spot rate as of March 31, 1997
Buying U.S. dollars forward	$6,879	$7,909

14. Commitments and Contingencies

Capital expenditure commitments — Commitments for capital expenditures outstanding at March 31, 1998 aggregated approximately ¥9,577 million ($72,553 thousand).

Contingencies — At March 31, 1998, contingent liabilities for notes endorsed with recourse and loans guaranteed in the ordinary course of business amounted to ¥4,374 million ($33,136 thousand) and ¥113,258 million ($858,015 thousand), respectively. Included in loans guaranteed were customers' housing loans from banks in the amount of ¥108,714 million ($823,591 thousand).

15. Subsequent Event

(1) The following appropriations of retained earnings at March 31, 1998 were approved at the Company's shareholders' meeting held on June 26, 1998:

	Millions of yen	Thousands of U.S. dollars
Year-end cash dividends, ¥17.0 ($0.13) per share	¥8,906	$67,469
Bonuses to directors and corporate auditors	150	1,136
Transfer to legal reserve	910	6,894

(2) At the general shareholders' meeting held on June 26, 1998, the Company's shareholders approved the purchase of treasury stock for retirement and related reduction of retained earnings. The Company is authorized to repurchase, at management's discretion, up to 50 million shares of the Company's stock for the purpose of canceling the shares by charging costs of repurchase to retained earnings. Any such amounts charged to retained earnings would not be available for future distribution to shareholders.

Independent Auditors' Report

Deloitte Touche Tohmatsu

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To the Board of Directors and Shareholders of
Daiwa House Industry Co., Ltd.:

We have examined the consolidated balance sheets of Daiwa House Industry Co., Ltd. and subsidiaries as of March 31, 1998 and 1997, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended March 31, 1998, all expressed in Japanese yen. Our examinations were made in accordance with auditing standards generally accepted in Japan and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Daiwa House Industry Co., Ltd. and subsidiaries as of March 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 1998 in conformity with accounting principles generally accepted in Japan applied on a consistent basis.

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

Deloitte Touche Tohmatsu

June 26, 1998

Deloitte Touche
Tohmatsu
International