

2003 Financial information

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Note: In the financial statements, the names given to our business segments are abbreviated as follows:

Housing: Residential Commercial construction: Commercial Resort hotels: Resort Home center business: Home Center Other businesses: Other

Consolidated seven-year summary

Daiwa House Industry Co., Ltd. and Subsidiaries
Years ended March 31, 1997 to 2003

	Millions of yen						
	2003	2002	2001	2000	1999	1998	1997
Net sales	¥1,184,544	¥1,197,925	¥1,016,237	¥ 951,073	¥ 896,006	¥1,069,789	¥1,188,295
Cost of sales	936,861	945,474	794,170	736,310	691,318	834,407	922,387
Selling, general and administrative expenses	202,411	206,420	177,777	167,266	164,473	186,932	182,019
Operating income	45,272	46,031	44,290	47,497	40,215	48,450	83,889
Income (loss) before income taxes and minority interests	(155,157)	9,538	12,796	32,123	21,414	48,685	75,601
Net income (loss)	(91,388)	5,217	6,256	17,450	16,699	20,373	42,452
Per share of common stock (in yen):							
Basic net income (loss)	(167.06)	9.55	12.05	33.52	31.88	38.89	82.76
Diluted net income				33.50		37.91	79.89
Shareholders' equity	884.55	1,066.63	1,182.01	1,188.63	1,151.12	1,136.55	1,115.04
Property, plant and equipment, less accumulated depreciation	349,646	426,630	383,853	376,489	365,502	346,543	338,166
Total assets	1,094,441	1,187,127	1,066,457	981,893	950,701	1,013,072	1,145,944
Shareholders' equity	483,684	582,438	613,867	617,421	603,060	595,429	584,157
Return on equity (%)	(18.89)	0.85	1.02	2.86	2.79	3.42	7.27

Management's discussion and analysis (on a consolidated basis)

Operating environment and financial strategy

The business environment remained difficult in Japan in the term under review. The economy became increasingly in the grip of deflation, with no sign of any improvement in the employment situation and both consumer spending and corporate capital investment remaining sluggish.

In the housing industry, the number of new construction starts remained below the 1.2 million level for the second straight year, and, more crucially, hit a 19-year low. In addition, owner-occupied housing starts fell particularly steeply, by 3.1% year-on-year to below the 370,000 mark. General construction, too, was generally weak against the backdrop of stagnant private-sector capital investment and continued curtailment of public works spending.

In the face of this business environment, the Daiwa House group has put priority on further strengthening its financial position. Particular emphasis was put on ensuring a return to financial health in the term under review, to which end we implemented an extraordinary depreciation of tangible assets as well as the lump-sum amortization of the transitional obligations and actuarial losses on retirement benefits. A major reduction was also effected in the interest-bearing liability burden, with Daiwa House Industry paying off all interest-bearing debt on a non-consolidated basis.

Results of operations

Net sales

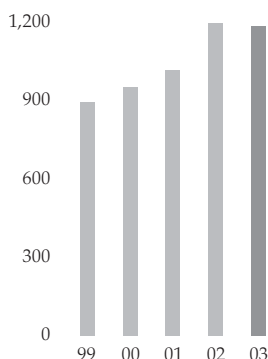
Net sales for the term ended March 31, 2003 decreased 1.1% from the previous term to ¥1,184.5 billion (US\$9,871.2 million); this was mainly attributable to a decline in new housing starts of 1,146 thousand, the lowest for 19 years, against the backdrop of prolonged stagnation in Japan. By segment, Housing operations (including inter-segment transactions), declined 1.7% to ¥791.9 billion (US\$6,599.8 million), and Commercial construction operations declined 4.9% to ¥248.0 billion (US\$2,066.7 million). While Resort hotels operations rose 7.0% to ¥51.9 billion (US\$432.5 million), Home center operations rose 14.7% to ¥52.1 billion (US\$434.6 million), and Other businesses rose 8.8% to ¥97.1 billion (US\$809.3 million). Declines in our mainstay businesses, Housing and Commercial construction operations, had a significant effect on the total sales.

Cost of sales, and selling, general and administrative expenses

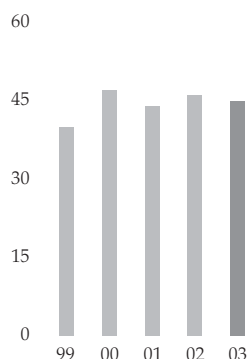
Cost of sales decreased ¥8.6 billion (US\$71.7 million) from the previous term to ¥936.8 billion (US\$7,807.1 million), while its ratio to sales rose 0.2 percentage points to 79.1% due to an increase in direct expenses.

Selling, general and administrative expenses decreased ¥4.0 billion from the previous term to ¥202.4 billion (US\$1,686.7 million), and their ratio to sales fell 0.2 percentage points to 17.1%, thanks to a reduction in expenses for advertising and sales commissions, despite a slight increase in personnel expenses.

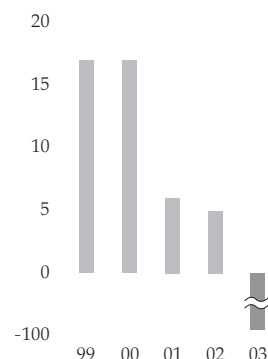
Net sales
(Billions of yen)



Operating income
(Billions of yen)



Net income (loss)
(Billions of yen)



Operating income

Although operating income declined 1.7% from the previous term to ¥45.2 billion (US\$377.2 million) in line with a decline in sales, its ratio to sales came to 3.8%, virtually the same as the previous term.

Analysis of operations by segment is as follows.

(Segment sales amounts prior to elimination of inter-segment transactions were used in the following analysis.)

Sales of Housing operations fell ¥14.0 billion, or 1.7%, from the previous term. However, we were rather satisfied with the results, taking into account the decline in new housing starts nationwide by 2.3% from 1,173 thousand for the previous term to 1,146 thousand. We attributed this relatively favorable result to organizational reform including an expansion in the number of sales offices and of the marketing system to meet local needs more precisely, as well as a change in product strategy to more accurately meet customer needs. Under this, for example, we offered solar power systems and high-insulation houses for residents in districts with particularly cold winters. Regarding condominiums, we focused on small condominiums in urban districts to take advantage of the trend in which the central areas of the nation's metropolises are once again becoming popular places to live.

The number of rental apartment units sold by us increased 8.8% on a non-consolidated basis over the previous term, against the backdrop of a rising need by landowners to more effectively use their landholdings. This trend results from the lack of favorable investment targets for financial assets due to the continued low level of interest rates and the termination of unlimited government guarantees on time deposits.

As a result, sales of Housing operations amounted to ¥791.9 billion. Operating income decreased ¥3.7 billion to ¥39.1 billion, and its ratio to sales fell 0.4 percentage points to 4.9%.

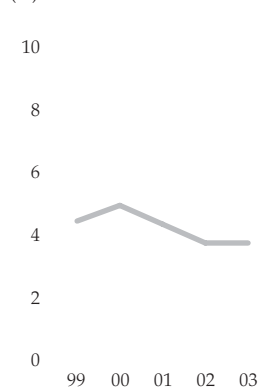
Sales of Commercial construction operations fell ¥12.7 billion, or 4.9%, from the previous term. During the term, we focused on communal dwellings for senior citizens incorporating our extensive know-how in medical and care facilities, as well as large-scale logistics facilities and shopping malls utilizing a nation-wide network of landowners and tenants. Floor space for rental use and the number of tenants were beginning to decline amidst weak consumer spending and sluggish capital investment. As a result, sales of Commercial construction operations came to ¥248.0 billion and operating income declined ¥0.7 billion to ¥17.6 billion. The ratio of operating income to sales, however, improved 0.1 percentage points over the previous term to 7.1%, the highest figure among the segments.

Resort hotels operations sales rose ¥3.4 billion, or 7.0%, over the previous term. The increase was mainly attributable to rises both in the number of guests and in room occupancy rates thanks to an improvement in Internet reservation systems for resort hotels and enhancement of marketing channels, which resulted in a rise in the number of foreign guests. We attracted more customers for our wedding facilities compared with the previous term thanks to an increase in the number of chapels within the resort hotels.

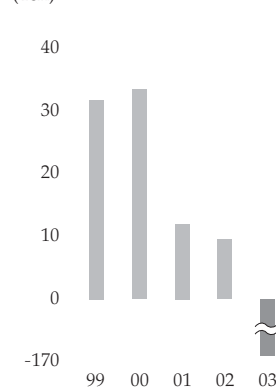
Revenues from golf club operations fell from the previous term, due to a decline in revenue per customer reflecting a general price decline.

As a result, Resort hotels operations sales came to ¥51.9 billion. We posted an operating loss of ¥3.9 billion, lower than the previous term.

Operating profit margin (%)



Basic net income (loss) per share (Yen)



Home center operations sales far exceeded the previous term's result by ¥6.6 billion, up 14.7%, thanks mainly to an increase in the number of outlets by two. It is undeniable that an increase in revenue for this business segment depends largely on the opening of new outlets. However, we expect to differentiate ourselves from our competitors by taking advantage of our expertise in housing construction. The Home center operations, therefore, is useful for achieving synergy with the Housing operations. As a result, the Home center operations sales amounted to ¥52.1 billion and operating income to ¥0.3 billion, almost same as the previous term. Its ratio to sales fell 0.1 percentage points to 0.6%.

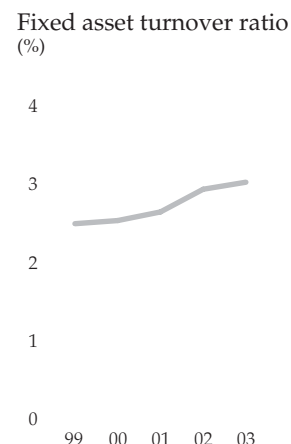
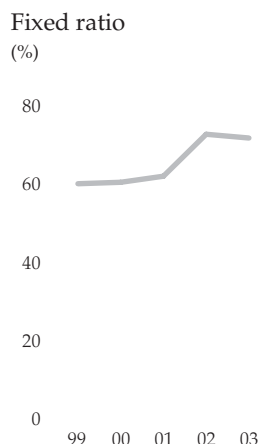
The Other businesses segment consists of a wide variety of businesses including construction materials manufacturing, logistics, hotel operations in urban areas. Sales for the segment rose ¥7.8 billion, or 8.8%, over the previous term. We are making efforts to improve the management efficiency of our logistics operations through transfer, merger and consolidation of branches. The number of urban-type hotels came to eight as of the term end, and is expected to increase still further. We are focusing on the development of price-competitive, value-added construction material products. As a result of the above, sales of the segment came to ¥97.1 billion and its ratio of operating income to sales fell 0.2 percentage points to 2.6%.

Other income and expenses

Due to our bold management decisions to implement a large-scale lump-sum amortization of liabilities on retirement benefits and total elimination of unrealized losses on land and securities holdings, we posted net other expenses of ¥200.4 billion. Other income came to ¥21.2 billion, up ¥12.5 billion, and

other expenses to ¥221.6 billion, up ¥176.4 billion. The increase in other income was mainly attributable to gains on amortization of prior service obligations resulting from revisions on regulations for retirement benefits, and the termination of agency service for the state-run employee pension fund. These measures were taken in line with fundamental reform of our retirement benefit system, and were necessary for improving our financial position regarding pensions.

On the other hand, the increase in other expenses was attributable to lump-sum amortization of retirement benefit obligations and total elimination of unrealized loss on land for resale and other property, and securities. We chose lump-sum amortization and total elimination as we judged that they were crucial for rebuilding a sound financial position preparatory to future expansion. Alongside pension obligations, unrealized losses were recognized on 1) real estate for operations and real estate for sale, and 2) securities and investments in affiliated companies. Regarding retirement benefits, we amortized in lump-sum ¥90.3 billion, consisting of unrecognized actuarial loss of ¥49.8 billion, actuarial loss resulting from changes in discount rates used for calculation of present value of pension assets of ¥31.7 billion and transitional obligations of ¥8.7 billion. For real estate for operations and real estate for sale, we carried out extraordinary depreciation of ¥75.1 billion on real estate for hotel, golf-club and rental use with large reduction in asset value, and posted valuation losses of ¥22.9 billion on land and buildings. We also posted losses of ¥9.8 billion on sale and valuation on securities and of ¥2.9 billion on liquidation of subsidiaries and affiliates.



Net income

As mentioned previous sections, we posted ¥200.4 billion under net other expenses for the term. As a result, we registered a loss before income taxes of ¥155.1 billion and net loss of ¥91.3 billion under tax effect accounting.

Liquidity and Capital Resources

Financial position

Total assets decreased ¥92.6 billion, or 7.8%, during the term to stand at ¥1,094.4 billion (US\$9,120.3 million) at the term end. Current assets and property, plant and equipment decreased ¥74.5 billion and ¥76.9 billion from the previous term end, respectively. Among current assets, a significant decline was seen in cash and cash equivalents, and in land held for resale under inventories. Reduced amounts in cash and cash equivalents were used for repayment interest-bearing liabilities to secure a sound financial position. The decline in land held for resale was largely attributable to the posting of valuation losses. Inventories, which consisted of construction projects in progress, land and buildings held for resale, and other inventories, declined ¥31.2 billion to ¥267.1 billion.

Among property, plant and equipment, the decline in buildings and structures was notable, due to extraordinary depreciation on properties with significant decline in asset values belonging to hotels and golf clubs, and other properties. As a result, buildings and structures declined ¥76.5 billion to ¥121.6 billion. Regarding land for business use, we carried out a one-time revaluation of own-use land in accordance with the revisions to the "Law on Land Revaluation," in the previous term. While investment securities declined due to the posting of valuation losses, investments and other securities as a whole increased, mainly due to an increase in deferred tax assets.

With regard to liabilities and shareholders' equity, current assets decreased ¥75.9 billion as a result of the repayment of short-term bank loans to secure a sound financial position. Interest-bearing liabilities (including bonds and long-term loans posted under long-term liabilities) stood at only ¥6.0 billion at the term end, which was equivalent to 0.6% of total assets. On a non-consolidated basis, the Company held no interest-bearing liabilities. Trade notes and accounts payable increased due to the balance sheet date falling on a bank holiday. The current ratio rose to 174.2% from 157.5% at the previous term end, which, in our opinion, represented a sufficient level of liquidity.

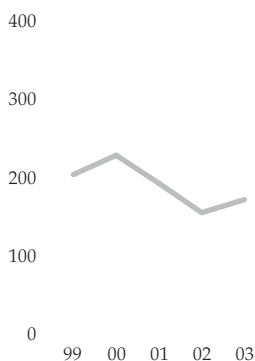
Long-term liabilities increased ¥83.1 billion, which was attributable to provisions for employees' retirement benefits in line with a thorough reform of the retirement benefits system at the parent company in accordance with introduction of a new pension accounting system.

Shareholders' equity decreased ¥98.7 billion to ¥483.6 billion (US\$4,030.7 million) due to a deduction in retained earnings resulting from the posting of a huge net loss. The equity ratio, however, declined 4.9 percentage points to 44.2%, which, in our opinion, was sufficient for a sound financial position.

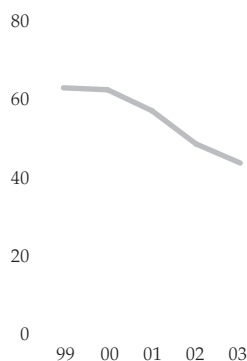
Cash flows

Cash and cash equivalents decreased ¥44.5 billion, or 30.0%, during the term, and stood at ¥103.9 billion (US\$866.2 million) at the term end. Net cash provided by operating activities amounted to ¥40.4 billion (US\$337.1 million, down ¥46.5 billion, or 53.5%, from the previous term. Net cash used in investing activities came to ¥27.3 billion (US\$227.6 million), down ¥8.9 billion, or 24.6%. Net cash used in financing activities amounted to ¥57.7 billion (US\$480.9 million), a decrease of ¥31.8 billion, or 35.5%, from the previous term.

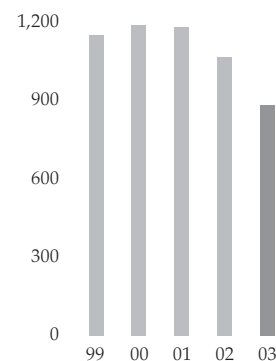
Current ratio (%)



Shareholders' equity / total assets (%)



Shareholders' equity per share (Yen)



The decline in net cash inflows from operating activities was mainly attributable to the posting of a large loss before income taxes. Losses on retirement benefits and extraordinary amortization expenses, however, did not contribute to the decline, as these items had no effect on cash flows. Another contributing factor in the decrease in the cash inflow was the large decline in trade notes and accounts payable. This, however, was attributable to the balance sheet date falling on a bank holiday. The de facto decline, therefore, was much smaller. The decline in cash outflows from investing activities was attributable to a decline in the acquisition of property and equipment for new facilities. The net cash outflow from financing activities declined despite a reduction in interest-bearing liabilities as part of an ongoing program to improve the Group's financial soundness (the parent company itself has already achieved zero interest-bearing liabilities).

As a result, free cash flow (combined cash flows of operating and investing activities) amounted to ¥13.1 billion, down ¥37.6 billion from the previous term.

Outlook

For the current business term, the fiscal year ending March 31, 2004, although some bright economic indicators have been seen, unemployment is expected to remain high and pay levels are likely to weaken. The overall outlook for the Japanese economy is thus projected to remain gloomy, taking into account the various unstable factors in the world economy.

For the current term, the construction industry will enjoy the plus factor of an expansion in the framework for application of tax-exempt status for donations of property. However, taking into account the disposable income situation, which reflects the lack of any improvement in employment conditions, housing

investment is likely to remain weak, leading to even fiercer competition among construction companies.

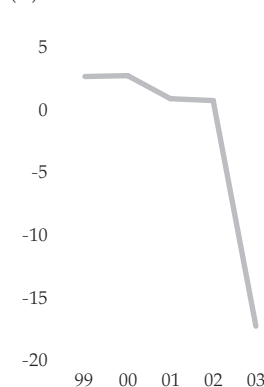
To cope with this difficult business environment, the management of Daiwa House will continue to pursue the Company's basic "customer first" policy by working to produce a stronger, leaner company through steps to cut expenses while improving our marketing, service provision and product development capabilities-centered on a branch-based marketing system tailored to the requirements of each individual region.

In our Housing operations, we plan to launch new single-family house models on the market offering stronger anti-burglary features. We will also step up our activities in the home renovation market. In Commercial construction operations, we will focus on medical and nursing care facilities to meet the needs of the aging population. In our Resort hotels operations, we will put even further efforts into providing unique services that take full advantage of the particular features of each locality. Finally, in our Home center operations, we plan to continue opening new stores while expanding our lineup of product and services in line with our aim of becoming a comprehensive lifestyle enterprise.

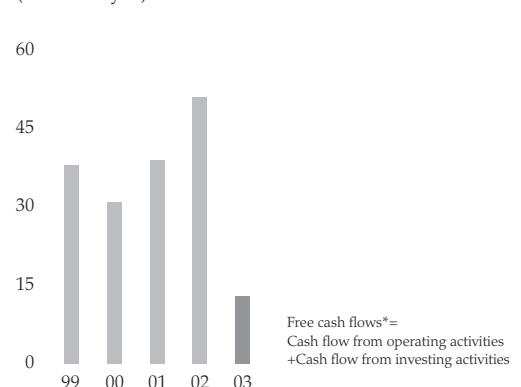
As a result of the steps toward a return to financial health taken in the reporting period, including an extraordinary depreciation of tangible assets as well as the lump-sum amortization of the transitional obligations and actuarial loss on retirement benefits, we expect to see a decline in depreciation expenses and in costs related to retirement benefits in the current term, putting us well on the way to realizing our goal of a tough and resilient financial position.

As a result of the foregoing, we anticipate net sales on a consolidated basis for fiscal 2003 of ¥1,220.0 billion, operating income of ¥56.0 billion, and net income of ¥30.0 billion.

Return on equity (%)



Free cash flows* (Billions of yen)



Consolidated balance sheets

Daiwa House Industry Co., Ltd. and Subsidiaries
March 31, 2003 and 2002

Assets

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Current assets:			
Cash and cash equivalents	¥ 103,950	¥ 148,520	\$ 866,250
Marketable securities (Note 4)	202	180	1,683
Short-term investments (Note 2-d)	133	1,599	1,108
Receivables:			
Trade notes	7,238	9,071	60,317
Trade accounts	55,685	56,804	464,042
Allowance for doubtful receivables	(1,972)	(1,766)	(16,433)
Inventories (Note 5)	267,199	298,424	2,226,658
Deferred tax assets (Note 12)	22,106	10,884	184,217
Prepaid expenses and other current assets	13,755	19,099	114,625
Total current assets	<u>468,296</u>	<u>542,815</u>	<u>3,902,467</u>
Property, plant and equipment:			
Land (Notes 6 and 7)	212,312	208,811	1,769,267
Buildings and structures (Note 7)	380,978	371,018	3,174,817
Accumulated depreciation	(259,286)	(172,816)	(2,160,717)
Machinery and equipment	51,264	52,531	427,200
Accumulated depreciation	(42,205)	(41,363)	(351,708)
Furniture and fixtures	36,695	37,041	305,792
Accumulated depreciation	(31,116)	(29,875)	(259,300)
Construction in progress	1,004	1,283	8,366
Net property, plant and equipment	<u>349,646</u>	<u>426,630</u>	<u>2,913,717</u>
Investments and other assets:			
Investment securities (Note 4)	25,988	35,402	216,567
Investments in and advances to associated companies	25,900	28,817	215,833
Long-term loans	5,024	9,445	41,867
Deferred tax assets (Note 12)	100,123	28,444	834,358
Deferred tax assets on land revaluation (Note 6)	41,211	43,135	343,425
Lease deposits and other assets	87,589	77,422	729,908
Allowance for doubtful accounts	(9,336)	(4,983)	(77,800)
Total investments and other assets	<u>276,499</u>	<u>217,682</u>	<u>2,304,158</u>
Total	<u>¥1,094,441</u>	<u>¥1,187,127</u>	<u>\$9,120,342</u>

See notes to consolidated financial statements.

Liabilities and shareholders' equity

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Current liabilities:			
Short-term bank loans (Note 7)	¥ 2,800	¥ 54,000	\$ 23,333
Current portion of long-term debt (Note 7)		1,000	
Payables:			
Trade notes	26,012	27,927	216,767
Trade accounts	90,890	146,846	757,417
Other accounts	58,639	35,482	488,658
Deposits received from customers	38,444	33,906	320,367
Income taxes payable	8,419	2,379	70,158
Accrued bonuses	9,769	10,099	81,408
Provision for product warranties	4,181	3,465	34,842
Accrued expenses and other current liabilities	29,657	29,622	247,142
Total current liabilities	<u>268,811</u>	<u>344,726</u>	<u>2,240,092</u>
Long-term liabilities:			
Long-term debt (Note 7)	3,237	2,000	26,975
Liability for employees' retirement benefits (Note 3 and 8)	136,480	51,224	1,137,333
Long-term deposits received from the Company's club members	64,243	67,721	535,358
Lease deposits and other long-term liabilities	115,229	115,103	960,242
Total long-term liabilities	<u>319,189</u>	<u>236,048</u>	<u>2,659,908</u>
Minority interests	<u>22,757</u>	<u>23,915</u>	<u>189,642</u>
Commitments and contingent liabilities (Notes 14, 15 and 16)			
Shareholders' equity (Notes 2-c, 2-m, 2-p, 6, 9 and 18):			
Common stock, authorized, 1,900,000,000 shares; issued, 550,664,416 shares in both 2003 and 2002	110,120	110,120	917,667
Capital surplus	147,755	147,755	1,231,292
Retained earnings	289,840	387,591	2,415,333
Land revaluation difference	(60,409)	(59,910)	(503,408)
Net unrealized gain on available-for-sale securities	777	1,358	6,475
Foreign currency translation adjustments	(881)	(809)	(7,342)
Treasury stock — at cost, 3,848,065 shares in 2003 and 4,610,098 shares in 2002	(3,518)	(3,667)	(29,317)
Total shareholders' equity	<u>483,684</u>	<u>582,438</u>	<u>4,030,700</u>
Total	<u>¥1,094,441</u>	<u>¥1,187,127</u>	<u>\$9,120,342</u>

Consolidated statements of operations

Daiwa House Industry Co., Ltd. and Subsidiaries
Years ended March 31, 2003, 2002 and 2001

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2003	2002	2001	2003
Net sales	¥1,184,544	¥1,197,925	¥1,016,237	\$9,871,200
Cost of sales	936,861	945,474	794,170	7,807,175
Gross profit	247,683	252,451	222,067	2,064,025
Selling, general and administrative expenses (Note 13)	202,411	206,420	177,777	1,686,758
Operating income	45,272	46,031	44,290	377,267
Other income (expenses):				
Interest income and dividends	546	569	796	4,550
Interest expense	(723)	(1,348)	(299)	(6,025)
Write-down of marketable and investment securities	(9,773)	(16,956)	(1,385)	(81,442)
Write-down of inventories	(22,900)	(5,994)	(5,291)	(190,833)
Loss on sales and disposal of property, plant and equipment	(3,488)	(1,594)	(543)	(29,067)
Prior service benefit from changes to employees' retirement benefit plan (Note 8)	6,736	1,583		56,133
Amortization of transitional obligation for employees' retirement benefits (Notes 2-h and 8)	(8,780)	(9,473)	(9,198)	(73,167)
Contribution to employees' retirement benefit trust (Notes 2-h and 8)			(14,732)	
Amortization of actuarial loss for employees' retirement benefits (Note 8)	(4,925)	(3,361)		(41,042)
Actuarial loss on retirement benefits (Notes 3 and 8)	(49,888)			(415,733)
Actuarial loss due to a change of discount rate (Notes 3 and 8)	(31,733)			(264,441)
Extraordinary depreciation for property, plant and equipment (Note 2-f)	(75,183)			(626,525)
Other — net (Note 11)	(318)	81	(842)	(2,650)
Other income (expenses) — net	(200,429)	(36,493)	(31,494)	(1,670,242)
Income (loss) before income taxes and minority interests	(155,157)	9,538	12,796	(1,292,975)
Income taxes (Note 12):				
Current	17,792	8,633	22,268	148,267
Deferred	(81,370)	(4,913)	(16,537)	(678,083)
Total	(63,578)	3,720	5,731	(529,816)
Minority interests in net (income) loss of subsidiaries	191	(601)	(809)	1,592
Net income (loss)	¥ (91,388)	¥ 5,217	¥ 6,256	\$ (761,567)
		Yen		U.S. dollars
Per share of common stock (Note 2-o):				
Basic net income (loss)	¥ (167.06)	¥ 9.55	¥ 12.05	\$(1.39)
Cash dividends applicable to the year	10.00	10.00	17.00	0.08

See notes to consolidated financial statements.

Consolidated statements of shareholders' equity

Daiwa House Industry Co., Ltd. and Subsidiaries
Years ended March 31, 2003, 2002 and 2001

	Thousands		Millions of yen					
	Issued number of shares of common stock	Common stock	Capital surplus	Retained earnings	Land revaluation difference	Net unrealized gain on available-for-sale securities	Foreign currency translation adjustments	Treasury stock
Balance, April 1, 2000	523,893	¥108,781	¥122,041	¥390,206				¥(3,607)
Net income				6,256				
Cash dividends, ¥17.0 per share				(8,831)				
Bonuses to directors and corporate auditors				(37)				
Foreign currency translation adjustments (Note 2-m)							¥(927)	
Net increase in treasury stock								(15)
Balance, March 31, 2001	523,893	108,781	122,041	387,594			(927)	(3,622)
Issuance for merger with Daiwa Danchi Co., Ltd. (Note 17)	26,771	1,339	25,714					
Retained earnings of Daiwa Danchi Co., Ltd. at April 1, 2001				3,663				
Net income				5,217				
Cash dividends, ¥17.0 per share				(8,829)				
Bonuses to directors and corporate auditors				(54)				
Land revaluation difference					¥(59,910)			
Net increase in unrealized gain on available-for-sale securities (Note 2-c)						¥1,358		
Foreign currency translation adjustments (Note 2-m)							118	
Net increase in treasury stock								(45)
Balance, March 31, 2002	550,664	110,120	147,755	387,591	(59,910)	1,358	(809)	(3,667)
Net loss				(91,388)				
Cash dividends, ¥10.0 per share				(5,461)				
Bonuses to directors and corporate auditors				(19)				
Effect of change in statutory tax rate and other					(1,382)			
Transfer due to sales of land				(883)	883			
Net decrease in unrealized gain on available-for-sale securities (Note 2-c)						(581)		
Foreign currency translation adjustments (Note 2-m)							(72)	
Net decrease in treasury stock								149
Balance, March 31, 2003	550,664	¥110,120	¥147,755	¥289,840	¥(60,409)	¥ 777	¥(881)	¥(3,518)

Thousands of U.S. dollars (Note 1)

	Common stock		Capital surplus	Retained earnings	Land revaluation difference	Net unrealized gain on available-for-sale securities	Foreign currency translation adjustments	Treasury stock
	Balance, March 31, 2002	\$917,667	\$1,231,292	\$3,229,925	\$(499,250)	\$11,317	\$(6,742)	\$(30,558)
Net loss			(761,567)					
Cash dividends, \$0.08 per share			(45,508)					
Bonuses to directors and corporate auditors			(159)					
Effect of change in statutory tax rate and other				(11,516)				
Transfer due to sales of land				(7,358)	7,358			
Net decrease in unrealized gain on available-for-sale securities (Note 2-c)						(4,842)		
Foreign currency translation adjustments (Note 2-m)							(600)	
Net decrease in treasury stock								1,241
Balance, March 31, 2003	\$917,667	\$1,231,292	\$2,415,333	\$(503,408)	\$ 6,475	\$(7,342)	\$(29,317)	

See notes to consolidated financial statements.

Consolidated statements of cash flows

Daiwa House Industry Co., Ltd. and Subsidiaries
Years ended March 31, 2003, 2002 and 2001

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2003	2002	2001	2003
Operating activities:				
Income (loss) before income taxes and minority interests	¥(155,157)	¥ 9,538	¥ 12,796	\$(1,292,975)
Adjustments to reconcile income (loss) before income taxes and minority interests to net cash provided by operating activities:				
Income taxes — paid	(6,230)	(24,236)	(22,418)	(51,917)
Depreciation	21,386	20,883	19,731	178,217
Write-down of golf club membership	147	411	820	1,225
Write-down of marketable and investment securities	9,773	16,956	1,385	81,442
Loss on sales and disposal of property, plant and equipment	3,488	1,594	543	29,067
Extraordinary depreciation for property, plant and equipment	75,183			626,525
Equity in earnings of associated companies	(278)	(1,052)	(933)	(2,317)
Contribution to employees' retirement benefit trust			14,732	
Provision for employees' retirement benefits, net of payments	85,002	17,053	14,319	708,350
Changes in certain assets and liabilities, net of consolidation:				
Decrease (increase) in receivables	3,571	3,942	(6,626)	29,758
Decrease (increase) in inventories	32,872	48,909	(39,652)	273,933
Increase (decrease) in payables — trade	(31,453)	(3,797)	63,256	(262,108)
Increase (decrease) in deposits received from customers	4,260	(508)	3,630	35,500
Other — net	(2,105)	(2,672)	2,491	(17,542)
Total adjustments	195,616	77,483	51,278	1,630,133
Net cash provided by operating activities	40,459	87,021	64,074	337,158
Investing activities:				
Purchases of property, plant and equipment	(26,464)	(30,405)	(19,235)	(220,533)
Purchases of marketable and investment securities	(4,269)	(3,873)	(502)	(35,575)
Increase in investments in and advances to associated companies	(1,275)	(1,881)	(1,247)	(10,625)
Proceeds from sales of marketable and investment securities	2,814	422	110	23,450
Proceeds from sales of property, plant and equipment	1,244	379	138	10,367
Net proceeds from purchases of shares of the newly consolidated subsidiary	1,489			12,408
Increase in lease deposits	(5,415)	(2,768)	(3,342)	(45,125)
Net decrease (increase) in other assets	4,560	1,897	(1,195)	38,000
Net cash used in investing activities	(27,316)	(36,229)	(25,273)	(227,633)
Financing activities:				
Net increase (decrease) in short-term bank loans	(52,005)	(80,060)	2,000	(433,375)
Proceeds from long-term debt	1,237		1,000	10,308
Repayments of long-term debt	(1,000)	(58)	(85)	(8,333)
Proceeds from issuance of bonds		2,000		
Repayments of convertible bonds		(2,005)		
Net of purchases and proceeds from sales of treasury stock	(200)	(43)	(15)	(1,667)
Dividends paid	(5,745)	(9,101)	(9,117)	(47,875)
Cash paid related to merger with Daiwa Danchi Co., Ltd.		(268)		
Net cash used in financing activities	(57,713)	(89,535)	(6,217)	(480,942)
Cash and cash equivalents increased by merger		14,062		
Net increase (decrease) in cash and cash equivalents	(44,570)	(24,681)	32,584	(371,417)
Cash and cash equivalents, beginning of year	148,520	173,201	140,617	1,237,667
Cash and cash equivalents, end of year	¥ 103,950	¥ 148,520	¥ 173,201	\$ 866,250

See notes to consolidated financial statements.

Nihon Jyutaku Ryutu Co., Ltd., formerly an associated company, has been included in consolidation in the fiscal year of 2003 as a result of the additional acquisition of its shares.

The assets and liabilities upon acquisition and the net proceeds from purchases of shares consisted of the following:

	Millions of yen	Thousands of U.S. dollars
Current assets	¥3,621	\$30,175
Long-term assets	5,642	47,017
Consolidation difference	98	817
Current liabilities	(2,418)	(20,150)
Long-term liabilities	(4,844)	(40,367)
Minority interests	(973)	(8,108)
Company's interest prior to acquisition	(1,094)	(9,117)
Acquisition cost	32	267
Cash and cash equivalents of the consolidated subsidiary	(1,521)	(12,675)
Net proceeds from purchases of shares	¥1,489	\$12,408
	Millions of Yen	
	2002	2001
Non-cash investing and financing activities:		
Fair value of securities contributed to employees' retirement benefit trust (Note 2-h)		¥14,732
Assets acquired and liabilities assumed in merger (Note 18):		
Current assets	¥143,756	
Long-term assets	132,201	
Total	<u>¥275,957</u>	
Current liabilities	¥176,694	
Long-term liabilities	54,595	
Total	<u>¥231,289</u>	

See notes to consolidated financial statements.

Notes to consolidated financial statements

Daiwa House Industry Co., Ltd. and Subsidiaries

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 Financial Reporting Standards, and its foreign subsidiary in conformity with those of its country of domicile. The consolidated financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

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.

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 ¥120 to \$1, the approximate rate of exchange at March 31, 2003. 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 "Group") based on the control or influence concept. Under the control or influence concept, those companies over whose operations the Parent, directly or indirectly, is able to exercise control are fully consolidated, and those companies over which the Group has the ability to exercise significant influence 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.

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.

b. Cash and cash equivalents

Cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value. Cash equivalents include time deposits and certificate of deposits, all of which mature or become due within three months of the date of acquisition.

c. Marketable and investment securities

Marketable and investment securities are classified and accounted for, depending on management's intent, as follows: i) held-to-maturity debt securities, which are expected to be held to maturity with the positive intent and ability to hold to maturity are reported at amortized cost and ii) available-for-sale securities, which are not classified as held-to-maturity. In accordance with the new accounting standard for financial instruments, available-for-sale securities were reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of shareholders' equity, effective April 1, 2001, and were reported at cost, prior to April 1, 2001.

Non-marketable available-for-sale securities are stated at cost, determined by the moving-average method. For other than temporary declines in fair value, investment securities are reduced to net realizable value by a charge to income.

d. Short-term investments

Short-term investments are time deposits and certificates of deposit, all of which mature or become due later than three months after the date of acquisition. Time deposits pledged as collateral as substitutes of deposits for certain construction and advertisement contracts were ¥29 million (\$242 thousand) and ¥677 million as of March 31, 2003 and 2002.

e. 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. However, appropriate write-downs are recorded for inventories with values considered to have been permanently or substantially impaired.

f. Property, plant and equipment

Property, plant and equipment are stated at cost. Depreciation is computed substantially by the declining-balance method while the straight-line method is applied to buildings acquired after April 1, 1998. The range of useful lives is principally from 15 to 39 years for buildings and structures, from 10 to 13 years for machinery and equipment and from 5 to 15 years for furniture and fixtures.

Extraordinary depreciation for property, plant and equipment is charged to income for the year ended March 31, 2003, for depreciable assets in which utilization declined significantly, these assets consist of resort hotels, club-houses on golf courses and commercial buildings for rent. The extraordinary depreciation recorded was ¥73,369 million (\$611,409 thousand), ¥856 million (\$7,133 thousand), and ¥958 million (\$7,983 thousand), for buildings and structures, machinery and equipment, and furniture and fixtures, respectively.

g. 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.

h. Retirement and pension plans

The Company and its domestic subsidiaries have unfunded retirement benefit plans and a contributory funded pension plan. The Company and its domestic consolidated subsidiaries account for the liability for employees' retirement benefits based on the projected benefit obligations and plan assets at the balance sheet date.

In August 2000, the Company contributed certain available-for-sale securities with a fair value of ¥14,732 million to the employees' retirement benefit trust for the parent company's non-contributory pension plans, and recognized a non-cash loss of ¥266 million.

The transitional obligation of ¥43,221 million, determined as of April 1, 2000, was reduced by an immediate charge to income in the amount of the fair value of the above contribution. The remaining transitional obligation of ¥28,489 million (including ¥896 million assumed in a merger with Daiwa Danchi Co., Ltd.) is principally being amortized over three years.

i. Revenue and profit recognition

Sales and related profits are generally recorded when sales contracts are completed 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.

j. Income taxes

The provision for income taxes is computed based on the pretax income included in the consolidated statements of operations. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

k. 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.

l. Foreign currency transactions

All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the current exchange rates at the balance sheet date. The foreign exchange gains and losses from translation are recognized in the statements of operations.

m. Foreign currency financial statements

The balance sheet accounts of the consolidated foreign subsidiary and associated companies are translated into Japanese yen at the current exchange rate as of the balance sheet date except for shareholders' equity, which is translated at historical exchange rates. Revenue and expense accounts of the consolidated foreign subsidiary and associated companies are translated into yen at the current exchange rate.

Differences arising from such translation are shown as "Foreign currency translation adjustments" in a separate component of shareholders' equity.

n. Reclassifications

Certain reclassifications and rearrangements have been made in the 2002 and 2001 financial statements to conform to the classifications used in 2003.

o. Per share information

Basic net income per share is computed by dividing net income available to common shareholders, by the weighted-average number of common shares outstanding for the year.

The weighted-average number of common shares outstanding for the years ended March 31, 2003, 2002 and 2001 were 547,045 thousand, 546,079 thousand and 519,391 thousand, respectively.

Diluted net income per share of common stock for the years ended March 31, 2002 and 2001 are not disclosed because it is anti-dilutive. Diluted net income per share of common stock for the year ended March 31, 2003 is not disclosed because the Company incurred a net loss.

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

p. Treasury stock

Effective April 1, 2002, the Company adopted a new accounting standard for treasury stock issued by the Accounting Standards Board of Japan. Under the new standard, the stock of the Company, which is held by its subsidiaries and associated companies, is stated as treasury stock according to the percentage of ownership.

3. Accounting change

Due to the deterioration of the stock market and the revision of the discount rate from 3.5% to 2.5%, the amount of unrecognized actuarial losses accumulated to 40% of the projected benefit obligation during 2003. With the government's approval of the Group's application for the exemption from future obligations related to the substitutional portion of the pension program (Note 8), the revision of the retirement benefit plan, and the reexamination of investment policy, the actuarial loss, which would be amortized evenly over principally 10 years under the Group's previous method, was changed to be recognized when incurred in order to disclose information about retirement and pension plans more timely. As a result, the loss before income taxes and minority interests increased by ¥81,621 million (\$680,175 thousand), compared with what would have been recorded under the previously method.

4. Marketable and investment securities

Marketable and investment securities as of March 31, 2003 and 2002 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Current:			
Government and corporate bonds	¥ 202	¥ 180	\$ 1,683
Non-current:			
Marketable equity securities	25,926	35,318	216,050
Government and corporate bonds	62	84	517
Total	<u>¥25,988</u>	<u>¥35,402</u>	<u>\$216,567</u>

The carrying amounts and aggregate fair values of marketable and investment securities at March 31, 2003 and 2002 were as follows:

	Millions of yen			
	2003			
	Cost	Unrealized gains	Unrealized losses	Fair value
Securities classified as:				
Available-for-sale:				
Equity securities	¥18,096	¥2,895	¥1,119	¥19,872
Held-to-maturity	264	1		265

	Millions of yen			
	2002			
	Cost	Unrealized gains	Unrealized losses	Fair value
Securities classified as:				
Available-for-sale:				
Equity securities	¥26,268	¥5,250	¥2,656	¥28,862
Held-to-maturity	264	1		265

	Thousands of U.S. dollars			
	2003			
	Cost	Unrealized gains	Unrealized losses	Fair value
Securities classified as:				
Available-for-sale:				
Equity securities	\$150,800	\$24,125	\$9,325	\$165,600
Held-to-maturity	2,200	8		2,208

Available-for-sale securities whose fair value is not readily determinable as of March 31, 2003 and 2002 were as follows:

	Carrying amount		
	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Available-for-sale:			
Equity securities	¥5,854	¥4,456	\$48,783
Debt securities	200	2,000	1,667
Total	<u>¥6,054</u>	<u>¥6,456</u>	<u>\$50,450</u>

The carrying values of debt securities by contractual maturities for securities classified as available-for-sale and held-to-maturity at March 31, 2003 are as follows:

	Millions of yen		Thousands of U.S. dollars	
	Available for sale	Held to maturity	Available for sale	Held to maturity
Due in one year or less		¥202		\$1,683
Due after one year through five years		62		517
Due after five years through ten years	¥200		\$1,667	
Total	<u>¥200</u>	<u>¥264</u>	<u>\$1,667</u>	<u>\$2,200</u>

5. Inventories

Inventories at March 31, 2003 and 2002 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Finished residential homes and condominiums	¥ 27,771	¥ 34,176	\$ 231,425
Construction projects in progress	28,745	21,428	239,542
Residential homes and condominiums in process	20,383	18,159	169,858
Land held:			
For resale	134,130	163,573	1,117,750
Under development	33,110	36,921	275,917
Undeveloped	11,687	12,561	97,391
Construction materials and supplies	11,373	11,606	94,775
Total	<u>¥267,199</u>	<u>¥298,424</u>	<u>\$2,226,658</u>

The Group engages 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 Group purchases land for development and resale.

6. Land revaluation

Under the "Law of Land Revaluation," the Company and certain subsidiaries elected a one-time revaluation of their own-use land to a value based on real estate appraisal information as of March 31, 2002.

The resulting land revaluation difference represents unrealized depreciation of land and is stated, net of income taxes, as a component of shareholders' equity. There was no effect on the statement of income. Continuous readjustment is not permitted unless the land value subsequently declines significantly such that the amount of the decline in value should be removed from the land revaluation difference account and related deferred tax liabilities. The details of the one-time revaluation as of March 31, 2002 were as follows:

	Millions of yen
Land before revaluation	¥311,703
Land after revaluation	<u>208,811</u>
Land revaluation difference	102,892
Deferred tax assets on land revaluation	43,135
Minority interests, net	<u>(153)</u>
Net land revaluation difference	<u>¥ 59,910</u>

7. Short-term bank loans and long-term debt

Short-term bank loans at March 31, 2003 and 2002 consisted of bank loans. The annual interest rates for the short-term bank loans ranged from 0.6% to 1.4% and from 0.5% to 1.4% at March 31, 2003 and 2002, respectively.

Long-term debt at March 31, 2003 and 2002 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Unsecured bank loans, 1.18%, due serially to 2002 September		¥1,000	
Unsecured bank loans, 1.50%, due serially to 2005 July	¥ 237		\$ 1,975
Unsecured 0.5% bonds due 2004 December	2,000	2,000	16,667
Loans from bank, 1.26%, due serially to 2007 March; Collateralized	1,000		8,333
Total	3,237	3,000	26,975
Less current portion		1,000	
Long-term debt, net of current portion	¥3,237	¥2,000	\$26,975

Annual maturities of long-term debt at March 31, 2003, were as follows:

Year ending March 31:	Millions of yen	Thousands of U.S. dollars
2005	¥2,047	\$17,058
2006	321	2,675
2007	869	7,242
Total	¥3,237	\$26,975

At March 31, 2003, assets pledged as collateral for secured long-term debt of ¥1,000 million (\$8,333 thousand) were as follows:

	Millions of yen	Thousands of U.S. dollars
Land	¥ 502	\$ 4,183
Buildings and structures	1,470	12,250
Total	¥1,972	\$16,433

As is customary in Japan, the Company maintains deposit balances with banks with which it has bank loans. Such deposit balances are not legally or contractually restricted as to withdrawal. In addition, collateral must be provided if requested by the lending banks and certain banks have the right to offset cash deposited with them against any bank loan or obligation that becomes due and, in case of default and certain other specified events, against all other debt payable to the bank concerned. The Company has never received any such request.

8. Retirement and pension plans

Under the unfunded employees' retirement benefit plan, employees of the Company and certain subsidiaries terminating their employment are entitled, in most circumstances, to lump-sum severance payments determined by reference to wage rates at the time of termination and years of service. In addition, the Company, together with certain subsidiaries and associated companies, has adopted a contributory funded defined benefit pension plan covering most of their employees.

The liability for employees' retirement benefits at March 31, 2003 and 2002 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Projected benefit obligation	¥199,597	¥228,306	\$1,663,308
Fair value of plan assets	(63,185)	(115,811)	(526,542)
Unrecognized actuarial loss		(51,864)	
Unrecognized transitional obligation		(9,474)	
Net liability	136,412	51,157	1,136,766
Prepaid benefit costs	68	67	567
Liability for employees' retirement benefits	¥136,480	¥ 51,224	\$1,137,333

The components of net periodic benefit costs are as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Service cost	¥ 10,845	¥11,967	\$ 90,375
Interest cost	7,182	7,535	59,850
Expected return on plan assets	(3,181)	(4,219)	(26,508)
Prior service benefit	(6,736)	(1,583)	(56,133)
Recognized actuarial loss	86,546	3,361	721,216
Amortization of transitional obligation	8,780	9,473	73,167
Net periodic benefit costs	¥103,436	¥26,534	\$861,967

Prior service benefit for the year ended March 31, 2002 represents the net effect of (1) a decrease in the benefit obligation of ¥5,964 million from raising the eligibility age for payments regarding the basic part of the welfare pension plan for employees of the Company and certain subsidiaries, which is similar to the national pension plan, in accordance with a revision in the Welfare Pension Insurance Law in March, 2000 and (2) an increase in the benefit obligation of ¥4,381 million from changing the Daiwa Danchi pension plan from a qualified pension plan to a welfare pension plan and unfunded retirement benefit plan. These changes were effective March 2002 and November 2001, respectively, and the full effect on the benefit obligation as of those dates was charged to income in the year ended March 31, 2002.

Prior service benefit for the year ended March 31, 2003 represents the effect of a decrease in the benefit obligation from the adoption of the revised retirement benefit plan concerning the lump-sum severance payments.

Assumptions used for the years ended March 31, 2003 and 2002 are set forth as follows:

	2003	2002
Discount rate	2.5%	3.5%
Expected rate of return on plan assets	3.5%	3.5%
Recognition period of actuarial gain (loss)	1 year	Principally 10 years
Amortization period of transitional obligation	Principally 3 years (completed)	Principally 3 years

The contributory funded defined benefit pension plan, which is established under the Japanese Welfare Pension Insurance Law, covers a substitutional portion of the governmental pension program managed by the Company on behalf of the government and a corporate portion established at the discretion of the company. According to the enactment of the Defined Benefit Pension Plan Law in April 2002, the Company applied for an exemption from obligation to pay benefits for future employee services related to the substitutional portion which would result in the transfer of the pension obligations and related assets to the government by another subsequent application. The Company obtained an approval of exemption from future obligation by the Ministry of Health, Labor and Welfare on October 28, 2002. As a result of this exemption, the Company and certain subsidiaries recognized a gain on exemption from future pension obligation of the governmental program in the amount of ¥8,575 million (\$71,458 thousand) in accordance with a transitional measurement of the accounting standard for employees' retirement benefits for the year ended March 31, 2003. The substitutional portion of the plan assets which will be transferred to the government in the subsequent year is measured to be approximately ¥38,040 million (\$317,000 thousand) as of March 31, 2003.

9. Shareholders' equity

Japanese companies are subject to the Japanese Commercial Code (the "Code") to which certain amendments became effective from October 1, 2001.

The Code was revised whereby common stock par value was eliminated resulting in all shares being recorded with no par value and at least 50% of the issue price of new shares is required to be recorded as common stock and the remaining net proceeds as additional paid-in capital, which is included in capital surplus. The Code permits Japanese companies, upon approval of the Board of Directors, to issue shares to existing shareholders without consideration as a stock split. Such issuance of shares generally does not give rise to changes within the shareholders' accounts.

The revised Code also provides that an amount at least equal to 10% of the aggregate amount of cash dividends and certain other appropriations of retained earnings associated with cash outlays applicable to each period shall be appropriated as a legal reserve (a component of retained earnings) until such reserve and additional paid-in capital equals 25% of common stock. The amount of total additional paid-in capital and legal reserve that exceeds 25% of the common stock may be available for dividends by resolution of the shareholders. In addition, the Code permits the transfer of a portion of additional paid-in capital and legal reserve to the common stock by resolution of the Board of Directors.

The revised Code eliminated restrictions on the repurchase and use of treasury stock allowing Japanese companies to repurchase treasury stock by a resolution of the shareholders at the general shareholders meeting and dispose of such treasury stock by resolution of the Board of Directors beginning April 1, 2002. The repurchased amount of treasury stock cannot exceed the amount available for future dividend plus amount of common stock, additional paid-in capital or legal reserve to be reduced in the case where such reduction was resolved at the general shareholders meeting.

The amount of retained earnings available for dividends under the Code was ¥188,031 million (\$1,566,925 thousand) as of March 31, 2003, based on the amount recorded in the parent company's general books of account. In addition to the provision that requires an appropriation for a legal reserve in connection with the cash payment, the Code imposes certain limitations on the amount of retained earnings available for dividends.

Dividends are approved by the shareholders at a meeting held subsequent to the fiscal year in 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.

10. Segment information

Information about operations in different industry segments of the Group for the years ended March 31, 2003, 2002 and 2001 is as follows:

Sales and operating income (loss)

Millions of yen							
2003							
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Sales to customers	¥789,325	¥245,999	¥51,903	¥51,219	¥46,098		¥1,184,544
Intersegment sales	2,656	2,015		940	51,019	¥(56,630)	
Total sales	791,981	248,014	51,903	52,159	97,117	(56,630)	1,184,544
Operating expenses	752,846	230,383	55,872	51,854	94,544	(46,227)	1,139,272
Operating income (loss)	¥ 39,135	¥ 17,631	¥ (3,969)	¥ 305	¥ 2,573	¥(10,403)	¥ 45,272

Thousands of U.S. dollars							
2003							
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Sales to customers	\$6,577,708	\$2,049,992	\$432,525	\$426,825	\$384,150		\$9,871,200
Intersegment sales	22,134	16,791		7,833	425,158	\$(471,916)	
Total sales	6,599,842	2,066,783	432,525	434,658	809,308	(471,916)	9,871,200
Operating expenses	6,273,717	1,919,858	465,600	432,116	787,866	(385,224)	9,493,933
Operating income (loss)	\$ 326,125	\$ 146,925	\$ (33,075)	\$ 2,542	\$ 21,442	\$ (86,692)	\$ 377,267

Millions of yen							
2002							
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Sales to customers	¥805,022	¥257,733	¥48,499	¥44,349	¥42,322		¥1,197,925
Intersegment sales	981	3,052		1,114	46,906	¥(52,053)	
Total sales	806,003	260,785	48,499	45,463	89,228	(52,053)	1,197,925
Operating expenses	763,070	242,434	52,854	45,162	86,708	(38,334)	1,151,894
Operating income (loss)	¥ 42,933	¥ 18,351	¥ (4,355)	¥ 301	¥ 2,520	¥(13,719)	¥ 46,031

Millions of yen							
2001							
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Sales to customers	¥648,804	¥246,113	¥39,823	¥40,777	¥40,720		¥1,016,237
Intersegment sales	2,882	685		1,266	45,114	¥(49,947)	
Total sales	651,686	246,798	39,823	42,043	85,834	(49,947)	1,016,237
Operating expenses	604,660	230,655	45,772	43,703	83,367	(36,210)	971,947
Operating income (loss)	¥ 47,026	¥ 16,143	¥ (5,949)	¥ (1,660)	¥ 2,467	¥(13,737)	¥ 44,290

Total assets, depreciation and capital investments

	Millions of yen						
	2003						
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Total assets	¥394,119	¥211,168	¥98,803	¥35,196	¥78,976	¥276,179	¥1,094,441
Depreciation	5,288	2,604	6,334	592	4,774	1,794	21,386
Capital investments	6,984	8,114	2,164	2,317	3,778	1,354	24,711

	Thousands of U.S. dollars						
	2003						
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Total assets	\$3,284,325	\$1,759,733	\$823,358	\$293,300	\$658,133	\$2,301,493	\$9,120,342
Depreciation	44,067	21,700	52,783	4,933	39,783	14,951	178,217
Capital investments	58,200	67,617	18,033	19,308	31,483	11,284	205,925

	Millions of yen						
	2002						
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Total assets	¥436,521	¥192,101	¥152,280	¥30,728	¥85,251	¥290,246	¥1,187,127
Depreciation	5,378	2,122	6,610	538	4,444	1,791	20,883
Capital investments	20,753	11,935	2,514	1,841	3,996	23,393	64,432

	Millions of yen						
	2001						
	Residential	Commercial	Resort	Distribution "Home Center"	Other	Eliminations/ Corporate	Consolidated
Assets	¥357,052	¥156,911	¥123,792	¥32,167	¥92,258	¥304,277	¥1,066,457
Depreciation	4,527	2,124	6,128	568	4,740	1,644	19,731
Capital investments	16,706	3,315	2,215	1,495	5,131	1,697	30,559

The industry segments consisted of the following:

Components of net sales in the consolidated statements of operations	Industry segment				
	Residential	Commercial	Resort	Distribution "Home Center"	Other
Construction	Construction of single/ multi-family houses and condominiums	Construction of commercial buildings			
Real estate	Sales of real estate for residential use	Sales and rental of real estate for commercial use			
	Real estate commissions				
	Rental of residential complexes				
Other	Care of condominiums	Care of commercial buildings	Operation of resort type hotels and golf courses	Operation of "do-it-yourself" hardware centers	Manufacture and sales of building materials Physical distribution Operation of city type hotels

Eliminations/Corporate 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.

11. Other income (expenses): Other — net

“Other income (expenses): Other — net” for the years ended March 31, 2003, 2002 and 2001 consisted of the following:

	Millions of yen			Thousands of U.S. dollars
	2003	2002	2001	2003
Exchange gains (losses)	¥ (7)	¥ (2)	¥ 92	\$ (58)
Real estate acquisition tax and other taxes	(277)	(257)	(420)	(2,308)
Retirement benefits for directors	(120)	(643)	(566)	(1,000)
Expenses for large-scale repairs to property, plant and equipment			(1,062)	
Gain (loss) on sales of marketable and investment securities	123	(544)	(120)	1,025
Allowance for doubtful accounts	(4,157)	(873)	(342)	(34,642)
Gain on exemption from future pension obligation	8,575			71,458
Loss on securities contributed to employees' retirement benefit trust			(266)	
Equity in earnings of associated companies	278	1,052	933	2,317
Write-down of golf club membership	(147)	(411)	(820)	(1,225)
Loss on sales of membership	(79)	(170)		(658)
Loss on liquidation of associated company	(2,145)			(17,875)
Bad debt expenses for long-term loans	(4,082)			(34,017)
Other — net	1,720	1,929	1,729	14,333
Total	<u>¥ (318)</u>	<u>¥ 81</u>	<u>¥ (842)</u>	<u>\$ (2,650)</u>

12. Income taxes

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 42.0% for the years ended March 31, 2003, 2002 and 2001.

The tax effects of significant temporary differences and loss carryforwards which resulted in deferred tax assets and liabilities at March 31, 2003 and 2002 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Current:			
Deferred tax assets:			
Write-down of land held for resale	¥ 15,257	¥ 6,472	\$127,142
Accrued bonuses	3,404	2,642	28,367
Accrued enterprise tax	769	240	6,408
Other	2,676	1,530	22,300
Deferred tax assets	<u>¥ 22,106</u>	<u>¥10,884</u>	<u>\$184,217</u>
Non-current:			
Deferred tax assets:			
Employees' retirement benefits	¥ 55,498	¥20,878	\$462,483
Unrealized gains on sales of property, plant and equipment	7,503	7,225	62,525
Extraordinary depreciation for property, plant and equipment	30,299		252,492
Other	9,703	3,605	80,858
Deferred tax assets	<u>103,003</u>	<u>31,708</u>	<u>858,358</u>
Deferred tax liabilities:			
Retained earnings appropriated for tax allowable reserves	¥ (2,038)	¥ (2,059)	\$ (16,983)
Net unrealized gain on available-for-sale securities	(723)	(1,118)	(6,025)
Other	(119)	(87)	(992)
Deferred tax liabilities	<u>(2,880)</u>	<u>(3,264)</u>	<u>(24,000)</u>
Net deferred tax assets	<u>¥100,123</u>	<u>¥28,444</u>	<u>\$834,358</u>

A reconciliation between the normal effective statutory tax rates and the actual effective tax rates reflected in the accompanying consolidated statements of income for the years ended March 31, 2003, 2002 and 2001 is as follows:

	2003	2002	2001
Normal effective statutory tax rates	42.0%	42.0%	42.0%
Increase (decrease) in tax rates due to:			
Permanently non-deductible expenses	(0.6)	9.2	6.5
Non-taxable dividend income	0.0	(0.2)	(0.7)
Equity in earnings of associated companies	0.1	(4.6)	(3.0)
Write-down of investments in and advances to associated companies	0.4	(0.7)	(1.2)
Per capita levy	(0.3)	5.4	4.2
Decrease in valuation allowance for deferred tax assets	1.2	(11.8)	
Decrease in deferred tax assets by change of tax rate	(2.0)		
Other — net	0.2	(0.3)	(3.0)
Actual effective tax rates	<u>41.0%</u>	<u>39.0%</u>	<u>44.8%</u>

On March 31, 2003, Cabinet Order No. 9 entitled “Reform of a Portion of Local Tax Law” was issued and this reform will apply to fiscal years beginning after April 1, 2004. As a result of this reform, the statutory income tax rate to be used for the calculation of deferred income taxes concerning temporary differences which are expected to be realized or settled after April 1, 2004 will be changed from 42.0% to 40.6%.

The effect of this change was to decrease deferred tax assets and deferred tax assets on land revaluation by ¥3,145 million (\$26,208 thousand) and ¥1,417 million (\$11,808 thousand), respectively, and to increase income taxes-deferred, net unrealized gain on available-for-sale securities and land revaluation difference by ¥3,170 million (\$26,417 thousand), ¥18 million (\$150 thousand) and ¥1,417 million (\$11,808 thousand), respectively, for the year ended March 31, 2003.

13. Research and development costs

Research and development costs charged to income were ¥5,609 million (\$46,742 thousand), ¥5,474 million and ¥5,535 million for the years ended March 31, 2003, 2002 and 2001, respectively.

14. Leases

Total lease payments under finance leases that are not deemed to transfer ownership of the leased property to the lessee were ¥4,815 million (\$40,125 thousand), ¥4,510 million, and ¥3,949 million for the years ended March 31, 2003, 2002 and 2001, respectively.

Pro forma information of leased property under finance leases that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the years ended March 31, 2003 and 2002 were as follows:

(Lessee)

	Millions of yen			
	2003			
	Buildings and structures	Machinery and equipment	Furniture and fixtures	Total
Acquisition cost	¥10,006	¥1,307	¥9,311	¥20,624
Accumulated depreciation	<u>4,193</u>	<u>480</u>	<u>4,874</u>	<u>9,547</u>
Net leased property	<u>¥ 5,813</u>	<u>¥ 827</u>	<u>¥4,437</u>	<u>¥11,077</u>

	Millions of yen			
	2002			
	Buildings and structures	Machinery and equipment	Furniture and fixtures	Total
Acquisition cost	¥8,740	¥896	¥10,110	¥19,746
Accumulated depreciation	<u>2,395</u>	<u>445</u>	<u>5,639</u>	<u>8,479</u>
Net leased property	<u>¥6,345</u>	<u>¥451</u>	<u>¥ 4,471</u>	<u>¥11,267</u>

	Thousands of U.S. dollars			
	2003			
	Buildings and structures	Machinery and equipment	Furniture and fixtures	Total
Acquisition cost	\$83,383	\$10,892	\$77,592	\$171,867
Accumulated depreciation	<u>34,941</u>	<u>4,000</u>	<u>40,617</u>	<u>79,558</u>
Net leased property	<u>\$48,442</u>	<u>\$ 6,892</u>	<u>\$36,975</u>	<u>\$ 92,309</u>

Obligations under such finance leases as of March 31, 2003 and 2002 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Due within one year	¥ 4,561	¥ 4,255	\$38,009
Due after one year	6,516	7,012	54,300
Total	<u>¥11,077</u>	<u>¥11,267</u>	<u>\$92,309</u>

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

Depreciation expenses, which are not reflected in the accompanying statements of income, computed by the straight-line method, respectively.

Obligations and future rental income under non-cancellable operating leases as of March 31, 2003 and 2002 were as follows:

(Lessee)

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Due within one year	¥ 25,456	¥ 21,835	\$ 212,133
Due after one year	313,820	252,757	2,615,167
Total	<u>¥339,276</u>	<u>¥274,592</u>	<u>\$2,827,300</u>

(Lessor)

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Due within one year	¥ 19,290	¥ 15,099	\$ 160,750
Due after one year	269,724	204,420	2,247,700
Total	<u>¥289,014</u>	<u>¥219,519</u>	<u>\$2,408,450</u>

15. Derivatives

The Group enters into foreign exchange forward contracts and interest rate swaps to hedge foreign exchange or interest rate risks.

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

Derivatives are subject to market risk and credit risk. Because the counterparties to those derivatives are limited to major international financial institutions, the Company does not anticipate any losses arising from such credit risk.

The Company implemented a risk control system for derivatives primarily to control the purpose, limitation and selection of the counterparties. The system's primary function is to avoid excess risks associated with derivatives. Each derivative transaction, which is based on these internal policies, is reported to the Director of the Financing Department, and the execution and control of derivatives are managed by the Finance Section of the Company.

As of March 31, 2003, the Group did not have any derivative contracts outstanding.

16. Contingencies

At March 31, 2003, contingent liabilities for notes endorsed with recourse and loans guaranteed in the ordinary course of business amounted to ¥1,483 million (\$12,358 thousand) and ¥80,033 million (\$666,942 thousand), respectively. Included in loans guaranteed were customers' housing loans from banks in the amount of ¥77,870 million (\$648,917 thousand).

17. Merger with Daiwa Danchi Co., Ltd.

Effective April 1, 2001, the Company merged with Daiwa Danchi, which was an associated company. Under the terms of the merger, the Company issued 0.3 shares of its common stock for each Daiwa Danchi common share, which resulted in the issuance of 26,771,371 shares and increases in common stock of ¥1,339 million and capital surplus of ¥25,714 million.

18. Subsequent event

The following appropriations of retained earnings at March 31, 2003 were approved at the Company's shareholders' meeting held on June 27, 2003:

	Millions of yen	Thousands of U.S. dollars
Year-end cash dividends, ¥10.0 (\$0.08) per share	¥5,503	\$45,858

Independent auditors' report

Daiwa House Industry Co., Ltd. and Subsidiaries

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**Deloitte
Touche
Tohmatsum**

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

We have audited the accompanying consolidated balance sheets of Daiwa House Industry Co., Ltd. and subsidiaries as of March 31, 2003 and 2002, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended March 31, 2003, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Daiwa House Industry Co., Ltd. and subsidiaries as of March 31, 2003 and 2002, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2003, in conformity with accounting principles and practices generally accepted in Japan.

As discussed in Note 2, effective April 1, 2001, in accordance with the new accounting standard for financial instruments, available-for-sale securities are reported at fair value. As discussed in Note 3, the Company and certain subsidiaries changed its method of accounting for liability for employees' retirement benefits as of March 31, 2003, and the actuarial loss, which previously would be amortized evenly over principally 10 years, was changed to be amortized when incurred.

Our audits 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 Tohmatsum

June 27, 2003