

Notes to Consolidated Financial Statements

Years ended March 31, 2003 and 2002

1. Basis of Presenting Consolidated Financial Statements

Kobe Steel, Ltd. (the "Company") and its consolidated domestic subsidiaries maintain their official accounting records in Japanese yen and in accordance with the provisions set forth in the Japanese Commercial Code and accounting principles and practices generally accepted in Japan ("Japanese GAAP"). The accounts of overseas subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries of domicile.

Certain accounting principles and practices generally accepted in Japan are different from International Accounting Standards and standards in other countries in certain respects as to application and disclosure requirements. Accordingly, the accompanying financial statements are intended for use by those who are informed about Japanese accounting principles and practices.

The accompanying consolidated financial statements have been restructured and translated into English (with some expanded descriptions and the inclusion of statements of stockholders' equity) from the consolidated financial statements of the Company prepared in accordance with Japanese GAAP and filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Securities and Exchange Law. Some supplementary information included in the statutory Japanese language consolidated financial statements, but not required for fair presentation is not presented in the accompanying consolidated financial statements.

The translation of the Japanese yen amounts into U.S. dollars are included solely for the convenience of readers outside Japan, using the prevailing exchange rate at March 31, 2003, which was ¥120.20 to U.S. \$1.00. The convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

2. Summary of Accounting Policies

(1) Consolidation

The consolidated financial statements include the accounts of the Company and its significant subsidiaries (the "Group"), the management of which is controlled by the Company. For the year ended March 31, 2003, the accounts of 150 (156 in 2002) subsidiaries have been included in the consolidated financial statements. Intercompany transactions and accounts have been eliminated.

Fifty-five consolidated subsidiaries are consolidated using a fiscal period ending December 31, which differs from that of the Company. Any material effects occurring during the January 1 to March 31 period are adjusted in these consolidated financial statements.

In the elimination of investments in subsidiaries, the assets and liabilities of the subsidiaries, including the portion attributable to minority shareholders, are evaluated using the fair value at the time the Company acquired control of the respective subsidiaries.

Investments in unconsolidated subsidiaries and affiliates, over which the Company has significant influence, except for insignificant companies, are accounted for by the equity method.

For the year ended March 31, 2003, 51 (51 in 2002) affiliates were accounted for by the equity method.

The difference, if considered significant, between the cost of investments and the equity in their net assets at their dates of acquisition is amortized over 5 years (40 years for acquisitions made by certain foreign consolidated subsidiaries).

When the Company's share of the net losses of an affiliate exceeds the adjusted cost of the investments, the Company discontinues applying the equity method and the investment is reduced to zero. Such losses in excess of the amounts due from the investee are recorded in other payables, when the losses are expected to be shared by the Company.

(2) Allowance for Doubtful Accounts

The Group provides for doubtful accounts principally at an amount computed based on the actual ratio of bad debts in the past plus the estimated uncollectible amounts based on the analysis of certain individual receivables.

(3) Securities

The Group has no trading securities. Held-to-maturity debt securities are stated at amortized cost. Equity securities issued by subsidiaries and affiliated companies, which are not consolidated or accounted for using the equity method, are stated at moving-average cost. Available-for-sale securities with available fair market values are stated at fair market value. Unrealized gains and unrealized losses on these securities are reported, net of applicable income taxes, as a separate component of stockholders' equity. Realized gains

and losses on sale of such securities are computed using moving-average cost based on carrying value at March 31, 2000 or later date of purchase.

Debt securities with no available fair market value are stated at amortized cost, net of the amount considered not collectible. Other securities with no available fair market value are stated at moving-average cost.

If the market value of held-to-maturity debt securities, equity securities issued by unconsolidated subsidiaries and affiliated companies, and available-for-sale securities declines significantly, such securities are stated at fair market value and the difference between fair market value and the carrying amount is recognized as a loss in the period of the decline. If the fair market value of equity securities issued by unconsolidated subsidiaries and affiliated companies, not on the equity method, is not readily available, such securities should be written down to net asset value with a corresponding charge in the statement of operations in the event net asset value declines significantly. In these cases such fair market value or the net asset value will be the carrying amount of the securities at the beginning of the next year.

(4) Inventories

Inventories are valued at cost, as determined principally by the following methods:

The two main works in the Iron and Steel Segment and the three main plants in the Aluminum and Copper Segment:
.....Last-in, first-out method

Finished goods and work in process in one plant in the Iron and Steel Segment, the Machinery Segment, the Construction Machinery Segment and the Real Estate Segment:
.....Specific identification method

Others:.....Average method

(5) Depreciation

Depreciation of plant and equipment and intangible assets is principally provided using the straight-line method over estimated useful lives. Useful lives are based on tax law. Intangible assets include software for internal use.

(6) Long-term Construction Contracts

Sales and related costs of certain long-term (over one year) construction contracts of the Company are recognized by the percentage of completion method.

(7) Research and Development Expenses

Expenses in respect of the development of new products and research into and the application of new technologies are charged directly to income. Research and development

expenses for the year ended March 31, 2003 were ¥17,797 million (\$148,062 thousand) and ¥22,054 million for the year ended March 31, 2002.

(8) Bond Issue Expenses and Share Issue Expenses

Bond issue expenses and share issue expenses are charged to expenses as they are incurred by the Company and the domestic consolidated subsidiaries.

(9) Income Taxes

The Company and its domestic consolidated subsidiaries apply deferred tax accounting to recognize tax effects of temporary differences between the carrying amounts of assets and liabilities for tax and financial reporting.

Deferred taxes relating to temporary differences between financial accounting and tax reporting are also recognized by certain foreign consolidated subsidiaries.

(10) Employees' Severance and Retirement Benefits

The Company and its consolidated domestic subsidiaries provide two types of post-employment benefit plans, unfunded lump-sum payment plans and funded non-contributory pension plans.

The Company and its consolidated domestic subsidiaries' accrued liabilities and expenses for severance and retirement benefits based on the amounts actuarially calculated using certain assumptions.

The Company and its consolidated domestic subsidiaries provide for employees' severance and retirement benefits based on the estimated amounts of projected benefit obligation and the fair value of the plan assets.

The excess of the projected benefit obligation over the total of the fair value of pension assets as of April 1, 2000, the date of adopting a new accounting standard, and the liabilities for severance and retirement benefits recorded as of April 1, 2000 (the "net transition obligation") are being recognized in expenses in equal amounts primarily over 5 years commencing with the year ended March 31, 2001. Prior service costs are recognized in expenses in equal amounts over 4 years. Actuarial gains and losses are recognized in expenses using the straight-line method within the average of the estimated remaining service lives (mainly 12 years) commencing with the following period.

(11) Allowance for Special Repairs

Blast furnaces and hot blast stoves, including related machinery and equipment, periodically require substantial component replacement and repair. The estimated future costs of such work are provided for and charged to income on a straight-line basis over the period to the date of the anticipated replacements and repair. The difference between such estimated costs and actual costs is charged or credited to

income at the time the repairs take place.

For the year ended March 31, 2003, the Company reversed the allowances for special repairs, which exceeded the future revised cost of repairs to blast furnaces and hot blast stoves located in the Kakogawa Works. Reversal of the allowance for special repairs is shown in the accompanying consolidated statements of operations.

(12) Land Revaluation

Land for operations was revaluated by certain consolidated subsidiaries in accordance with the Land Revaluation Law in the years ended March 31, 2002 and 2001. The revaluation amount, net of related taxes, is shown as a separate component of stockholders' equity.

(13) Provision for Restructuring Costs

The provision for restructuring costs is stated at the estimated loss on restructuring of discontinued operations at the end of the fiscal year.

(14) Translation of Foreign Currencies

Receivables and payables denominated in foreign currencies are translated into Japanese yen at the year-end rates.

Financial statements of consolidated overseas subsidiaries are translated into Japanese yen at the year-end rate, except stockholders' equity accounts which are translated at historical rates and statement of operations items resulting from transactions with the Company at the rates used by the Company.

The Company and its consolidated domestic subsidiaries report foreign currency translation adjustments in stockholders' equity (and minority interests).

(15) Leases

Finance leases, which do not transfer ownership and do not have bargain purchase provisions, are accounted for in the same manner as operating leases by the Company and consolidated domestic subsidiaries.

(16) Cash and Cash Equivalents

In preparing the consolidated statements of cash flows, cash on hand, readily-available deposits and short-term highly liquid investments with maturities not exceeding three months at the time of purchase are considered to be cash and cash equivalents. See note 12.

(17) Derivatives

The Company and its consolidated domestic subsidiaries state derivative financial instruments at fair value and recognize changes in the fair value as gains or losses unless derivative financial instruments are used for hedging purposes.

If derivative financial instruments are used as hedges and meet certain hedging criteria, the Group defers recognition of gains or losses resulting from changes in fair value of derivative financial instruments until the related losses or gains on the hedged items are recognized.

Also, if interest rate swap contracts are used as hedges and meet certain hedging criteria, the net amount to be paid or received under the interest rate swap contract is added to or deducted from the interest on the assets or liabilities for which the swap contract was executed.

(18) Effect of Bank Holiday on March 31, 2002

As financial institutions in Japan were closed on March 31, 2002, ¥7,922 million of trade notes receivable and ¥8,090 million of trade notes payable, maturing on March 31, 2002, were settled on the following business day, April 1, 2002 and accounted for accordingly.

(19) Accounting Standard for Treasury Stock and Reversal of Statutory Reserves

Effective April 1, 2002, the Company adopted the new accounting standard for treasury stock and reversal of statutory reserves (Accounting Standards Board Statement No. 1, "Accounting Standard for Treasury Stock and Reversal of Statutory Reserves", issued by the Accounting Standards Board of Japan on February 21, 2002).

The effect on net income of the adoption of the new accounting standard was not material.

(20) Net Income (Loss) per 1,000 Shares

Effective April 1, 2002, the Company adopted the new accounting standard for earnings per share and related guidance (Accounting Standards Board Statement No. 2, "Accounting Standard for Earnings Per Share" and Financial Standards Implementation Guidance No. 4, "Implementation Guidance for Accounting Standard for Earnings Per Share", issued by the Accounting Standards Board of Japan on September 25, 2002).

The effect on earnings per share of the adoption of the new accounting standard was not material.

3. Differences between Japanese Accounting Principles and International Accounting Standards

As stated in Note 1, there are differences between Japanese GAAP and International Accounting Standards ("IAS"). With respect to the consolidated financial statements, the Company has identified differences between Japanese GAAP and IAS including the significant items summarized below.

It has generally not been practicable to quantify the effects on net income of these differences in accounting policy and determine the additional disclosure required by IAS.

(1) Accounting Principles of Overseas Consolidated Subsidiaries

The Company consolidates the accounts of foreign subsidiaries based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries of domicile. Under IAS 27, the accounting principles used in the financial statements of consolidated subsidiaries should be conformed to the accounting principles of the Group before such financial statements are consolidated.

(2) Leases

IAS 17 requires that finance leases be reflected in the lessee's accounts by recording an asset and liability equal to the lower of the net fair value of the leased property and the present value of the minimum lease payments. The asset should be depreciated and rentals apportioned between finance charges and reduction of the outstanding liability. As described in Note 2 (15), in Japan, finance leases may be accounted for in the same manner as operating leases. For the years ended March 31, 2003 and 2002, the Company had no finance leases that were required to be capitalized.

(3) Inventories

As noted in Note 2 (4), the Company and consolidated domestic subsidiaries value inventories at cost. IAS 2 requires that inventories be measured at the lower of cost and net realizable value. Furthermore, for determining the cost of certain inventories the Company applies the last-in, first-out (LIFO) method which is an allowed alternative treatment under IAS 2 for which additional disclosure is required.

(4) Employees' Severance and Retirement Benefits

As described in Note 2 (10), The net transition obligation is amortized on a straight-line method over 5 years. Under IAS 8 the net transition obligation should be recognized immediately or under IAS 19 as an expense on a straight-line basis over a maximum of 5 years.

4. Leases

Original lease obligations as lessee under non-capitalized finance leases at March 31, 2003 and 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Buildings and structures	¥264	¥266
Machinery and equipment.....	63,222	64,231
	¥63,486	¥64,497
		\$528,169

Future minimum lease payments as lessee under non-capitalized finance leases at March 31, 2003 and 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Due within one year	¥10,481	¥10,410
Due after one year	19,219	19,485
	¥29,700	¥29,895
Lease expense for the years ended March 31	¥12,148	¥12,675
		\$101,065

Future minimum lease payments as lessee under operating leases at March 31, 2003 and 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Due within one year	¥2,322	¥2,064
Due after one year	8,354	3,554
	¥10,676	¥5,618
		\$88,819

Leased assets as lessor under finance leases, accounted for as operating leases, at March 31, 2003 and 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Machinery and equipment.....	¥584	¥618
Less accumulated depreciation	(448)	(433)
	¥136	¥185
		\$1,132

Future minimum lease payments receivable as lessor under finance leases, accounted for as operating leases, at March 31, 2003 and 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Future minimum lease payments receivable:		
Due within one year	¥82	¥93
Due after one year	131	186
	¥213	¥279
Lease income for the years ended March 31	¥105	¥127
		\$874

Future minimum lease payments receivable as lessor under operating leases, at March 31, 2003 and 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Due within one year	¥295	¥299
Due after one year	4,774	5,032
	¥5,069	¥5,331
		\$42,171

5. Securities

The following tables summarize acquisition costs, book values and fair values of securities with available fair values as of March 31, 2003 and 2002:

	Millions of yen						Thousands of U.S. dollars (Note 1)
	2003			2002			2003
	Book values	Fair values	Difference	Book values	Fair values	Difference	Difference
Held-to-maturity debt securities							
Securities with available fair values exceeding book values:							
Bonds.....	¥50	¥54	¥4	¥50	¥55	¥5	¥33
Other securities.....	23	23	—	21	21	(0)	—
	¥73	¥77	¥4	¥71	¥76	¥5	\$33
	Millions of yen			Millions of yen			Thousands of U.S. dollars (Note 1)
	Acquisition costs	Book values	Difference	Acquisition costs	Book values	Difference	Difference
Available-for-sale securities							
Securities with available book values exceeding acquisition costs:							
Equity securities.....	¥7,626	¥10,107	¥2,482	¥9,944	¥13,376	¥3,432	\$20,649
Bonds.....	—	—	—	30	30	0	—
	7,626	10,107	2,482	9,974	13,406	3,432	20,649
Other securities:							
Equity securities.....	17,886	15,080	(2,806)	24,145	19,497	(4,648)	(23,345)
Bonds.....	46	33	(13)	50	37	(13)	(108)
	17,932	15,113	(2,819)	24,195	19,534	(4,661)	(23,453)
	¥25,558	¥25,220	¥(337)	¥34,169	¥32,940	¥(1,229)	\$ (2,804)

The following table summarizes book values of securities with no available fair values as of March 31, 2003 and 2002:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Available-for-sale securities:			
Non-listed equity securities	¥17,550	¥20,772	\$146,007
Preferred subscription certificate	5,000	—	41,597
Non-listed foreign equity securities denominated in yen	—	1,000	—
Non-listed foreign equity securities denominated in foreign currency	—	393	—
Money management fund	—	0	—

Available-for-sale securities with maturities and held-to-maturity debt securities mature as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Within one year	¥5	¥12	\$42
Over one year but within five years	73	470	607
Over five year but within ten years	—	1,000	—

Sales of available-for-sale securities for the years ended March 31, 2003 and 2002 were as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Sales	¥3,260	¥10,615	\$27,121
Gains on sales	310	4,019	2,579
Losses on sales	2,028	14	16,872

Sales of held-to-maturity securities for the year ended March 31, 2002 were as follows:

	Millions of yen
	2002
Book values	¥8,004
Sales	6,867
Net losses on sales	1,137

6. Derivative Transaction

The Group enters into forward currency exchange contracts and currency swap agreements to hedge the risk of changes in foreign currency exchange rates associated with transactions denominated in foreign currencies, interest rate swap agreements and cap agreements to hedge the risk related to interest on borrowings, and commodities forward contracts to hedge the risk of movements in market values of aluminum and copper. The Group does not enter into derivative transactions for speculative purposes. However, the

Group may be exposed to losses in the case of movements in foreign currency exchange rates, interest rates and commodity market values and is exposed to credit risk in the event of non-performance by counterparties to derivative transactions.

The Company has established policies and controls to manage both market and credit risk, including using only highly-rated banks and trading companies as counterparties, hedging exposed positions, limits on transaction types and amounts, and reporting to management.

Forward currency exchange contracts and swap agreements outstanding at March 31, 2003 and 2002 were as follows:

	Millions of yen						Thousands of U.S. dollars (Note 1)
	2003			2002			2003
	Contracted amount	Fair value	Recognized gain (loss)	Contracted amount	Fair value	Recognized gain (loss)	Recognized gain (loss)
Foreign currency exchange contracts							
To sell foreign currencies:							
U.S. dollars	¥6,820	¥6,906	¥(86)	¥7,136	¥7,309	(¥173)	(\$715)
Others	—	—	—	0	0	(0)	—
To buy foreign currencies:							
U.S. dollars	5,073	5,072	(1)	3,977	3,977	(0)	(8)
			¥(87)			¥(173)	(\$723)

1. The fair values were estimated by multiplying the contracted foreign currency amount by the forward rate.

2. The above table does not include derivative transactions for which hedge accounting is applied and outstanding foreign exchange contracts which relate to foreign currency receivables and payables that are recorded in the balance sheet by the contracted foreign exchange rates at March 31, 2003 and 2002.

Interest rate swap agreements outstanding at March 31, 2003 and 2002 were as follows:

	Millions of yen				Thousands of U.S. dollars (Note 1)
	2003		2002		2003
	Contracted amount	Recognized gain (loss)	Contracted amount	Recognized gain (loss)	Recognized gain (loss)
Interest rate swap agreements:					
To receive floating and pay fixed rates	¥3,188	(¥81)	¥2,938	(¥79)	(\$674)
To receive fixed and pay floating followed by fixed rates	55,300	(2,317)	60,000	(2,876)	(19,276)
		(¥2,398)		(¥2,955)	(\$19,950)

1. The recognized gains (losses) were estimated by obtaining quotes from counterparty banks.

2. Hedge accounting was not applied to the derivative transactions in the above table at March 31, 2003 and 2002.

7.Short-Term Borrowings and Long-Term Debt

Short-term borrowings at March 31, 2003 and 2002 consisted of the following:

consisted of the following:	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Bank loans (average rate 1.4% in 2003, and 1.2% in 2002).....	¥164,025	¥221,028	\$1,364,601

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

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Floating rate (Libor plus 0.5%) notes due 2002	¥ —	¥10,000	\$ —
Floating rate (Libor plus 0.75%) notes due 2003	—	2,000	—
Floating rate (Libor plus 0.95%) notes due 2004	2,139	4,440	17,804
Floating rate (20 year swap rate minus 2 year swap rate plus 1.2% per annum subject to minimum interest rate of 0.0% per annum) notes due 2007	10,000	10,000	83,195
1.12% to 3.58% yen bonds, due 2002 through 2012	272,900	348,248	2,270,383
Euro medium-term notes, due 2003 through 2005	6,147	10,220	51,140
Loans, principally from banks and insurance companies	503,194	536,218	4,186,306
	794,380	921,126	6,608,828
Less current portion	154,775	193,238	1,287,646
	¥639,605	¥727,888	\$5,321,181

The aggregate annual maturities of long-term debt at March 31, 2003 were as follows:

Years ended March 31

Years ended March 31	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
2004	¥154,775	¥193,238	\$1,287,646
2005	178,824	176,426	1,487,720
2006	128,158	131,437	1,066,206
2007 and thereafter	332,623	420,025	2,767,256
	¥794,381	¥921,126	\$6,608,828

At March 31, 2003 and 2002, assets pledged as collateral for short-term borrowings and long-term debt were as follows:

short-term borrowings and long-term debt were as follows:		Millions of yen	Thousands of U.S. dollars (Note 1)	
		2003	2002	2003
Assets pledged as collateral				
Plant and equipment-net of accumulated depreciation.....		¥251,715	¥152,763	\$2,094,135
Other assets.....		17,512	24,348	145,691
		¥269,227	¥177,111	\$2,239,826
Secured short-term borrowings and long-term debt				
Bonds (includes due within 1 year).....		¥3,265	¥7,278	\$27,163
Short-term borrowings.....		23,538	29,912	195,824
Long-term borrowings (includes due within 1 year).....		98,499	108,203	819,459
Other debt.....		99	—	824
		¥125,401	¥145,393	\$1,043,270

With the start of operations of Shinko Kobe Power Inc. on April 1, 2002, the construction in progress account which includes the plant which is pledged at the end of March 2002 as collateral for a long-term loan. The cost of the pledged asset is approximately ¥114 billion.

At March 31, 2003 included in the assets pledged as collateral are assets that are promised to be pledged as collateral for the short-term borrowings of ¥10,848 million (\$90,250 thousand) and long-term borrowings of ¥61,388 million (\$510,715 thousand) as well as the above-mentioned debt.

8. Contingent Liabilities

At March 31, 2003 the Company and its consolidated domestic subsidiaries were contingently liable as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Trade notes discounted	¥7,977	¥10,242	\$66,364
Trade notes endorsed	2,140	556	17,804
Guarantees of loans			
Related parties	6,948	11,727	57,804
Others	3,798	4,740	31,597
Contingent liability undue debt assumption agreement	25,000	—	207,987
	¥45,863	¥27,265	\$381,556

Guarantees of loans include contingent guarantees and letters of awareness of ¥685 million (\$5,699 thousand)

9. Stockholders' Equity

Under the Commercial Code of Japan, the entire amount of the issue price of shares is required to be accounted for as capital, although a company may, by resolution of its Board of Directors, account for an amount not exceeding one-half of the issue price of the new shares as additional paid-in capital, which is included in capital surplus. Effective October 1, 2001, the Commercial Code provides that an amount equal to at least 10% of cash dividends and other cash appropriations shall be appropriated and set aside as a legal earnings reserve until the total amount of legal earnings reserve and additional paid-in capital equals 25% of common stock. The total amount of legal earnings reserve and additional paid-in capital of the Company has reached 25% of common stock, and therefore the Company is not required to provide any more

legal earnings reserve. The legal earnings reserve and additional paid-in capital may be used to eliminate or reduce a deficit by resolution of the shareholders' meeting or may be capitalized by resolution of the Board of Directors.

On condition that the total amount of legal earnings reserve and additional paid-in capital remains equal to or exceed 25% of common stock, they are available for distribution by the resolution of shareholders' meeting. Legal earnings reserve is included in retained earnings in the accompanying financial statements.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Commercial Code.

10. Selling, General and Administrative Expenses

Selling, general and administrative expenses for the years ended March 31, 2003 and 2002 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Freight	¥30,321	¥31,099	\$252,255
Employees' compensation	29,142	34,757	242,446
Research and development	5,430	7,592	45,175
Depreciation	3,084	4,686	25,657
Other	54,301	62,186	451,755
	¥122,278	¥140,320	\$1,017,288

11. Income Taxes

Significant components of the Group's deferred income tax assets and liabilities as of March 31, 2003 and 2002 were as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Deferred income tax assets:			
Loss carryforwards	¥44,554	¥60,720	\$370,666
Unrealized profit	20,486	24,548	170,433
Other	59,462	61,762	494,691
Total deferred income tax assets	124,502	147,030	1,035,790
Valuation allowance	(17,696)	(15,257)	(147,221)
Deferred income tax assets	106,806	131,773	888,569
Deferred income tax liabilities:			
Gain on merger	12,666	15,402	105,374
Deferred gains on sales of property	3,156	13,189	26,256
Other	8,054	14,330	67,006
Total deferred income tax liabilities	23,876	42,921	198,636
Net deferred income tax assets	¥82,930	¥88,852	\$689,933

Significant items in the reconciliation of the aggregate statutory income tax rate to the effective income tax rate for the year ended March 31, 2003 were as follows:

	2003
Aggregate statutory income tax rate in Japan	42.0%
Non-deductible entertainment expenses	20.2
Reduction of carry-forward tax assets due to tax rate changes	18.4
Revision of tax effect due to unrealized gains in fixed assets	17.7
Equity in income of unconsolidated subsidiaries and affiliates	(14.7)
Other	0.6
Effective income tax rate	84.2%

Significant items in the reconciliations of the aggregate statutory income tax rate to the effective income tax rate for the year ended March 31, 2002 are not disclosed because of the loss before income taxes.

The aggregate statutory income tax rate will be reduced for the years commencing on April 1, 2004 or later due to the revised local tax law. At March 31, 2003, the Company and consolidated domestic subsidiaries applied the reduced aggregate statutory income tax rate of 40.6 % for calculating deferred tax assets and liabilities that are expected to be recovered or settled in the years commencing on April 1, 2004 or later. As a result, deferred taxes assets decreased by ¥2,875 million (\$23,918 thousand), provision for deferred income taxes increased by ¥2,949 million (\$24,534 thousand), net unrealized holding losses on securities increased by ¥5 million (\$42 thousand) and land revaluation increased by ¥79 million (\$657 thousand) compared with what would be reported using the currently applicable tax rate of 42.0%.

12.Consolidated Statements of Cash Flows

The reconciliations of cash and cash equivalents in the cash flow statements and balance sheets are as follows:

March 31, 2003 and 2002

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2003	2002
Cash and cash equivalents (balance sheet).....	¥82,419	¥115,900
Time deposits (due over 3 months)	(610)	(633)
Repurchase agreements accounted for as short term loans receivable.....	—	5
Money management fund accounted for as marketable securities	—	20
Cash and cash equivalents (cash flow statement).....	¥81,809	¥115,292
		\$680,607

Non-cash transactions-Finance leases calling for total payments of ¥23,999 million (\$199,659 thousand) and ¥34,359 million were entered into for the years ended March 31, 2003 and 2002 respectively.

Assets and liabilities of KMT Semiconductor Co., Ltd., which was excluded from consolidated subsidiaries for 2002, were as follows:

April 1, 2001

	Millions of yen
Current assets	¥19,794
Fixed assets	52,908
Total assets	¥72,702
Current liabilities	¥34,582
Long-term liabilities	10,618
Total liabilities	¥45,200

Assets and liabilities of Kobelco System Co., Ltd., which was excluded from consolidated subsidiaries for 2002, were as follows:

March 31, 2002

	Millions of yen
Current assets	¥8,233
Fixed assets	1,459
Total assets	¥9,692
Current liabilities	¥5,465
Long-term liabilities	1,337
Total liabilities	¥6,802

Assets and liabilities of Kobelco America Inc., which was excluded from consolidated subsidiaries for 2002, were as follows:

December 31, 2001

	Millions of yen
Current assets	¥11,503
Fixed assets	1,962
Total assets	¥13,465
Current liabilities	¥8,310
Long-term liabilities	59
Total liabilities	¥8,369

13.Related Party Transactions

Net sales include sales to Shinsho Corporation, which is an affiliate of the Company, of ¥146,111 million (\$1,215,566

thousand) and ¥155,244 million for the years ended March 31, 2003 and 2002, respectively.

14.Employees' Severance and Retirement Benefits

The liabilities for severance and retirement benefits included in the liability section of the consolidated balance sheets as of March 31, 2003 and 2002 consist of the following:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Projected benefit obligation	¥(221,360)	¥(219,937)	\$(1,841,597)
Fair value of pension assets	118,570	134,498	986,439
Unrecognized net transition obligation	26,842	39,687	223,311
Unrecognized actuarial differences	47,754	19,140	397,288
Unrecognized prior service costs	(13,950)	(20,925)	(116,057)
Prepaid pension cost	(12,062)	(7,282)	(100,349)
Liability for severance and retirements benefits	¥(54,206)	¥(54,819)	\$(450,965)

Included in the consolidated statements of operations for the years ended March 31, 2003 and 2002 are severance and retirement benefit expenses comprised of the following:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	2002	2003
Service costs - benefits earned during the year	¥6,758	¥8,138	\$56,223
Interest cost on projected benefit obligation	6,130	7,497	50,998
Expected return on plan assets	(3,095)	(3,152)	(25,749)
Amortization of net transition obligation	12,813	13,090	106,598
Amortization of actuarial differences	1,741	1,871	14,484
Amortization of prior service costs	(6,975)	(6,975)	(58,028)
Severance and retirement benefit expenses	¥17,372	¥20,469	\$144,526

Notes

1. The estimated amount of all retirement benefits to be paid at future retirement dates is allocated equally to each service year using the estimated number of total service years.
2. The discount rates are mainly 2.5% in 2003 and 3.0% in 2002 and the rates of expected return on plan assets used by the Group are mainly 3.1% in 2003 and 2002.
3. During the year ended March 31, 2002, the Company changed the rules and regulations of post-employment benefit plans. As a result, the projected benefit obligation decreased.

15. Segment Information

(1) Industry Segment

The Group's operations are divided into six principal business segments: Iron and Steel, Aluminum and Copper, Machinery,

Construction Machinery, Real Estate, and Other Businesses. Business segment information was as follows:

Years ended March 31, 2003 and 2002		Millions of yen		Thousands of U.S. dollars (Note 1)
		2003	2002	2003
Sales to outside customers:	Iron and Steel	¥511,750	¥476,023	\$4,257,488
	Aluminum and Copper	247,330	256,030	2,057,654
	Machinery	209,280	223,457	1,741,098
	Construction Machinery	156,929	147,885	1,305,566
	Real Estate	38,293	40,063	318,577
	Other Businesses	41,168	54,556	342,496
	Consolidated net sales	1,204,750	1,198,014	10,022,879
Inter-segment sales:	Iron and Steel	11,725	10,360	97,545
	Aluminum and Copper	710	511	5,907
	Machinery	6,936	8,755	57,704
	Construction Machinery	470	420	3,910
	Real Estate	4,297	4,984	35,749
	Other Businesses	15,201	27,605	126,464
		39,339	52,635	327,279
Total sales:	Iron and Steel	523,475	486,383	4,355,033
	Aluminum and Copper	248,040	256,541	2,063,561
	Machinery	216,216	232,212	1,798,802
	Construction Machinery	157,399	148,305	1,309,476
	Real Estate	42,590	45,047	354,326
	Other Businesses	56,369	82,161	468,960
		1,244,089	1,250,649	10,350,158
Operating costs and expenses:	Iron and Steel	474,707	475,110	3,949,309
	Aluminum and Copper	235,637	248,573	1,960,375
	Machinery	211,993	228,501	1,763,669
	Construction Machinery	153,330	146,445	1,275,624
	Real Estate	38,261	37,095	318,311
	Other Businesses	50,663	81,306	421,489
	Eliminations	(40,895)	(54,515)	(340,224)
	Consolidated operating costs and expenses	1,123,696	1,162,515	9,348,553
Operating income:	Iron and Steel	48,768	11,273	405,724
	Aluminum and Copper	12,403	7,968	103,186
	Machinery	4,223	3,711	35,133
	Construction Machinery	4,069	1,860	33,852
	Real Estate	4,329	7,952	36,015
	Other Businesses	5,706	855	47,471
	Eliminations	1,556	1,880	12,945
	Consolidated operating income	¥81,054	¥35,499	\$674,326

Years ended March 31, 2003 and 2002

		Millions of yen		Thousands of U.S. dollars (Note 1)
		2003	2002	2003
Assets:	Iron and Steel	¥908,093	¥954,727	\$7,554,850
	Aluminum and Copper	241,134	246,113	2,006,106
	Machinery	229,269	255,911	1,907,396
	Construction Machinery	172,521	180,720	1,435,283
	Real Estate.....	121,370	165,529	1,009,734
	Other Businesses	71,702	74,161	596,522
	Corporate and Eliminations	158,553	168,142	1,319,077
	Total.....	1,902,642	2,045,303	15,828,968
Depreciation:	Iron and Steel	54,606	52,670	454,293
	Aluminum and Copper	11,920	14,188	99,168
	Machinery	7,941	8,256	66,065
	Construction Machinery	3,001	3,229	24,967
	Real Estate.....	2,044	2,696	17,005
	Other Businesses	3,308	3,508	27,521
	Corporate and Eliminations	2,270	2,368	18,884
	Total.....	85,090	86,915	707,903
Capital expenditures:	Iron and Steel	27,410	106,029	228,037
	Aluminum and Copper	7,685	8,831	63,935
	Machinery	3,874	3,181	32,230
	Construction Machinery	1,697	4,812	14,118
	Real Estate.....	1,532	7,215	12,745
	Other Businesses	1,327	1,564	11,040
	Corporate and Eliminations	446	788	3,710
	Total.....	¥43,971	¥132,420	\$365,815

Corporate assets

Corporate assets of ¥287,352 million (\$ 2,390,616 thousand) and ¥269,468 million at March 31, 2003 and 2002, respectively, are comprised principally of bank and time deposits and assets of administration departments of the Company.

(2) Geographic Area

Years ended March 31, 2003 and 2002

		Millions of yen		Thousands of U.S. dollars (Note 1)
		2003	2002	2003
Sales to outside customers:	Japan	¥1,115,160	¥1,083,359	\$9,277,537
	Asia	38,314	25,591	318,752
	North America	16,394	47,379	136,389
	Other areas	34,882	41,685	290,201
	Total	1,204,750	1,198,014	10,022,879
Inter-segment sales:	Japan	30,559	33,385	254,235
	Asia	1,111	1,284	9,243
	North America	2,949	2,101	24,534
	Other areas	208	296	1,730
	Total	34,827	37,006	289,742
Total sales:	Japan	1,145,719	1,116,744	9,531,772
	Asia	39,425	26,875	327,995
	North America	19,343	49,480	160,923
	Other areas	35,090	41,981	291,931
	Total	1,239,577	1,235,080	10,312,621
Operating costs and expenses:	Japan	1,069,708	1,085,140	8,899,401
	Asia	36,451	26,271	303,253
	North America	19,415	48,284	161,522
	Other areas	33,606	40,413	279,585
	Eliminations	(35,484)	(37,593)	(295,208)
	Total	1,123,696	1,162,515	9,348,553
Operating income:	Japan	76,011	31,604	632,371
	Asia	2,974	604	24,742
	North America	(72)	1,196	(599)
	Other areas	1,484	1,568	12,346
	Eliminations	657	527	5,466
	Total	81,054	35,499	674,326
Assets:	Japan	1,534,963	1,700,758	12,770,075
	Asia	36,661	29,046	305,000
	North America	41,215	43,770	342,887
	Other areas	42,733	55,196	355,516
	Corporate and eliminations	247,070	216,533	2,055,490
	Total	¥1,902,642	¥2,045,303	\$15,828,968

Principal countries in each segment are:

AsiaSingapore, Malaysia, Thailand, China
 North AmericaUnited States, Canada
 Other areasNetherlands, Australia

Corporate assets of ¥287,352 million (\$2,390,616 thousand) and ¥269,468 million at March 31, 2003 and 2002, respectively, are comprised principally of bank and time deposits and assets of administration departments of the Company.

(3) Overseas Sales

Overseas sales for the years ended March 31, 2003 and 2002 were as follows:

Years ended March 31, 2003 and 2002		Percentages of 2003 consolidated net sales	Millions of yen		Thousands of U.S. dollars (Note 1)
			2003	2002	2003
Overseas Sales:	Asia	13.3%	¥160,215	¥123,202	\$1,332,904
	North America	2.8%	33,916	52,028	282,163
	Other areas	4.6%	54,804	60,570	455,940
	Total	20.7%	¥248,935	¥235,800	\$2,071,007

Overseas sales consisted of export sales of the Company and domestic consolidated subsidiaries, and sales of overseas consolidated subsidiaries excluding sales to Japan.

Principal countries and areas in each segment are:

AsiaChina, Taiwan, South Korea,
 Malaysia, Indonesia
 North AmericaUnited States, Canada
 Other areasAustralia, Italy