Capcom is a corporation who provides “infinite media” that transmits unlimited excitement, embodying the world of imagination and delivering it to users. By crossing all linguistic and cultural barriers, we help to build a bridge of communication between the people of the world.

Opening up a new dimension of creativity with flowing originality and superior technique, we are boldly taking up the challenge to transcend all information media.

Capcom is involved in numerous areas of the amusement industry. Having established our place in the arcade game industry with the Streetfighter series, we also produce and sell arcade machines, home video games and manage amusement facilities. Since our start in May 1979, we have taken a leading role in the game software industry and have continued to respond to the demands and expectations of modern society. In October 1993, our shares were listed on the second section of the Osaka Stock Exchange. Subsequently we have succeeded in producing one hit after another, and the release of Resident Evil in March 1996 established a new genre, “Survival Horror”, which is unrivaled by our competitors. The outstanding Resident Evil Series, which has worldwide popularity overseas as well as in Japan, has contributed enormously to Capcom’s growth.

With the 21st century just around the corner, we are aware that a uniform approach will not enable us to fully respond to consumers’ increasingly diversified needs. Dedicated to inspiring each and every person, we will be entirely flexible in selling and renting both arcade games and home video games, as well as venturing into new fields. We will continue our commitment to offering people access to the world of innovative entertainment.

### COMPANY PROFILE

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### Financial Highlights

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<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Net sales</strong></td>
<td>¥ 58,201</td>
<td>¥ 41,650</td>
<td>$ 36,061</td>
</tr>
<tr>
<td><strong>Net income (loss)</strong></td>
<td>( ¥ 4,760)</td>
<td>502</td>
<td>( ¥ 36,061)</td>
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<tr>
<td><strong>Shareholders’ equity</strong></td>
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<td>36,267</td>
<td>224,333</td>
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<tr>
<td><strong>Amounts per share (in yen and dollars)</strong></td>
<td>( ¥ 135.24)</td>
<td>¥14.29</td>
<td>($ 1.02)</td>
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<tr>
<td><strong>Cash dividends</strong></td>
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<td>53.00</td>
<td>0.15</td>
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<tr>
<td><strong>Total assets</strong></td>
<td>¥ 100,833</td>
<td>¥ 118,330</td>
<td>$ 673,886</td>
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</table>

Note: U.S. dollar amounts are translated from yen, for convenience only, at the rate of ¥132 to $1. Amounts per share are computed based on weighted average method and are retroactively adjusted for the effect of the stock splits.
For Capcom, fiscal 1997 was an excellent year in which we continued to expand our net sales and market share. On a global scale, sales growth and market potential are expected to increase in the software industry, one of the key industries of the 21st century. In particular, the rapidly increasing popularity of 32-bit game machines has been an important factor in Capcom's favor, and we will utilize our expertise in the interactive entertainment world to further position the company in the consumer and arcade game markets.

Net sales and operating income have grown annually for three straight years, and we are pleased to report increased earnings this term as well. Total income on a consolidated basis rose from ¥41,650 million to ¥58,201 million, an increase of 39.7% over the last term, and operating income was up 94.7% from ¥5,353 million to ¥10,423 million, one of Capcom’s highest profits. These results are indicative of Capcom’s top-class earning power in the software industry.

On a net profit basis, we recorded a deficit balance of ¥4,760 million as a result of a total of ¥13,000 million in special losses, due to asset appraisal of our subsidiaries and a focus on cash flow in order to improve our financial position. The special losses include ¥8,000 million required to liquidate our subsidiary Capcom Mexico, ¥3,000 million in reserves for credit to our finance subsidiary, ¥2,000 million in reserves for credit to our overseas business agent. This term’s readjustments of doubtful assets have contributed enormously to improving operational control and efficiency, and we have disposed of the majority of worthless assets and unprofitable divisions. As a result, our financial balance has improved. Owing to our good performance, cash flow has strengthened significantly and we were able to redeem this term’s convertible bonds of ¥11,346 million as well as last term’s mortgage bonds and convertible bonds of ¥6,337 million, which further contributed to improved performance.

Furthermore, with cash flow predicted to increase ¥910 billion annually, we will be able to provide the capital to repay ¥25 billion in convertible bonds redeemable in September 2001.

In the home video game hardware market, Sony Computer Entertainment clearly emerged as the leader this term. Nintendo is close behind with formidable sales of its popular N64 console, while Sega is now focusing on the launch of its new 128-bit Dreamcast system this fall in Japan. In light of these circumstances, we will continue to increase development efforts for the PlayStation, but following a recent licensing agreement with Nintendo, we also plan to release our first N64 product next term. As hardware transitions take place, we will continue our multi-platform strategy to flexibly develop products that offer variety, quality and a long life span.

Our premier product, Resident Evil 2, was undeniably one of the industry’s most successful products this year, selling more than 3.6 million units in the first two months of its release, with sales rivaling that of major motion pictures. Towards the end of this term, total sales of the Resident Evil series amounted to over 7.5 million units, and its popularity has stirred excitement across the globe. Its predecessor, Resident Evil, gave birth to “survival horror”, one of the most popular genres to date. While other software developers and publishers have had successes in duplicating this style, it was Resident Evil that clearly paved the way. Resident Evil sets the standard for 32-bit game machines, fully utilizing the system’s outstanding performance in game requisites such as visual effects, sound reproduction and screenplay. Furthermore, Resident Evil 2 has been the driving force in positioning the PlayStation as the leading console in the home video game hardware market. An undeniable leader in the market, Capcom continues to drive sales by releasing innovative series for home video game software such as the Resident Evil series, our ever popular Mega Man series and the unforgettable Street Fighter line.

Marketing and public relations efforts have been stepped up to improve Capcom’s visibility. We continue to emphasize the importance of strategic product release timing as an effective sales device, and the distribution knowledge used to create Capcom’s mega-hits is being utilized on our entire line. Another key element to Capcom’s success is retailer relationships. Always the innovator, we are introducing an industry first sales promotion program for the American market called Fighter’s Edge, which offers advantages to the consumer for purchasing multiple Capcom fighting games and benefits the retailer by generating store traffic. This program will also breathe new life into Capcom’s product catalogue by providing advertising support for every fighting game. This type of original thinking, coupled with our strong key retailer relationships, allows for excellent product display, quality in-store promotions and valuable pre-order benefits.

This term our domestic and North American operations have experienced remarkable success, as a result of our global marketing efforts combined with the excellence of our software. We anticipate that next term’s release of Resident Evil 2 in Europe will largely increase our revenue in the region. Our success is supported by our strength in the R&D field. The R&D division anticipates changing times and values and concentrates on developing new products to respond to market needs, aiming to develop outstanding software games that surpass Resident Evil. Capcom Digital Studios, our R&D base in North America, is focusing on developing and publishing original products to suit the American consumer. The expertise of our R&D staff will contribute enormously to Capcom’s growth.

Creativity, our forte, has broadened through years of developing arcade game software. Using cutting-edge technology and ideas, we produce arcade games first and then utilize the same know-how in developing home video games to produce high-quality, best-selling home games. It is the multiple effects of our accumulated expertise in both fields that has built the Capcom of today. Popular game properties such as the Street Fighter series has secured a firm position for Capcom in this highly-competitive industry.

We utilize this same expertise in amusement facility management. The convergence of entertainment is especially prevalent in this field as the classic arcade is replaced with venues that encompass other forms of entertainment including bars, restaurants, shopping centers and indoor sports centers. Additionally, the development of family entertainment centers is moving forward. Our first location in the US that incorporates this concept in a recently opened and improved Nickel City, a new amusement facility with a theme integrated into the local community. Nickel City has succeeded in attracting a large customer base, offering services that meet players’ expectations, and contributing to the development of the region by providing safe facilities at an extremely low price. Our continued awareness of the changing times, and our commitment to providing users with the high-quality products and services they require, allows us to adapt and excel in this ever-changing market.

Licensing showed excellent growth and continues to be an important aspect of our business. In an effort to better leverage our properties, we have established and continue to maintain numerous solid licensing relationships with various corporations. As a recent example, the success of the Resident Evil series has peaked interest from Hollywood with plans for a feature film underway.

Capcom leads the industry through our unwavering commitment of providing end users with products that immerse them into a world of superior entertainment. This pledge to the customer guarantees that we will continue to produce best-selling products that meet the highest industry standards through continued technology investments. Considering the breadth of the market, we must continue to address the varied interests of the consumer by providing a diverse lineup of products, and for this purpose we are working with cutting-edge technology to develop the highest quality and most entertaining properties.

When all is said and done, it is our employees that sustain our role as an industry leader. Their continued passion for excellence in product management, creativity, technological expertise and consumer awareness is unparalleled. My sincerest thanks to all of Capcom’s employees and you, our stockholders, for your support as we continue to demonstrate our ingenuity and expertise in one of the most exhilarating industries in the world.

Kenzo Tsujimoto
President
Creating Games that Fulfill Players’ Criteria

Here we introduce the extent of Capcom’s perfection through the ultimate interactive video game, Resident Evil 2.

1. Sharing Values with the Player

The player’s action changes the course of the story. Either of the two leading characters can be selected and the system allows the player to switch back and forth between the two. This results in an intricate sequence of alternating companions who crack the mystery, while maintaining complete control. Ultimately, it is up to the player to decide how the story ends. Capcom believes in producing games that draw on the players’ imagination and creativity. Since we allow such flexibility, we cater to the players’ desire to be the infinite “game-master.”

2. Meeting Players’ Expectations with High-Quality Games

Resident Evil 2 is an adventure game in which the player hunts for and destroys all the rooms in which there are zombies. The player searches for the escape route while solving the mystery of the virus and eliminating the enemies on the way. The unprecedented scare-factor has contributed towards establishing a new industry genre: “survival horror.” This large-scale game with its complex and interesting story has even succeeded in attracting female fans who tend to make up only a small portion of the growing market.

“There are professionals drawing pictures, creating programs and composing music for video games, but not writing screenplays. We would like to improve the standard of screenplays throughout the video game industry.” (Yoshiki Okamoto, President, Flagship)

3. Creativity without Compromise

There are more zombies and weapons in Resident Evil 2 than the original. The movement of both humans and monsters has been greatly improved. The stereoscopic 3D polygon technique makes the graphics even more realistic, allowing the player to feel that he or she is really there. The submerging sound and cinematic gameplay raises the level of fear, enhancing the true to life feeling of the “survival horror” genre.

In cooperation with Sony Music Entertainment Intermedia (SIM), Capcom ventured into the music world with the establishment of Suleputer, a music software production and marketing label set up within the Multimedia Department of the R&D Division.

This term Capcom brought in a number of well-known screenwriters with television and film experience and set up a new company, Flagship, to specialize in plotting new video games. The specialist screenwriters include Hirohisa Masuda (Power Ranger, Kikaida) and Shozo Uehara (Ultraman). On a par with movies, Capcom’s exciting screenplays broaden the player’s horizon and contribute to market growth.
At Capcom we consider video games a medium for helping players to enrich their perceptiveness. Our true to life games enable the player to develop their senses through maximum enjoyment. This type of sensory development can be found by reading novels and comic strips or by watching movies and animated cartoons.
Divisions

Arcade Game Division

The return of old favorites this term ensured that the popular Marvel Super Heroes vs. Streetfighter and Marvel vs. Capcom Clash of Super Heroes would be successful at home and abroad. Vampire Savior also enjoyed good sales due to its strong following. The unique Rival Schools with elaborately devised characters made headway in the competitive fighting game market. However, net sales were down slightly in this division since the release of other leading games was held back until next term.

Arcade Game Rental Division

Capcom game machines can be found around the country in a variety of locations, including video stores, convenience stores and shopping centers. During this term we focused on consolidating and reorganizing rental machines and increasing the number of games in profitable, well-patronized locations to improve profitability. Through our explicit product strategy and efficient development of arcade locations, we endeavored to increase repeat orders and stimulate the demand for new business. Despite our efforts, results were sluggish due to a fall in the customer unit price and a static market.

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Home Video Game Division

The second installment in the “survival horror” series Resident Evil 2 was released in the home console market this term and was an instant blockbuster. Capcom experienced record-breaking sales with Resident Evil 2, selling 3.6 million units in the first two months. Incorporating computer graphics with 3D polygons, realistic images and movie-like production techniques, Resident Evil 2 boasts a degree of excellence that transcends the first game. The title gained overwhelming popularity among fans around the world. The additional release of Resident Evil Director’s Cut anchored the popular Resident Evil series as one of Capcom’s leading franchises. Megaman X4 and Megaman 8 enjoyed solid sales due to a nationwide campaign to commemorate Megaman’s 10th anniversary. Breath of Fire III, another addition to a popular series, has also done well. As a result, the home video game division recorded a substantial increase in revenue.

Amusement Facilities Division

Capcom creates clean amusement facilities with a pleasant atmosphere in harmony with our concept of “managing clean, bright and fun facilities”. At present, we manage 50 facilities in Japan, 7 overseas, and are striving to unearth demand and develop new customer business. Our new facilities include Plaza Capcom Pal Pal, Plaza Capcom Yokosuka (a Las Vegas-style facility and our first in a city shopping mall) and the recently renovated Capcom Circus. Several more facilities are scheduled to open within the year. Our commitment to attracting families to our establishment distinguishes our amusement facilities from others. In particular, Nickel City in San Jose, California is enjoying great success in the region as a new social and recreation spot. When it comes to managing dreamlike amusement facilities, Capcom is on the leading edge.
A World of Creativity

Creators Adhere to a High-Quality Source

Production of one game takes at least one year to finish, and sometimes takes several years. Graphics are drawn repeatedly to achieve the most appealing pictures, while the program is modified to give a sense of split-second action. Perfectionists produce Capcom's games. These games are typically regarded highly among the editorial community.

If the creators are not satisfied, we can't expect the players to be.

Latest Equipment and Greater Manpower to Enhance Development

The genius of Capcom's top quality creators are Capcom's greatest resources. Our development and research staff, whose work includes game planning, character design, setting design, sound production and program design, constitutes 60% of the total work force. Even before the establishment of the screenplay-planning company, Flagship, we endeavored to develop games using our innovative methodology. We have continually succeeded in creating high-grade original games. All these specialists are supported by highly-experienced producers and cutting-edge machinery installed at our Research and Development Building.

Sweeping Popularity for Home Video Games

Having succeeded in the arcade game business, we began to make inroads in the home video game market. Over ten years ago, Capcom began an OEM contract with Nintendo Co., Ltd. Now, we are fully confident in our ability to fulfill the needs of consumers who require higher quality and a wider variety for home video games. The advent of the first 16-bit and later 32-bit home video game machine has accelerated our involvement in the home video game market. Most of the arcade software we have produced using our own “CP System” can be converted to be used on home video game consoles. Moreover, we have accumulated the knowledge necessary for producing these games.

Capcom’s Unique Flair for Creativity

Drawing from our gold mine of creative power, we will work to stay ahead of our competitors and bring our creativity into full play. Whether it be in graphics, character formation, screenplay, music, game design, Capcom will maintain its leadership role.

Overseas Operation

There are no cultural or national boundaries when it comes to good-quality software, and this is shown by Capcom's rising international position in the game and entertainment world. Accordingly, we have an increasing responsibility to respond to customers' needs by developing outstanding and interesting software. We continue in our efforts to provide the best products and service through our sales network that covers the globe.

North America

The Capcom USA consolidated group consists of Capcom USA, the holding company, Capcom Coin-Op which sells arcade game machines and operates amusement facilities, Capcom Entertainment which sells home video products, and Capcom Digital Studios, which develops games for the US market. As a result of the past restructuring of our US operations, we have been able to expand the business efficiently and improve our position in the market. This term we posted the highest income in the company's history, which was supported by Capcom Entertainment's favorable returns.

Asia

Capcom Asia carries an important role in the Asian region and we anticipate high potential in this market. Capcom Asia aims to discover potential markets and increase popularity in Asia while balancing business between the arcade game and consumer game markets.

Europe

We have achieved a firm position in the European game market through our sales network at Capcom Europe. The release of Resident Evil 2 in Europe next term is expected to increase our revenue in the region.

This term we decided to close down Capcom Mexico. Although we have had long-term goals to maintain our overseas operations, in light of the current financial situation, and the impact of changes in the industry, we consider it necessary to improve our financial balance. This includes repaying short-term credit. It will take time to rectify the cumulative losses which accompanied the currency crisis in Mexico. We took action to liquidate the company and since then our Mexican division has experienced satisfactory results and remained in the black during fiscal 1997. We will change our policy to expand sales through an agency, ensuring smooth sales activity in the Mexican market.

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Corporation History

1979
May: Capcom is established as a manufacturer and distributor of electronic game machines.

1983
Oct.: Tokyo branch office opens.

1985
Jul.: A contract is concluded with Nintendo Co., Ltd. for the sale of Nintendo Entertainment System software.
Aug.: Capcom USA is established in California.

1988
May: An important contract is concluded with Walt Disney Company for the development and marketing of games featuring Disney themes/characters.
Jul.: The CP System, Capcom’s unique hardware system for arcade game machines, is put on the market.

1989
Apr.: Capcom enters the rental arcade game machine business.
May: Matsubara Works opens in Osaka Prefecture.

1990
Mar.: The head office building opens.
Oct.: Over-the-counter trading of Capcom stock begins.
Dec.: Employee recreation facilities in Mie Prefecture are completed.

1991
Feb.: Sapporo sales office opens.
Apr.: Fukuoka sales office opens.
Nov.: Convertible bonds due 1996 ($101 million) payable in Swiss francs are issued.

1992
Feb.: Hirano Works opens in Osaka Prefecture. Capcom Europe GmbH is established in Germany to spearhead sales for the European region.
Jul.: Sendai sales office opens.
Sep.: Nagoya sales office opens.
Oct.: Convertible bonds due 1996 ($20 billion) are issued. Okayama sales office opens.

1993
Mar.: Contract with Sega Enterprises is concluded for the manufacture and sale of video game software.
Apr.: Capcom enters the amusement facilities business.
May: Convertible bonds due 1997 ($12 billion) are issued.
Jul.: Capcom Asia Company Ltd. is established in Hong Kong to lead sales for the China and Southeast Asia region.
Aug.: Nagoya sales office opens.
Oct.: Trading unit changes from 1,000 to 100.

1994
May: Ueno Works opens in Mie Prefecture.
Jun.: Convertible bonds due 2001 ($25 billion) are issued.
Aug.: Release of the animated movie Street Fighter II.
Oct.: Release of the action movie Street Fighter.

1995
Jun.: Capcom Coin-Op Inc., Capcom Entertainment Inc., and Capcom Digital Studios, Inc. are established with Capcom USA as the holding company.
Aug.: Matsubara Works is merged into Ueno Works and shuts down.

1996
Mar.: Construction of Research and Development Building begins.
Dec.: Hirano Works is merged into Ueno Works and shuts down.

1999
Jun.: Hirano Works is merged into Ueno Works and shuts down.

Financial Review

Net Sales
Total net sales increased ¥16,551 million (39.7%) from last term’s ¥41,650 million to ¥58,201 million, mainly due to increased sales in the Home Video Game Division following the launch of Resident Evil 2 and other software.

Net Income (Loss)
We recorded a net loss of ¥4,760 million, a decrease of ¥5,262 million over last term, as a result of special losses totaling ¥13 billion which were essential this term in order to carry out measures to improve our financial balance including appraisal of the assets of our subsidiaries.

Total Assets
Although we increased our cash enormously this term, current assets were down 29.0% from last term’s ¥54,305 million to ¥38,559 million, resulting from consolidation to scale down our inventory and sales of securities. As a result, total assets decreased 14.8% to ¥100,833 million.

Total Shareholders’ Equity
Total Shareholders’ Equity decreased 18.4% from last term’s ¥36,267 million to ¥29,612 million. As a result, deficit at the end of the term amounted to ¥10,345 million due to the net loss of ¥4,760 million as well as an increase in dividends payable.
### CONSOLIDATED BALANCE SHEETS

CAPCOM CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES

MARCH 31, 1998 AND 1997

<table>
<thead>
<tr>
<th>Assets</th>
<th>Millions of yen</th>
<th>Thousands of U.S. dollars (Note 1)</th>
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<tbody>
<tr>
<td><strong>Current assets:</strong></td>
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</tr>
<tr>
<td>Cash and time deposits</td>
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<td>$4,574</td>
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<tr>
<td>Marketable securities</td>
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<tr>
<td>Notes and accounts receivable —</td>
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<td>Trade</td>
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<tr>
<td>Allowance for doubtful accounts</td>
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<tr>
<td>Short-term loans receivable</td>
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<td>Inventories (Note 4)</td>
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<td>Prepaid expenses</td>
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<td>Deferred income taxes</td>
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<td>Other</td>
<td>2,290</td>
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</tr>
<tr>
<td><strong>Total current assets</strong></td>
<td>38,559</td>
<td>54,305</td>
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<tr>
<td><strong>Investments and other assets:</strong></td>
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<td></td>
</tr>
<tr>
<td>Investments in securities (Note 5)</td>
<td>2,375</td>
<td>2,465</td>
</tr>
<tr>
<td>Long-term loans receivable (Note 6)</td>
<td>20,696</td>
<td>8,978</td>
</tr>
<tr>
<td>Long-term prepaid expenses</td>
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<td>Deferred income taxes</td>
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<td>586</td>
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<tr>
<td>Other</td>
<td>5,524</td>
<td>5,676</td>
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<tr>
<td>Allowance for doubtful accounts (Note 6)</td>
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<td><strong>Total investments and other assets</strong></td>
<td>21,883</td>
<td>19,433</td>
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<td><strong>Property, plant and equipment (Notes 7 and 8):</strong></td>
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<td></td>
</tr>
<tr>
<td>Land</td>
<td>26,298</td>
<td>26,375</td>
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<tr>
<td>Buildings and structures</td>
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<tr>
<td>Machinery and equipment</td>
<td>14,991</td>
<td>17,610</td>
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<tr>
<td>Construction in progress</td>
<td>13</td>
<td>2</td>
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<tr>
<td>Accumulated depreciation</td>
<td>(15,511)</td>
<td>(16,647)</td>
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<tr>
<td><strong>Total property, plant and equipment</strong></td>
<td>39,497</td>
<td>41,848</td>
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<tr>
<td>Excess cost over net assets of acquired subsidiaries</td>
<td>114</td>
<td>170</td>
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<tr>
<td>Translation adjustments</td>
<td>780</td>
<td>2,774</td>
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<tr>
<td><strong>Total assets</strong></td>
<td>¥100,833</td>
<td>¥118,330</td>
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</tbody>
</table>

The accompanying notes are an integral part of these statements.

<table>
<thead>
<tr>
<th>Liabilities and Shareholders' Equity</th>
<th>Millions of yen</th>
<th>Thousands of U.S. dollars (Note 1)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current liabilities:</strong></td>
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<tr>
<td>Short-term borrowings (Note 8)</td>
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<td>¥386</td>
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<td>Current portion of long-term debt (Note 8)</td>
<td>—</td>
<td>4,229</td>
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<tr>
<td>Notes and accounts payable</td>
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<tr>
<td>Accrued expenses</td>
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<td>1,714</td>
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<td>Accrued income taxes (Note 9)</td>
<td>130</td>
<td>1,999</td>
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<td>Other</td>
<td>2,866</td>
<td>1,806</td>
</tr>
<tr>
<td><strong>Total current liabilities</strong></td>
<td>23,655</td>
<td>34,367</td>
</tr>
<tr>
<td><strong>Long-term liabilities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long-term debt (Note 8)</td>
<td>45,786</td>
<td>46,242</td>
</tr>
<tr>
<td>Accrued retirement allowances (Note 10)</td>
<td>130</td>
<td>94</td>
</tr>
<tr>
<td>Other</td>
<td>1,628</td>
<td>1,360</td>
</tr>
<tr>
<td><strong>Total long-term liabilities</strong></td>
<td>47,544</td>
<td>47,696</td>
</tr>
<tr>
<td>Minority interest in a consolidated subsidiary</td>
<td>22</td>
<td>—</td>
</tr>
</tbody>
</table>

Shareholders' equity (Notes 11 and 12):

- **Common stock, ¥50 par value**
  - Authorized — 69,000,000 shares
  - Issued — 35,196,011 shares
- **Capital surplus**
- **Legal reserve**
- **Accumulated deficit**
- **Treasury stock**
- **Total shareholders' equity**
- **Total liabilities and shareholders' equity**

The accompanying notes are an integral part of these statements.
CONSOLIDATED STATEMENTS OF OPERATIONS  
CAPCOM CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES  
MARCH 31, 1998 AND 1997

<table>
<thead>
<tr>
<th></th>
<th>Millions of yen</th>
<th>Thousands of U.S. dollars (Note 1)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1998</td>
<td>1997</td>
</tr>
<tr>
<td>Net sales</td>
<td>¥ 58,201</td>
<td>¥ 41,650</td>
</tr>
<tr>
<td>Cost of sales</td>
<td>33,300</td>
<td>23,069</td>
</tr>
<tr>
<td>Gross profit</td>
<td>24,901</td>
<td>18,581</td>
</tr>
<tr>
<td>Selling, general and administrative expenses</td>
<td>11,542</td>
<td>10,631</td>
</tr>
<tr>
<td>Research and development expenses</td>
<td>2,936</td>
<td>2,597</td>
</tr>
<tr>
<td>Operating income</td>
<td>10,423</td>
<td>5,353</td>
</tr>
<tr>
<td>Other income (expense):</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest and dividend income</td>
<td>743</td>
<td>1,021</td>
</tr>
<tr>
<td>Exchange gain, net</td>
<td>623</td>
<td>1,877</td>
</tr>
<tr>
<td>Loss on sales or disposition of property, plant and equipment</td>
<td>(311)</td>
<td>(278)</td>
</tr>
<tr>
<td>Write off of investments in securities</td>
<td>(670)</td>
<td>—</td>
</tr>
<tr>
<td>Special losses, mainly for liquidation of an unconsolidated subsidiary (Note 13)</td>
<td>(12,867)</td>
<td>(1,641)</td>
</tr>
<tr>
<td>Loss from discontinued operations</td>
<td>(579)</td>
<td>(901)</td>
</tr>
<tr>
<td>Income (loss) before income taxes</td>
<td>(3,639)</td>
<td>4,052</td>
</tr>
<tr>
<td>Income taxes (Note 9):</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current</td>
<td>160</td>
<td>2,766</td>
</tr>
<tr>
<td>Deferred</td>
<td>912</td>
<td>727</td>
</tr>
<tr>
<td></td>
<td>1,072</td>
<td>3,493</td>
</tr>
<tr>
<td>Amortization of excess cost over net assets of acquired subsidiaries</td>
<td>(57)</td>
<td>(57)</td>
</tr>
<tr>
<td>Minority interest in a consolidated subsidiary, credit</td>
<td>8</td>
<td>—</td>
</tr>
<tr>
<td>Net income (loss)</td>
<td>(¥ 4,760)</td>
<td>¥ 502</td>
</tr>
</tbody>
</table>

Per share amounts:

<table>
<thead>
<tr>
<th></th>
<th>Millions of yen</th>
<th>U.S. dollars</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net income (loss)</td>
<td>¥ 135,24</td>
<td>¥ 14.29</td>
</tr>
<tr>
<td>Cash dividends paid</td>
<td>20.00</td>
<td>0.00</td>
</tr>
</tbody>
</table>

CONSOLIDATED STATEMENT OF SHAREHOLDERS’ EQUITY  
CAPCOM CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES  
MARCH 31, 1998 AND 1997

<table>
<thead>
<tr>
<th></th>
<th>Millions of yen</th>
<th>Thousands of U.S. dollars (Note 1)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1998</td>
<td>1997</td>
</tr>
<tr>
<td>Common stock:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance at beginning of year</td>
<td>¥ 18,211</td>
<td>¥ 18,210</td>
</tr>
<tr>
<td>Shares issued upon conversion of bonds</td>
<td>—</td>
<td>1</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td>18,211</td>
<td>18,211</td>
</tr>
<tr>
<td>Capital surplus:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance at beginning of year</td>
<td>21,098</td>
<td>21,097</td>
</tr>
<tr>
<td>Excess of principal amount of bonds converted over the amount credited to common stock issued</td>
<td>—</td>
<td>1</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td>21,098</td>
<td>21,098</td>
</tr>
<tr>
<td>Legal reserve:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance at beginning of year</td>
<td>458</td>
<td>388</td>
</tr>
<tr>
<td>Transfer from retained earnings</td>
<td>190</td>
<td>70</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td>648</td>
<td>458</td>
</tr>
<tr>
<td>Accumulated deficit:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance at beginning of year</td>
<td>(3,500)</td>
<td>(3,228)</td>
</tr>
<tr>
<td>Net income (loss) for the year</td>
<td>(4,760)</td>
<td>502</td>
</tr>
<tr>
<td>Cash dividends</td>
<td>(1,865)</td>
<td>(704)</td>
</tr>
<tr>
<td>Bonuses to directors and statutory auditors</td>
<td>(30)</td>
<td>—</td>
</tr>
<tr>
<td>Transfer to legal reserve</td>
<td>(190)</td>
<td>(70)</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td>(¥ 10,345)</td>
<td>(¥ 3,500)</td>
</tr>
</tbody>
</table>

The accompanying notes are an integral part of these statements.
CONSOLIDATED STATEMENTS OF CASH FLOWS

Millsions of yen Thousands of U.S. dollars (Note 1)


Cash flows from operating activities:

Net income (loss) (¥ 4,760) ¥ 502 (¥ 36,060)
Adjustments to reconcile net income (loss) to net cash provided by operating activities — — —
Depreciation and amortization 3,157 3,884 23,916
Provision for doubtful accounts 4,007 — 30,356
Liquidation losses of an unconsolidated subsidiary 7,558 — 57,256
Decrease (increase) in notes and accounts receivable (447) 5,304 (3,386)
Decrease in inventories 4,919 385 37,265
Increase (decrease) in notes and accounts payable 1,115 (98) 8,447
Other (506) (271) (3,833)
Total adjustments 19,803 9,204 150,021
Net cash provided by operating activities 15,043 9,706 113,961

Cash flows from investing activities:

Proceeds from sales of facilities 1,454 6,793 11,015
Capital expenditures — — (18,863)
Decrease (increase) in short-term loans receivable 1,123 (674) 8,508
Decrease (increase) in marketable securities 6,351 (4,983) 48,114
Increase in long-term loans receivable 1,067 (7,142) (8,084)
Other 311 769 2,356
Net cash provided by (used in) investing activities 5,682 (7,757) 43,046

Cash flows from financing activities:

Net borrowings (repayments) of short-term borrowings and current portion of long-term debt (11,068) 6,543 (83,848)
Proceeds from long-term debt 154 67 1,167
Repayments of long-term debt (610) (11,123) (4,621)
Cash dividends paid (1,895) (704) (14,356)
Other 1,361 945 10,310
Net cash used in financing activities (12,056) (4,272) (91,348)

Translation adjustment (267) (1,664) (2,023)

Net increase (decrease) in cash 8,400 (3,805) 63,636

Cash and time deposits at beginning of year ¥ 12,974 ¥ 4,574 ¥ 98,288
Cash and time deposits at end of year ¥ 4,574 ¥ 8,379 ¥ 34,652

The accompanying notes are an integral part of these statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. MAJOR POLICIES IN PREPARING CONSOLIDATED FINANCIAL STATEMENTS:

The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in Japan and are a translation of those publicly issued in Japan after modification to enhance foreign readers’ understanding.

The U.S. dollar amounts are included solely for convenience. These translations should not be construed as representations that the Japanese yen amounts actually represent, or have been or could be converted into, U.S. dollars. As the amounts shown in U.S. dollars are for convenience only, and are not intended to be computed in accordance with generally accepted translation procedures, the rate of ¥132=US$1, the approximate current rate prevailing on March 31, 1998, has been used for the purpose of presentation of the U.S. dollar amounts in the accompanying consolidated financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES:

(1) Consolidation and accounting for investments in affiliates:

The consolidated financial statements consist of the accounts of Capcom Co., Ltd. (the "Company") and, with minor exceptions, those of its majority-owned subsidiaries at the relevant balance sheet date. All significant intercompany transactions and accounts are eliminated.

During the year ended March 31, 1998 the financial statements of CAPCOM MEXICO S.A. DE C.V. were excluded from the consolidation because the Company commenced liquidation procedure of that company.

Capitalized development costs of game software for 32-bit and 64-bit game machines are stated at cost on a specific project basis.

Production, print and certain advertising costs relating to specific motion picture titles comprise motion picture film costs and are presented as investments.

The film costs are amortized in proportion to the revenue earned to total estimated revenue. Un amortized film costs are evaluated in relation to the estimated future revenue.

(2) Revenue recognition:

Revenues from sales of products are recognized when products are shipped to customers.

Motion picture revenue is recognized on the dates of theatrical exhibition.

(3) Statement of cash flows:

A portion of cash exceeds daily requirements is invested in temporary cash investments, mainly consisting of time deposits, which are low risk short-term financial instruments readily convertible to known amounts of cash. The company deems the time deposits as cash equivalents for the purposes of the statement of cash flows.

(4) Translation of foreign currencies:

Foreign currency amounts are translated into Japanese yen at the rates prevailing at the relevant balance sheet date for short-term assets and liabilities and at historical rates for long-term assets and liabilities. When the historical exchange rates differ significantly from the year-end rates, the year-end rates are used to translate the long-term assets or liabilities. Receivable and payable in foreign currency hedged by forward exchange contracts are translated into Japanese yen at the contracted rates of exchange. Income and expenses in foreign currencies are translated at the rates prevailing at the time of the transactions. Resulting exchange gains or losses are credited or charged to income as incurred.

All of assets, liabilities, income and expenses of foreign subsidiaries in the financial statements of foreign subsidiaries are translated into Japanese yen at the rates in effect at the balance sheet date, except for shareholders’ equity which are translated at the rates prevailing at the time when transaction occurred and the resulting translation differences are debited or credited to the translation adjustments accounts of the consolidated financial statements.

(5) Marketable securities and investments in securities:

Marketable securities and other marketable securities both of current and non-current nature are stated at the lower of cost or market. Other security investments are stated at cost.

The cost of securities sold is determined based on the average cost of all such securities held at the time of sale.

(6) Inventories:

Inventories are stated at the lower of cost or market, cost being principally determined by the average cost method.

Capitalized development costs of software for 32-bit and 64-bit game machines are stated at cost on a specific project basis.

Production, print and certain advertising costs relating to specific motion picture titles comprise motion picture film costs and are presented as investments.

The film costs are amortized in proportion to the revenue earned to total estimated revenue. Un amortized film costs are evaluated in relation to the estimated future revenue.

(7) Property, plant and equipment and depreciation:

Property, plant and equipment are stated at cost.

Depreciation of property, plant and equipment is principally computed by the declining balance method at rates based on estimated useful lives of the assets.

Significant renewals and additions are capitalized at cost.

Maintenance and repairs, including minor renewals and betterments, are charged to income as incurred.

(8) Research and development expenses:

Research and development expenses for development of existing products or development of products other than capitalized costs of game software for 32-bit and 64-bit game machines, including basic research and development costs, are charged to income when incurred.
4. INVENTORIES:

<table>
<thead>
<tr>
<th></th>
<th>1998</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finished goods</td>
<td>1,685</td>
<td>988</td>
</tr>
<tr>
<td>and merchandise</td>
<td>$ 12,765</td>
<td>$ 7,728</td>
</tr>
<tr>
<td>Work in process</td>
<td>380</td>
<td>647</td>
</tr>
<tr>
<td>Capitalized development costs</td>
<td>2,949</td>
<td>18,932</td>
</tr>
<tr>
<td>Raw materials</td>
<td>521</td>
<td>3,947</td>
</tr>
<tr>
<td>Supplies</td>
<td>2,186</td>
<td>6,032</td>
</tr>
<tr>
<td>Films</td>
<td>27,280</td>
<td>22,436</td>
</tr>
</tbody>
</table>

Total inventories: $107,764 million ($82,988 million)

5. MARKETABLE EQUITY SECURITIES:

<table>
<thead>
<tr>
<th></th>
<th>1998</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>1,454</td>
<td>1,924</td>
</tr>
<tr>
<td>Market</td>
<td>1,453</td>
<td>1,926</td>
</tr>
<tr>
<td>Unrealized gain (loss)</td>
<td>12</td>
<td>232</td>
</tr>
</tbody>
</table>

6. LONG-TERM LOANS RECEIVABLE:

At March 31, 1998, long-term loans receivable contain loans receivable from an unconsolidated subsidiary, CAPCOM MEXICO S.A. DE C.V., amounted to ¥5,551 million ($42,816 thousand) in addition to write off of some such loans that were reclassified to long-term loans receivable from an unconsolidated subsidiary, CAPCOM MEXICO S.A. DE C.V., at the time of the acquisition.

7. PROPERTY, PLANT AND EQUIPMENT:

Depreciation charges for the years ended March 31, 1998 and 1997 amounted to ¥2,031 million ($15,387 thousand).

8. SHORT-TERM BORROWINGS AND LONG-TERM DEBT:

8.1. SHORT-TERM BORROWINGS:

<table>
<thead>
<tr>
<th></th>
<th>1998</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank overdrafts</td>
<td>3,760</td>
<td>5,575</td>
</tr>
<tr>
<td>with interest</td>
<td>$ 55,757</td>
<td>$ 7,721</td>
</tr>
<tr>
<td>Unsecured loan payable to banks with interest 1.625% per annum</td>
<td>6,069</td>
<td>45,977</td>
</tr>
<tr>
<td>Notes payable with interest 3.5% per annum</td>
<td>950</td>
<td>6,440</td>
</tr>
</tbody>
</table>

Total short-term borrowings: $76,274 million

8.2. LONG-TERM DEBT:

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

<table>
<thead>
<tr>
<th></th>
<th>1998</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.8% convertible bonds due 2001</td>
<td>$ 25,000</td>
<td>$ 31,097</td>
</tr>
<tr>
<td>1.0% convertible bonds due 2005</td>
<td>19,866</td>
<td>150,500</td>
</tr>
<tr>
<td>Loans payable to banks and other financial institutions due 1998 - 2005, with interest at 15.625% - 17.25%</td>
<td>14,279</td>
<td>22,761</td>
</tr>
<tr>
<td>Secured</td>
<td>1,936</td>
<td>2,072</td>
</tr>
<tr>
<td>Unsecured</td>
<td>16,243</td>
<td>19,689</td>
</tr>
</tbody>
</table>

Total long-term debt: $79,587 million

The aggregate annual maturities of long-term debt at March 31, 1998 were as follows:

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>Thereafter</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Millions of yen)</td>
<td>388</td>
<td>349</td>
<td>720</td>
<td>1,936</td>
<td>190,121</td>
<td>150,758</td>
<td>150,500</td>
<td>190,121</td>
</tr>
</tbody>
</table>

The 1.0% convertible bonds due 2005 were issued on June 17, 1994 and are convertible into common stock at conversion price of ¥4,982 per share. These convertible bonds are redeemable at Company's option in the period from October 1, 1998 to September 29, 2005 as provided in the indentures.

The substantial difference between the tax rate in the income statements and the effective statutory tax rates for the years ended March 31, 1998 and 1997 was caused by the operating losses of consolidated subsidiaries.

Filing of a consolidated tax return by a group of corporations is not permitted in Japan, irrespective of the percentage of ownership.

9. INCOME TAXES:

The Company and its Japanese consolidated subsidiaries are subject to a number of different income taxes which, in the aggregate, indicate effective statutory tax rates of approximately 52%. The ordinary relationship between income tax expenses and pretax accounting income is distorted by a number of items including various tax credits, tax effect to timing differences, permanent non-deductibility of certain expenses and operating losses incurred by the consolidated subsidiaries.

10. PENSION PLAN AND ACCRUED RETIREMENT ALLOWANCES:

The amounts charged to income for the years ended March 31, 1998 and 1997 with respect to the pension plan and retirement allowances were ¥3,924 million ($304 thousand) and ¥103 million, respectively.

Pension assets (based on the latest available information) of the pension plan at March 31, 1998 and 1997 amounted to ¥255 million ($19,777 thousand) and ¥290 million ($2,197 thousand), respectively.

Unamortized past service costs of pension plan have been substantially amortized.

11. COMMON STOCK:

The changes in the number of issued shares of common stock of the Company during the years ended March 31, 1998 and 1997 are summarized below:

<table>
<thead>
<tr>
<th></th>
<th>1998</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Thousands of shares)</td>
<td>35,196</td>
<td>35,195</td>
</tr>
<tr>
<td>Balance at beginning of year</td>
<td>35,196</td>
<td>35,195</td>
</tr>
<tr>
<td>Issued upon conversion</td>
<td>35,196</td>
<td>35,195</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td>35,196</td>
<td>35,195</td>
</tr>
</tbody>
</table>
The Japanese Commercial Code provides that an amount determined by appropriate legal procedures, but is recorded in the subsequent accounting year after shareholder approval has been obtained.

that it relates, but is recorded in the subsequent accounting year after shareholder approval has been obtained.

sub-total

The other segment mainly comprises the game software and hardware to amusement facility developments, manufactures, distributes and/or rents arcade game software and hardware to amusement facility operators. The other segment mainly comprises the operation of amusement facilities. The following tables present certain information regarding the business segments for the years ended March 31, 1998 and 1997.


corporate expenses and eliminations

Cost of sales and direct expenses:

Cost of sales and direct expenses:

Operating income (loss):

Operating income (loss):

Cost of sales and direct expenses:

Cost of sales and direct expenses:

Operating income (loss):

Operating income (loss):

Total assets:

Total assets:

Corporate assets and eliminations

Corporate assets and eliminations

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REPORT OF INDEPENDENT ACCOUNTANTS

June 26, 1998

To the Board of Directors and Shareholders of Capcom Co., Ltd.

In our opinion, based upon our audits and the report of other auditors, the accompanying consolidated balance sheets and the related consolidated statements of operations, of shareholders' equity and of cash flows present fairly, in all material respects, the financial position of Capcom Co., Ltd. and its consolidated subsidiaries at March 31, 1998 and 1997, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries, which statements reflect total assets of ¥15,592 million and ¥21,909 million at March 31, 1998 and 1997, respectively, and total revenues of ¥12,369 million and ¥7,758 million for the years ended March 31, 1998 and 1997, respectively. Those statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for those companies, is based solely on the reports of the other auditors.

We conducted our audits of these statements in accordance with generally accepted auditing standards which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for the opinion expressed above.

Presidential Office: Osaka Center Building
1-3, Kyutarou-machi 4-chome
Chuo-ku, Osaka 541-0056

Price Waterhouse

(Corporate Information)

(Directors and Statutory Auditors)

President: Kenzo Tsujimoto
Executive Vice President: Tadashi Aikawa
Senior Managing Director: Heiji Oshima
Managing Directors: Takashi Aoki
Masatoishi Yoshida
Haruhiko Tsujimoto
Noritaka Funamizu
Directors: Morio Kuroda
Fumitaki Kawamoto
Shizuhiko Yamamoto
Tadashi Kadowaki

CORPORATE DATA

Date of Establishment: May 30, 1979
Paid-in Capital: ¥18,211 million
(US $137,962 thousand)
End of Term: March 31
Number of Employees: 946

Head Office:
3-3-3 Uchihiranomachi,
Chuo-ku, Osaka 540-0037, Japan
Phone: 06-6920-3600
Fax: 06-6920-5100
http://www.capcom.co.jp/

Tokyo Branch:
Shinjuku Sumitomo Building
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Tokyo 163-0266, Japan
Phone: 03-3340-0710
Fax: 03-3340-0711

CONSOLIDATED SUBSIDIARIES

CAPCOM USA, Inc.
475 Oakmead Parkway
Sunnyvale, California 94086, USA
Phone: 1-408-774-0500
Fax: 1-408-774-3994

CAPTRON Co., Ltd.
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STATUS Co., Ltd.
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