Keynotes by Kazuhiko Abe, Director and Managing Corporate Officer at November 2006 Mid-term Results Meeting

My name is Kazuhiko Abe and I would like to present the details regarding our mid-term financial results.

P1-5 :

Mid-Term Consolidated Statements of Income From April 1, 2006 to September 30, 2006

[Overview of Mid-Term Financial Results ended September 30, 2006]

Let me begin by presenting a summary of our mid-term results for the term ended September 30th, 2006. Before going into the numbers, I would like to first give an overview of the results. We have made great progress with our structural reforms in the consumer video game business, as evidenced by healthier profits. In particular, reforms in the North American subsidiary have demonstrated their effectiveness. Behind these reforms is years of reexamining our R&D and administrative processes. These reforms are currently on track and have led to a significant reduction in the number of titles that are not profitable as well as paved a solid foundation for R&D and administrative divisions for the future. As announced at the recent CEDEC, we have worked out a unique PC development environment for creating next-generation titles.

I feel that our successful implementation of this unique development environment has given Capcom a development edge over the competition. A few of our business divisions may require further reforms, but in most instances our business divisions have lived up to our expectations. As President Tsujimoto mentioned in his talk earlier, from a financial perspective our operating cash flow has become substantially more stable and we will therefore be able to cover the upcoming redemption of convertible bonds with cash in hand or by using a commitment line. That is the general overview of our mid-term results, so now I would like to go through the numbers point-by-point.

This first chart compares last fiscal year’s mid-term figures with the current mid-term ones. This mid-term’s net sales, operating income and ordinary income figures have all demonstrated improvement over last year’s numbers. Net income is the only figure number to have dropped off slightly from the same period last year. Review on deferred tax assets, etc. in the previous fiscal mid-term is the primary reason for this difference.

Next is the chart indicating our mid-term results compared with the estimates made at the beginning of the period. Net sales, operating income, ordinary income and net income have all exceeded forecasted expectations.

P6-11 : Summary of Mid-Term Financial Results ended September 30, 2006

I will go into further detail now regarding our net sales, which totaled 29.1 billion yen as of September 2006. This is 1.4 billion yen higher than the same period last fiscal year. Several factors contributed to this increase, most notably the success of consumer game titles such as the overseas-targeted Dead Rising and the domestic successes of Devil Kings 2 and Monster Hunter Freedom, etc. The arcade operations business has also contributed to the overall increase with the opening of three new large arcade facilities in the first quarter.

I will explain the details by business segments later in the presentation; however, I will give a brief overview of the different market segments at this point. Both consumer games and arcade operations have seen an increase in profits, while arcade games have stayed relatively even, and contents expansion has experienced a drop. I will of course provide further details regarding these factors later.

This mid-term's operating income has totaled 3 billion yen as of September 2006. This is a 2.4 billion yen increase over the same period last fiscal year. In the charts, the results are listed by segment, starting with Japan. The net sales experienced a slight dip compared to the same period last fiscal year, while operating income has increased by 500 million yen. One important factor to note is that the operating margin has increased by 3.1% from 12.4% last year to 15.5% this year. This is largely due to a reduction in unprofitable game titles and is a key reason why we have increased our income despite a drop in net sales.

The North American segment has experienced significant improvement in net sales, operating income and operating margin. With Dead Rising in particular, titles released in North America been quite successful, leading to increased sales and income. This marked improvement has brought our North American operating margin to 14.5%, which is more in line with our Japanese domestic margin.

The final regional segment is Europe. While there was a slight dip in net sales, the income has shifted into the black to a total of 455 million yen. There may not have been a strong lineup of titles this year in Europe, but favorable sales of Dead Rising and reduced management costs have helped create this change in income. In addition, the development of a title in the previous fiscal year hurt profits during that period.

Net income has experienced a drop of 1.2 billion yen from the same period last fiscal year to a total of 1.9 billion yen this mid-term mostly due to the previously mentioned review on the deferred tax assets. The resolution of a legal settlement of 103 million yen has been recognized under extraordinary income. As for extraordinary losses, the cancellation of projects, including the projects cancelled as a result of Clover Studio's dissolution, is the main source of the 365 million yen in losses.

P12-13 : Mid-Term Balance Sheets as of September 30, 2006

The next area in my presentation is the mid-term consolidated balance sheet.

The first chart is a comparison of the figures at the end of last fiscal year with the current mid-term ones. Some large changes are a 4 billion yen drop in current assets and a 2 billion yen increase in fixed assets. In addition, total net assets have dropped by 2.3 billion yen. The change in capital is a result of Capcom buying back 3.2 billion yen worth of its own shares.

P14-15 : Summary of Mid-Term Balance Sheets as of September 30, 2006

I will now go further into some of the details behind the numbers starting with assets. Cash and cash equivalents totaled 35.9 billion yen as of September 2006, a 4.6 million yen drop from the end of the last fiscal year. Payment of 2 billion yen in corporate taxes correction coming from past years, the 1.6 billion yen acquisition of Cosmic Infinity, the acquisition of 3.2 billion yen in treasury shares, and the 1.8 billion yen used for investing in arcade operations totaled up to more than 8 billion yen and are the primary reasons for the change. The change in current assets is a result of an increase in cash advances to other parties as a business transaction. The goodwill payment of 1 billion yen listed at the bottom was the payment used during the acquisition of the Canadian company, Cosmic Infinity.

With liabilities, compared to the end of last fiscal year, our accrued income tax amount has gone down by 1.7 billion yen from the payment of the tax correction based on transfer price taxation assessed at the end of the last fiscal year. The increase in current liabilities is from an increase in cash advances from other parties as a provision for business operations.

P16-17 : Summary of Mid-Term Statements of Cash Flow From April 1, 2006 to September 30, 2006

The next part of my presentation is about Capcom’s mid-term cash flow.

The cash flow from operating activities totaled 3.3 billion yen this mid-term. If the 1.7 billion yen tax correction for last year’s taxes is removed from the figure, the actual mid-term cash flow from operating activities totals over 5 billion yen. Cash flow from investing activities totals -3.9 billion yen due to the aforementioned 1.6 billion acquisition of Cosmic Infinity and the investment of 1.8 billion yen in arcade facilities. Part of this mid-term’s negative cash flow from financing activities is due to a 3.2 billion yen acquisition of treasury shares. In the previous fiscal year, the redemption of 12.2 billion yen worth of convertible bonds is what contributed to the -13.9 billion yen figure.

P18-21 : Overview and Future Strategy by Business Segment

[Overview of Home Video Games Business for 1st Half ended September 30, 2006]

I will now move on to the different business segments and the future strategies for each of them.

There are six points I would like to discuss regarding the consumer game business. The first is that titles such as Dead Rising, Monster Hunter Freedom and Devil Kings 2 have been great hits. Dead Rising was designed primarily for the North American and European markets, while Monster Hunter and Devil Kings were primarily for the Japanese market. Although most of the focus on reforms has involved our North American subsidiary, I would like to note that we have also made many important operating reforms within the Japan offices as well. One example is the introduction of staff that travel around to various retail stores throughout Japan to try and judge areas in need of improvement. Their efforts have led to the procurement of useful information along with the improvement of the displays of our products. A new, more detailed approach to sales has thus been made possible, leading to increased retail sales, especially within Japan.

The second major point that I want to mention is the positive reception of Lost Planet for Microsoft's Xbox 360 console. Anticipation over the title has grown, and it has already been the recipient of several awards such as the Leipzig Game Show Best Xbox 360 Game Award among others.

The third major point involves the publicity we have garnered through awards by the Japanese press for three of our gaming titles in Monster Hunter , Phoenix Wright 4 and Lost Planet.

The fourth point involves our reforms in the North American subsidiary, most notably in consumer home video games which are at the core of Capcom's business strategy. I briefed about the reforms at my last presentation earlier in May, and I am happy to say they are still proceeding along smoothly and effectively.

In particular, personnel changes have been accompanied by organizational changes. One major area of improvement is the transition to direct sales to large retail chains.

We have already implemented direct sales starting with Game Stop and Electronics Boutique. Direct sales to Wal-Mart will have commenced in October to be followed later by direct sales to Best Buy and Target. Once completed, Capcom will be selling directly to the top five retail chains in terms of the sale of Capcom products. These top five retail chains account for 60-70% of Capcom's total sales in the North American market and the transition to direct selling will increase overall profitability. In addition, we had been placing orders with 30 different resellers, but have now lowered that count to around 5 or 6, helping to reduce the cost of commissions.

Another major change is the marketing process. Efforts are being made to provide news and assets about our games on a regular basis in order to help facilitate awareness about the Capcom brand. Thanks to these marketing efforts, awareness of the different title brands has increased. Marketing is also taking steps to analyze traffic to Capcom's official web site in order to better gauge user trends to improve game sales. These reforms help to make sure that Capcom is doing everything it can to best position its products.

The third reform, which is still in progress, is the strengthening of the R&D process. We are in the process of selecting promising overseas development partners with an intimate knowledge of their market to work with on new game titles. We are currently working on one title, and are reviewing design documents with our future plan being to develop 1-2 titles a year with development taking place in America by our development partners.

The fifth point is that R&D reforms have been proceeding steadily. Our internal R&D divisions have been reorganized from what they were a few years ago, leading to many business activities being done in a more controlled manner. In particular, Capcom is known for actively producing new titles; however, in the past, the development of new titles coincided with an increase in the number of titles that went into the red. Both management and R&D understand the need to change this trend, which has led to several reforms that have dramatically improved the management of titles and reduced the number of titles in the red. Such changes have included reforms to the title approval process, improved cost management, and improved schedule management.

Another major change that has occurred has been a change in the way R&D addresses next-generation development. Capcom has traditionally chosen the introduction of new hardware platforms as the time to release new titles. This generation is no exception with Dead Rising and Lost Planet being two entirely new games developed for the Xbox 360. Dead Rising has experienced extremely favorable sales and Lost Planet has received a lot of positive praise. It is our belief that Capcom has successfully made the transition into development for the next-generation hardware. Capcom's unique PC-based next-generation development environment has also helped make it easy to port between the Xbox 360, PS3 and PC platforms. The length of time to port a game has been dramatically reduced along with a reduction in porting cost. This development environment has helped to keep Capcom a step ahead of the competition.

The sixth and final point regarding the consumer games business is regarding our online business. At this point in time we are actively preparing to launch our online business. As mentioned in a press release earlier this year, together with the Dwango Group, we have co-founded the new company, Daletto, in October. Daletto's primary focus will be on operating a portal site along with related online games, avatar services, e-commerce and advertising businesses. We believe that this online business venture will be an integral part of Capcom's future success and we are putting our full support behind it accordingly.

P22-23 : Overview of Home Video Games Business for 1st Half ended September 30, 2006

I will provide a brief overview of the consumer games business which was the subject of the aforementioned reforms. As a result, we have produced four fewer titles than the same period the previous year. As shown on the chart, net sales have increased by 1.4 billion yen compared with the same term last year. Our operating margin has been greatly improved by 6.6% to a total of 14.4%. The number of games sold is similar to the same period last year with 4.7 million sold. One thing to note is that 1.7 million of those games were sold in Japan, compared with 3 million sold in North America and Europe. These numbers help to demonstrate the significant number of our titles sold overseas.

The next chart shows the sales figures for the major titles in the first half of the fiscal year. The first listed is Dead Rising for the Xbox 360 with a total of 930,000 units sold as of the end of September across all territories. Next are Devil Kings 2 with 300,000 units and Okami with 290,000 units sold in just Japan and North America as Okami had not yet been released in the European territories at the time of these numbers. Monster Hunter Freedom has sold 410,000 units in Japan, North America and Europe. When combined, titles in the Mega Man series this period have sold almost 600,000 units.

P24-26 : Home Video Games Business Strategy for 2nd half of Fiscal Year 2006

The following titles are scheduled for release in the next mid-term period. Lost Planet is forecasted to sell 740,000 units. Mega Man Star Force is forecasted to sell 600,000 units. Monster Hunter Freedom 2^{nd} is forecasted to sell 500,000 units. Phoenix Wright 4 is forecasted to sell 200,000 units.

The projected figures for games to be released in the second half of this fiscal year are shown on this chart. The projected net sales are 34.4 billion yen, which is 8.3 billion lower than the same period last fiscal year. At the same time, the operating margin is projected to be 12.2% this time, a 5.4% increase over the 6.8% for the same period last year. The leading cause for the marked increase is the reform that has taken place at the North American and European offices. In addition, improvements in the R&D process leading to fewer titles falling into the red have made an impact, pushing the operating margin higher.

P27 : Overview of Arcade Operations Business for 1st Half ended September 30, 2006

The next set of figures is about the arcade business. The net sales for the arcade business in the mid-term ended September, 2006 are 6.5 billion yen, an 800 million yen increase over the same period the previous year. The operating margin has taken a slight dip of 3.2% down to 17.6%. The cost of opening up new arcades in the first quarter factors into the drop. Sales at existing arcades has maintained 99% of the profit compared with the same period last year, while 2 new shopping center arcades and 1 new roadside arcade have been opened to expand the business. A total of 6 new large arcades are planned for this fiscal year.

P28 : Arcade Operations Business Strategy for 2nd Half of Fiscal Year 2006

After factoring in a lagging market, existing arcade sales are projected to be 102% of sales for the same period in the previous year. 3 new arcades will be opened in the second half of the fiscal year, with one already opened in October. For this fiscal year, net sales are projected to be 13.7 billion yen, which is 2.1 billion yen higher than last year’s 11.6 billion yen. The operating margin will experience a slight drop from the previous fiscal year with a margin of 20.4% mostly due to the cost of opening up new arcades.

P29 : Overview of Arcade Games Sales Business for 1st Half ended September 30, 2006

Now I will move on to discussing the figures for the arcade game sales business. This mid-term’s net sales almost parallel those of last year’s at 4.4 billion yen. Operating margin has dipped 2.1% to 20.5% this mid-term. The favorable reception of Gundam in arcades has bolstered sales. Originally, the game was projected to move 3,000 units, but ended up moving 7,200 units. 1,600 Mega Man Battle Network arcade card game units geared for a young male audience have been rented. Although the number of these Mega Man Battle Network arcade units rented nearly matched projections, the number of chips sold through these units has not quite met with our original projections affecting the final net sales.

P30 : Arcade Games Sales Business Strategy for 2nd half of Fiscal Year 2006

Second-half strategy includes focusing on developing prize and medal games which are currently in high demand by the public. As for specific titles due to be released in the second half, the rental of the unit aimed at young girls, Wantame Music Channel, began at the end of September and has received a very positive reception. The next unit available for rental, starting in November, is the mid-sized medal unit, Donkey King Banana Kingdom. Current second half projections center around the sales of these two units. Initial projections have been revised to account for the mid-term card sales along with future competition and for the possibility of some medal machines being postponed until the next fiscal year. Although 8.7 billion yen for the fiscal year is still an increase over the previous fiscal year, it is still lower than the original projections for the period.

The costs for development have influenced the operating margin, causing the projection to drop to 6.9%.

P31 : Overview of Contents Expansion Business for 1st Half ended September 30, 2006

The final business figures I will discuss are those for the contents expansion business. Net sales for the mid-term have totaled 1.3 billion yen. This is 900 million yen lower than the same period the previous fiscal year. As originally planned, there were no pachinko or pachislo sales in the first half of the fiscal year. There is, however, activity in the mobile contents division. The most notable news is the acquisition of the Canadian company Cosmic Infinity. The purchase of Cosmic Infinity helped to fill a gap in Capcom's North American mobile content presence. Specific areas Cosmic Infinity supplements Capcom are: their business connections to carriers, their mobile content development staff, and their know-how with the casual games market. One other point to note with the mobile contents division is that sales of the mobile phone version of Phoenix Wright are going strong.

P32 : Contents Expansion Business Strategy for 2nd Half of Fiscal Year 2006

The pachinko & pachislo business division strategy for the second half focuses mostly on sales of pachinko and pachislo hardware units. For the mobile contents division, the two major releases are Monster Hunter, to come preinstalled on FOMA mobile units, and Lost Planet, which will be capable of multiplayer action across mobile units.

The projected net sales for the fiscal year are 7.5 billion yen, a nearly 1.8 billion increase over last fiscal year's net sales. The operating margin is 25.3%, 15.8% lower than last fiscal year, due primarily to the costs involved with setting up the North American mobile contents division. These forecasts are in line with our initial forecasts for the period.

P33 : Business Forecast of Fiscal Year 2006

Last in my presentation are the forecasted business results for the fiscal year. Net sales are projected to be 68.4 billion yen, while operating income and ordinary income are both projected to total 7 billion yen each. Net income is projected to be 3.9 billion yen and remain the same as our initial forecast. Reforms in the consumer game division have been proceeding excellently, but the results for the arcade games business division and the online business division as well as certain areas of strategic focus are still uncertain, so we are leaving our initial forecast unchanged. The expected net income per share is 70.95 yen. Dividends were originally planned to be 20 yen per share, but we have changed the payout to 15 yen for the mid-term and end-of-the-year periods for a total of 30 yen for the fiscal year.

This concludes my presentation on the mid-term financial results for the period ended September 30th, 2006.