

DAIWA SECURITIES GROUP INC.
CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2001

DAIWA SECURITIES GROUP INC.
CONSOLIDATED BALANCE SHEET
March 31, 2001

| ASSETS | <u>Millions of Yen</u> | <u>Millions of U. S. Dollars</u> |
|---|------------------------|--------------------------------------|
| | 2001 | 2001 |
| Cash and cash equivalents | ¥ 310,382 | \$ 2,505 |
| Time deposits | 10,674 | 86 |
| Cash and securities segregated for regulatory purposes and deposits with clearing organizations | 94,516 | 763 |
| Trading assets: | | |
| Equities and convertible bonds | 319,386 | 2,578 |
| Japanese government and agency bonds | 530,370 | 4,281 |
| Non-Japanese government and agency bonds | 82,470 | 666 |
| Corporate debt securities | 340,168 | 2,745 |
| Derivative contracts | 315,811 | 2,549 |
| Other | 31,403 | 253 |
| Total trading assets | 1,619,608 | 13,072 |
| Securities purchased under agreements to resell | 1,845,731 | 14,897 |
| Securities borrowed | 1,023,054 | 8,257 |
| Securities pledged as collateral | 1,272,649 | 10,272 |
| Receivables from: | | |
| Broker-dealers and clearing organizations | 364,755 | 2,944 |
| Customers | 158,600 | 1,280 |
| Other, net of allowance for doubtful accounts of ¥8,070 million (\$65 million) | 80,456 | 649 |
| Investments in and advances to affiliated companies | 23,053 | 186 |
| Investments | 299,710 | 2,419 |
| Property, equipment and leasehold improvements, net of accumulated depreciation and amortization of ¥107,546 million (\$868 million) | 253,552 | 2,046 |
| Deferred income taxes | 91,414 | 738 |
| Other assets | 106,813 | 862 |
| Total Assets | ¥ 7,554,967 | \$ 60,976 |

| LIABILITIES AND SHAREHOLDERS' EQUITY | <u>Millions of Yen</u> | <u>Millions of U. S. Dollars</u> |
|--|------------------------|--------------------------------------|
| | 2001 | 2001 |
| Liabilities | | |
| Short-term borrowings | ¥ 999,954 | \$ 8,071 |
| Trading liabilities: | | |
| Equities and convertible bonds | 93,375 | 754 |
| Japanese government and agency bonds | 667,766 | 5,389 |
| Non-Japanese government and agency bonds | 333,553 | 2,692 |
| Corporate debt securities | 14,834 | 120 |
| Derivative contracts | 300,875 | 2,428 |
| Total trading liabilities | 1,410,403 | 11,383 |
| Securities sold under agreements to repurchase | 2,451,630 | 19,787 |
| Securities loaned | 867,748 | 7,004 |
| Payables to: | | |
| Broker-dealers and clearing organizations | 32,725 | 264 |
| Customers | 155,445 | 1,255 |
| Other | 74,922 | 605 |
| Income taxes payable and deferred income taxes | 45,121 | 364 |
| Accrued employee compensation and benefits | 62,023 | 500 |
| Long-term debt | 674,608 | 5,445 |
| Subordinated borrowings | 41,030 | 331 |
| Total Liabilities | 6,815,609 | 55,009 |
| Commitments and contingent liabilities | | |
| Minority interest | 178,821 | 1,443 |
| Shareholders' Equity | | |
| Preferred stock, 100 million shares authorized, no shares outstanding | — | — |
| Common stock, ¥50 par value, 4,000 million shares authorized, 1,331,735,258 shares issued and outstanding | 138,432 | 1,117 |
| Additional paid-in capital | 115,569 | 933 |
| Retained earnings | 326,038 | 2,631 |
| Accumulated other comprehensive loss, net of tax | (16,823) | (136) |
| Common stock held in treasury, at cost, 3,627,000 shares | (2,573) | (20) |
| Deferred stock compensation | (106) | (1) |
| Total Shareholders' Equity | 560,537 | 4,524 |
| Total Liabilities and Shareholders' Equity | ¥ 7,554,967 | \$ 60,976 |

The accompanying notes are an integral part of these consolidated financial statements.

DAIWA SECURITIES GROUP INC.
CONSOLIDATED STATEMENT OF EARNINGS
Year ended March 31, 2001

| | Millions of Yen | Millions of U. S. Dollars |
|---|-----------------|------------------------------|
| | 2001 | 2001 |
| Net Revenues: | | |
| Commissions and fees | ¥ 207,632 | \$ 1,676 |
| Principal transactions | 171,807 | 1,387 |
| Investment banking | 41,010 | 331 |
| Losses on investment securities, net | (60,310) | (487) |
| Interest revenue and dividends | 225,254 | 1,818 |
| Non-securities related income | 77,606 | 626 |
| Other income | 5,140 | 42 |
| Total Revenues | 668,139 | 5,393 |
| Less interest expenses | (201,999) | (1,630) |
| Less non-securities related expenses | (52,488) | (424) |
| Total Net Revenues | 413,652 | 3,339 |
| Non-interest expenses: | | |
| Employee compensation and benefits | 144,285 | 1,165 |
| Floor brokerage, communication and other transaction related costs | 37,499 | 303 |
| Data processing and other services | 16,128 | 130 |
| Occupancy and equipment | 37,775 | 305 |
| Taxes other than income taxes | 7,610 | 61 |
| Depreciation and amortization | 18,217 | 147 |
| Other expenses | 43,877 | 354 |
| Total Non-Interest Expenses | 305,391 | 2,465 |
| Income Before Income Taxes | 108,261 | 874 |
| Provision for income taxes | 43,394 | 350 |
| Income Before Minority Interest and Equity in Income | 64,867 | 524 |
| Minority interest | (28,481) | (230) |
| Equity in net income of affiliates | 209 | 1 |
| Net Income | ¥ 36,595 | \$ 295 |
| Earnings Per Share | | |
| | Yen | U.S. Dollars |
| Basic | ¥ 27.57 | \$ 0.22 |
| Diluted | 26.43 | 0.21 |

The accompanying notes are an integral part of these consolidated financial statements.

DAIWA SECURITIES GROUP INC.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
Year ended March 31, 2001

| | Millions of Yen | Millions of U. S. Dollars |
|--|-----------------|------------------------------|
| | 2001 | 2001 |
| Net Income | ¥ 36,595 | \$ 295 |
| Other Comprehensive Income, Net of tax: | | |
| Foreign currency translation adjustment | 8,854 | 71 |
| Minimum pension liability : | | |
| Minimum pension liability | (838) | (7) |
| Tax benefit and minority interest | 361 | 3 |
| Minimum pension liability, net | (477) | (4) |
| Other Comprehensive Income, Net of tax | 8,377 | 67 |
| Comprehensive Income | ¥ 44,972 | \$ 362 |

The accompanying notes are an integral part of these consolidated financial statements.

DAIWA SECURITIES GROUP INC.
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
Year ended March 31, 2001

| | Millions of Yen | | | | | | | | | |
|---|-----------------|-----------|----------------------------------|----------------------|---|---------|-------------------------------------|-----------------------------------|----------------------------------|---|
| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss, net of tax | | Common Stock Held in Treasury | Deferred Stock Compensation | Total Shareholders' Equity | |
| | | | | | Number of Shares | Amount | | | | Foreign Currency Translation Adjustment |
| | | | | | | | | | | |
| Balance at April 1, 2000 | 1,331,733,430 | ¥ 138,431 | ¥ 115,419 | ¥ 306,689 | ¥ (25,200) | ¥ — | ¥ (3,613) | ¥ — | ¥ 531,726 | |
| Net income | — | — | — | 36,595 | — | — | — | — | 36,595 | |
| Dividends on common stock 13 yen per share | — | — | — | (17,246) | — | — | — | — | (17,246) | |
| Translation adjustments | — | — | — | — | 8,854 | — | — | — | 8,854 | |
| Minimum pension liability, net | — | — | — | — | — | (477) | — | — | (477) | |
| Conversion of convertible bonds | 1,828 | 1 | 1 | — | — | — | — | — | 2 | |
| Purchase of treasury stock | — | — | — | — | — | — | (278) | — | (278) | |
| Exercise of stock options | — | — | — | — | — | — | 973 | — | 973 | |
| Resales of treasury stock | — | — | — | — | — | — | 322 | — | 322 | |
| Resales of treasury stock accompanied by forfeit of stock options | — | — | — | — | — | — | 23 | — | 23 | |
| Deferred stock compensation from incentive warrants granted to employees | — | — | 149 | — | — | — | — | (149) | — | |
| Amortization of deferred stock compensation expense | — | — | — | — | — | — | — | 43 | 43 | |
| Balance at March 31, 2001 | 1,331,735,258 | ¥ 138,432 | ¥ 115,569 | ¥ 326,038 | ¥ (16,346) | ¥ (477) | ¥ (2,573) | ¥ (106) | ¥ 560,537 | |

| | Millions of U. S. Dollars | | | | | | | | | |
|---|---------------------------|----------|----------------------------------|----------------------|---|--------|-------------------------------------|-----------------------------------|----------------------------------|---|
| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss, net of tax | | Common Stock Held in Treasury | Deferred Stock Compensation | Total Shareholders' Equity | |
| | | | | | Number of Shares | Amount | | | | Foreign Currency Translation Adjustment |
| | | | | | | | | | | |
| Balance at April 1, 2000 | 1,331,733,430 | \$ 1,117 | \$ 932 | \$ 2,475 | \$ (203) | \$ — | \$ (29) | \$ — | \$ 4,292 | |
| Net income | — | — | — | 295 | — | — | — | — | 295 | |
| Dividends on common stock 13 yen per share | — | — | — | (139) | — | — | — | — | (139) | |
| Cumulative translation adjustments | — | — | — | — | 71 | — | — | — | 71 | |
| Minimum pension liability, net | — | — | — | — | — | (4) | — | — | (4) | |
| Conversion of convertible bonds | 1,828 | 0 | 0 | — | — | — | — | — | 0 | |
| Purchase of treasury stock | — | — | — | — | — | — | (2) | — | (2) | |
| Exercise of stock options | — | — | — | — | — | — | 8 | — | 8 | |
| Resales of treasury stock | — | — | — | — | — | — | 3 | — | 3 | |
| Resales of treasury stock accompanied by forfeit of stock options | — | — | — | — | — | — | 0 | — | 0 | |
| Deferred stock compensation from incentive warrants granted to employees | — | — | 1 | — | — | — | — | (1) | — | |
| Amortization of deferred stock compensation expense | — | — | — | — | — | — | — | 0 | — | |
| Balance at March 31, 2001 | 1,331,735,258 | \$ 1,117 | \$ 933 | \$ 2,631 | \$ (132) | \$ (4) | \$ (20) | \$ (1) | \$ 4,524 | |

The accompanying notes are an integral part of these consolidated financial statements.

DAIWA SECURITIES GROUP INC.
CONSOLIDATED STATEMENT OF CASHFLOWS
Year ended March 31, 2001

| | Millions of Yen | Millions of U. S. Dollars |
|--|-----------------|------------------------------|
| | 2001 | 2001 |
| Cash Flows from Operating Activities | | |
| Net income | ¥ 36,595 | \$ 295 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation and amortization | 18,217 | 147 |
| Provision for allowance for doubtful accounts | 4,935 | 40 |
| Deferred income taxes | (5,078) | (41) |
| Net realized gains on sales of investments | (8,768) | (71) |
| Net unrealized losses and write off of investments | 69,079 | 558 |
| Net realized gains on disposition of property, equipment and leasehold improvements, net | (182) | (1) |
| Minority interest | 28,481 | 230 |
| (Increase) decrease in operating assets: | | |
| Cash and securities segregated for regulatory purposes | 149,800 | 1,209 |
| Trading assets, including those under pledge | 215,536 | 1,740 |
| Securities purchased under agreements to resell | (1,297,351) | (10,471) |
| Securities borrowed | 97,131 | 784 |
| Receivables from brokers and dealers | (278,502) | (2,248) |
| Receivables from customers | 222,369 | 1,795 |
| Increase (decrease) in operating liabilities: | | |
| Trading liabilities | (76,655) | (619) |
| Securities sold under agreements to repurchase | 740,153 | 5,974 |
| Securities loaned | (57,661) | (465) |
| Payables from brokers and dealers | 7,742 | 62 |
| Payables from customers | (125,109) | (1,010) |
| Other, net | (12,571) | (102) |
| Cash used in Operating Activities | (271,839) | (2,194) |
| Cash Flows from Investing Activities | | |
| Purchases of investments | (160,985) | (1,299) |
| Proceeds from sales and maturities of investments | 184,708 | 1,491 |
| Purchases of property, equipment and leasehold improvements | (32,292) | (261) |
| Proceeds from sales of property, equipment and leasehold improvements | 6,642 | 54 |
| Net change in time deposits | (2,223) | (18) |
| Other, net | 6,221 | 50 |
| Cash provided by Investing Activities | 2,071 | 17 |
| Cash Flows from Financing Activities | | |
| Proceeds from short-term borrowings, net | 91,193 | 736 |
| Repayments for long-term debt | (216,882) | (1,750) |
| Proceeds from long-term debt | 218,109 | 1,760 |
| Issuance of subsidiary's stock | 2,145 | 17 |
| Dividends paid | (17,276) | (139) |
| Other, net | (119) | (1) |
| Cash provided by Financing Activities | 77,170 | 623 |
| Effect of exchange rate changes on cash and cash equivalents | 7,990 | 64 |
| Decrease in cash and cash equivalents | (184,608) | (1,490) |
| Cash and cash equivalents, beginning of year | 494,990 | 3,995 |
| Cash and cash equivalents, end of year | ¥ 310,382 | \$ 2,505 |
| Supplemental Information on Cash Flows | | |
| Interest payments | ¥ 206,092 | \$ 1,663 |
| Income tax payments | 91,012 | 735 |
| Non-cash financing activity - conversion of convertible bonds into equity | 2 | 0 |

The accompanying notes are an integral part of these consolidated financial statements.

DAIWA SECURITIES GROUP INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2001

1. Basis of Financial Statements

The consolidated financial statements include the accounts of Daiwa Securities Group Inc. (the "Company"), a Japanese corporation, and its subsidiaries (collectively "Daiwa"). Daiwa's principal subsidiaries include:

- Daiwa Securities Co. Ltd. ("Daiwa Securities")
- Daiwa Securities SB Capital Markets Co. Ltd. ("Daiwa SBCM")
- Daiwa Asset Management Co. Ltd. ("Daiwa Asset Management")
- Daiwa Institute of Research Ltd. ("DIR")
- NIF Ventures Co., Ltd. ("NIF")

Daiwa Securities is the retail-securities arm of Daiwa. This company operates through a network of 124 branches as well as non-traditional routes, including the Internet. Daiwa Securities also operates a full-fledged call center to provide telephone-based securities-related services. Daiwa SBCM is the wholesale securities company of Daiwa. Daiwa SBCM was established on April 5, 1999 as a 60%-owned joint venture with Sumitomo Bank. Daiwa Asset Management is the asset management company of Daiwa. In addition, Daiwa has several other overseas subsidiaries, mainly engaged in the securities business.

Subsequent to year end, on April 1, 2001, Sumitomo Bank and Sakura Bank merged to form Sumitomo Mitsui Banking Corporation. Associated with this merger, Sakura Securities, a securities subsidiary of Sakura Bank, was integrated into Daiwa SBCM, which was subsequently renamed to Daiwa Securities SMBC Co. Ltd. The integration of Sakura Securities was accounted for as a purchase.

Daiwa is primarily engaged in the business of a securities broker-dealer, pursuant to which Daiwa provides services including brokerage, trading, underwriting, strategic advice, product development, and structured finance. In addition, Daiwa provides various support services, including research, asset and capital management and venture capital, through a network in major capital markets.

The accounts of the Company and its domestic subsidiaries are maintained in yen and in conformity with Japanese income tax laws and accounting practices. Daiwa's foreign subsidiaries primarily maintain their accounts in conformity with the accounting practices of the countries of their domicile. The functional currency of those foreign subsidiaries is mainly the currency of their domicile.

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and reflect adjustments and reclassifications which are not included in the consolidated financial statements issued by the Company or by its subsidiaries in Japan in accordance with the applicable statutory requirements and accounting practices in the countries of their incorporation. The accompanying consolidated financial statements are stated in yen. The translations of yen amounts to U.S. dollars are included solely for the convenience of the reader, using the approximate exchange rate of ¥123.90 to US \$1, which was prevailing at March 31, 2001 as quoted by the Bank of Tokyo-Mitsubishi. The convenience translations should not be construed to be representative of yen amounts that have been, could have been, or could in the future be converted to U.S. dollars.

Management of the Company has made a number of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosures of contingent assets and liabilities, to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from those estimates.

2. Significant Accounting Policies

The accompanying consolidated financial statements of the Company and its subsidiaries have been prepared in conformity with the following accounting policies:

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and companies that are controlled by the Company through direct or indirect ownership of more than 50% of the voting rights. All inter-company balances and transactions have been eliminated in consolidation.

Investments in companies of which the Company directly or indirectly owns greater than 20% are accounted for using the equity method. Certain companies of which the Company has less than 20% but greater than 15% of the voting rights and has the ability to exercise significant influence on operating and financial policies of the investees are also accounted for using the equity method.

Cash and cash equivalents

For purposes of reporting cash flows, Daiwa defines cash and cash equivalents as cash on hand, readily-available deposits and highly liquid investments with original maturities not exceeding three months.

Trading assets and liabilities

Trading assets and liabilities are recorded on a trade date basis in the consolidated balance sheet at either market value or fair value. Trading liabilities include securities and other financial instruments sold but not owned, for which Daiwa will be obligated to purchase at a future date. Market values are principally based on quoted market prices. If quoted market prices are not readily available, fair values are determined based on other relevant factors, including broker or dealer price quotations, price quotations for similar instruments, or pricing models. Changes in the market values or fair values are reflected in principal transactions in the accompanying consolidated statement of earnings. Interest revenues and dividends or interest expenses arising from financial instruments used in trading activities are reflected in the consolidated statement of earnings as interest and dividend revenues or interest expenses.

Derivative financial instruments used for trading purposes are reported at market or fair values in the consolidated balance sheet as trading assets or trading liabilities, as appropriate. Margin on futures and options contracts is included in receivables and payables, as applicable. Gains and losses generated from derivatives held or issued for trading purposes are reported as principal transactions in the consolidated statement of earnings, which includes realized gains and losses as well as changes in the market values or fair values of such instruments.

Derivatives used for hedging purposes, including foreign exchange forwards, interest rate swaps and currency swaps, are principally accounted for on an accrual basis. Gains or losses from the forward contracts are recognized as adjustments to foreign exchange gains or losses of the underlying hedged items. Both interest from the swaps and the hedged items are accrued as interest revenues or expenses over the life of their contracts. Related accruals are recognized as receivables from or payables to others in the consolidated balance sheet.

Securities financing transactions

Securities purchased under agreements to resell or securities sold under agreements to repurchase, which is principally composed of commercial paper and government or government agency securities, are treated as collateralized financing transactions and are carried at their contractual amounts plus accrued interest. It is Daiwa's policy to take possession of securities purchased under agreements to resell. Daiwa monitors the market value of the underlying collateral regularly to ensure its sufficiency as compared with the related receivable. Additional collateral is obtained where appropriate, to protect against credit exposure, as specified in the respective agreements.

Securities borrowed and loaned are treated as collateralized financing transactions and are recorded on the accompanying consolidated balance sheet at the amount of cash collateral advanced or received. These transactions are generally collateralized by cash, securities or letters of credit. Daiwa monitors the market value of the securities borrowed or loaned on a daily basis and obtains additional cash or securities, as necessary, to ensure that such transactions are adequately collateralized.

In Japan, there is a market for securities borrowing/lending transactions where no collateral is required. Daiwa is engaged in securities borrowing as a participant of the market, but does not participate as a lender of securities.

On the consolidated balance sheet, all firm-owned securities pledged to counterparties, where the counterparties have the right, by contract or custom, to sell or repledge the securities, are classified as securities pledged as collateral as required by Statement of Financial Accounting Standards ("SFAS") No. 140.

Customer transactions

Customer securities transactions are recorded on a settlement date basis. Receivables from and payables to customers include amounts due on cash and margin transactions. Securities owned by customers, including those that collateralize margin or other similar transactions, are not reflected on the consolidated balance sheet.

Commissions charged for executing customer transactions and related expenses are accrued on a trade date basis and are included in current period earnings.

Investment banking activity

Underwriting revenues and fees from mergers and acquisitions are accrued when services for transactions are substantially completed. Expenses related to securities offering in which Daiwa acts as an underwriter or agent are deferred to match the related revenue recognition.

Investments

Investments made by the Company and certain subsidiaries include equity securities, debt securities, venture capital investments, investment partnerships, and funds in trust and other. Marketable investments are recorded at market value, based on quoted market prices. Non-marketable investments, including venture capital investments and investment partnerships, are recorded at fair value, based on management's estimate of realizable value. Unrealized gains or losses of investments are recognized in the consolidated statement of earnings.

Equity securities and debt securities have been acquired mainly for Daiwa's non-brokerage investment purposes and consist of marketable and non-marketable securities. Venture capital investments and investment partnerships are owned principally by an investment subsidiary of the consolidated group for the purpose of obtaining capital gains to be realized primarily through sales at the time of, or following, an initial public offerings.

Property and equipment

Property, equipment and leasehold improvements are stated at cost, net of accumulated depreciation and amortization, except for land which is reported at historical cost. Depreciation of buildings is computed by straight-line or declining-balance method over their estimated useful lives. Equipment is depreciated on a declining-balance method and leasehold improvements are amortized on a straight-line method over the lesser of the remaining term of the lease or the economic useful lives of the assets. Certain internal use direct software development costs are capitalized and amortized on a straight-line basis over their expected useful lives. Maintenance and repairs are charged to expenses as incurred, while significant improvements are capitalized.

Impairment of long-lived assets

In accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of," long-lived assets and certain identifiable intangibles to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Where undiscounted future expected cash flow is less than the carrying amount of the assets, an impairment loss is recognized based on the fair value of the assets. Assets to be disposed of are inherent reported at the lower of carrying amount or estimated fair value less cost to sell.

Allowance for doubtful accounts

The allowance for doubtful accounts is maintained at a level that, in the judgment of management, is adequate to provide for inherent losses on receivables whose uncollectibility may be reasonably anticipated. The allowance is increased by provisions charged to income and is decreased by charge-offs, net of recoveries. In evaluating the adequacy of the allowance, management considers various factors, including current economic conditions, credit concentrations or deterioration in pledged collateral and historical loss experience. Receivables are charged off when, in the opinion of management, the likelihood of full collection is believed to be minimal. Doubtful receivables are included in receivables from others, also net of allowance for doubtful accounts, in the consolidated balance sheet.

Under SFAS No. 114, "Accounting by Creditors for Impairment of a Loan," impaired loans are measured according to the present value of expected future cash flows discounted at the loan's original effective interest rate. As a practical expedient, impairment is measured on the basis of the loan's observable market price or the fair value of the collateral, if the loan is collateral-dependent. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance. As of March 31, 2001, impaired loans amounted to ¥61,752 million (\$498 million) and the related valuation allowance was ¥35,474 million (\$286 million). These loans are included in other assets in the consolidated balance sheet, net of valuation allowance. Interest revenue is recognized on an accrual basis in the consolidated statement of earnings.

Goodwill

The cost of acquired subsidiaries and affiliates in excess of fair value of the related net assets at acquisition is recorded as goodwill and is being amortized over 5 years on a straight line basis.

Stock-based compensation

Daiwa accounts for stock-based compensation plans in accordance with the intrinsic value method prescribed by Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," rather than the fair value method as described in SFAS No. 123, "Accounting for Stock-Based Compensation." In accordance with APB No. 25, compensation cost is recognized for such plans that have intrinsic value on the date of grant.

Translation of foreign currencies

Assets and liabilities are translated at the exchange rate in effect at fiscal year-end and income and expenses are translated at the average rate of exchange prevailing during the fiscal year. The effect of translating the financial statements of subsidiaries where the functional currency is not the Japanese yen is included in accumulated other comprehensive loss. Gains or losses resulting from foreign currency transactions are included in the consolidated statement of earnings.

Income taxes

In accordance with SFAS No. 109, "Accounting for Income Taxes," deferred tax assets and liabilities are recorded for the expected future tax consequences of temporary differences between the financial reporting and the tax bases of the assets and liabilities based upon enacted tax laws and rates. Daiwa recognizes deferred tax assets to the extent they are expected to be realized. Deferred tax assets and liabilities are reported as deferred income taxes in the accompanying consolidated balance sheet. Deferred tax expenses or benefits are recognized in the consolidated statement of earnings for the changes in deferred tax liabilities or assets between years.

Earnings per share

Earnings per share of common stock is computed in accordance with SFAS No. 128, "Earnings Per Share." Earnings per share is based on the weighted average number of common shares outstanding during the year. Diluted earnings per share is computed based on the weighted average number of common shares and share equivalents outstanding for the year.

Non-securities related income and expenses

Non-securities related income consists of revenues which are derived from subsidiaries not engaged in the broker dealer business. Non-securities related expenses are the related costs of revenues derived from non-broker dealer subsidiaries.

3. New Accounting Pronouncements

Derivatives and hedge accounting

Daiwa will adopt SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. SFAS No. 133 establishes new accounting and reporting standards for derivative instruments and hedging activities as of April 1, 2001. It requires an entity to recognize all derivatives as either assets or liabilities on the consolidated balance sheet and measure those derivatives at fair value. The accounting for the gains and losses resulting from changes in fair value of those derivatives depends on the intended use of the derivative and whether it qualifies for hedge accounting.

Currently, the majority of Daiwa's derivative instruments are recognized at fair value as trading assets and liabilities, as these transactions are entered into for trading purposes. However, Daiwa also enters into derivative contracts to hedge its exposure relating to non-trading assets and liabilities, which are recorded on an accrual basis, as described above under Note 2 "Significant Accounting Policies." The new standard requires adjustments to be made to the carrying value of such derivatives upon initial adoption of SFAS No. 133. Daiwa estimates that it will record an after tax decrease to other comprehensive income of approximately ¥378 million (\$3 million). Daiwa does not anticipate the impact on net income of non-trading derivatives will be material.

Accounting for transfers and servicing of financial assets and liabilities

In September 2000, the Financial Accounting Standards Board (“FASB”) has issued SFAS No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, a replacement of FASB Statement No. 125.” This statement revises certain criteria promulgated in previous accounting literature for accounting for securitizations and other transfers of financial assets and collateral, and requires additional disclosures concerning these activities. The accounting requirements of SFAS No. 140 for securitizations and other transfers of financial assets are effective for these activities occurring on or after April 1, 2001. Applicable disclosure requirements and certain reclassification requirements on the financial statements for fiscal years ending after December 15, 2000, have been incorporated. The effect of adopting SFAS No. 140 provisions, which will become applicable to Daiwa after April 1, 2001, is not anticipated to have a material impact on Daiwa’s consolidated financial statements.

4. Financial Instruments

Trading transactions

Revenues from Daiwa’s trading transactions, including derivative transactions, for the year ended March 31, 2001, are as follows:

| | <u>Millions of Yen</u> | <u>Millions of U. S. Dollars</u> |
|--|------------------------|--------------------------------------|
| | 2001 | 2001 |
| Fixed income | ¥ 38,481 | \$ 311 |
| Equity | 130,522 | 1,053 |
| Foreign exchange and other derivatives | 2,804 | 23 |
| Total | ¥171,807 | \$1,387 |

Financial instruments with off-balance-sheet risk

Daiwa enters into various transactions involving derivatives and other off-balance-sheet financial instruments. These financial instruments include futures, forward and foreign exchange contracts, exchange-traded and over-the-counter options, and interest rate and foreign currency swap agreements. These derivative financial instruments are used to meet the needs of customers, conduct trading activities, and manage market risks and are, therefore, subject to varying degrees of market and credit risk. Derivative transactions are entered into for trading purposes or to hedge other positions or transactions.

Futures and forward contracts provide for the delayed delivery of the underlying instruments. As a writer of options, Daiwa receives a premium in exchange for giving the counterparty the right to buy or sell the security at a future date at a contracted price. Interest rate swaps involve the exchange of payments based on fixed or floating rates applied to notional amounts. The notional or contractual amounts related to these financial instruments reflect the volume and activity and do not reflect the amounts at risk. Futures contracts are executed on an exchange, and cash settlement is made on a daily basis for market movements. Accordingly, futures contracts generally do not have credit risk. The credit risk for forward contracts, options, and swaps is limited to the unrealized market valuation gains recorded in the consolidated balance sheet. Market risk is substantially dependent upon the value of the underlying financial instruments and is affected by market forces such as volatility and changes in interest and foreign exchange rates.

In addition, Daiwa has sold securities that it does not currently own and will therefore be obligated to purchase such securities at a future date. Daiwa has recorded these obligations in the consolidated financial statements at March 31, 2001, at the market value of the related securities and will incur a loss if the market value of the securities increases subsequent to March 31, 2001.

In the normal course of business, Daiwa's customer activities involve the execution, settlement, and financing of various customer securities transactions. These activities may expose Daiwa to off-balance-sheet risk in the event the customer or the other broker is unable to fulfill its contractual obligations and thus, Daiwa has to purchase or sell the financial instrument underlying the contract at a loss.

Daiwa's customer securities activities are transacted on either a cash or margin basis. In margin transactions, Daiwa extends credit to its customers, subject to various regulatory and internal margin requirements, collateralized by cash and securities in the customers' accounts. In connection with these activities, Daiwa executes and clears customer transactions involving the sale of securities not yet purchased, substantially all of which are transacted on a margin basis subject to individual exchange regulations. Such transactions may expose Daiwa to significant off-balance-sheet risk in the event margin requirements are not sufficient to fully cover losses that customers may incur. In the event the customer fails to satisfy its obligations, Daiwa may be required to purchase or sell financial instruments at prevailing market prices to fulfill the customer's obligations.

Daiwa seeks to control the risks associated with its customer activities by requiring customers to maintain margin collateral in compliance with various regulatory and internal guidelines. Daiwa monitors required margin levels daily and, pursuant to such guidelines, requires the customer to deposit additional collateral or to reduce positions when necessary.

Daiwa's customer financing and securities settlement activities require Daiwa to pledge customer securities as collateral in support of various securities financing transactions. In the event the counterparty is unable to meet its contractual obligation to return customer securities pledged as collateral, Daiwa may be exposed to the risk of acquiring the securities at prevailing market prices in order to satisfy its customer obligations. Daiwa controls this risk by monitoring the market value of securities pledged on a daily basis and by requiring adjustments of collateral levels in the event of excess market exposure. Furthermore, Daiwa establishes credit limits for such activities and monitors compliance on a daily basis.

Derivative financial instruments used for trading purposes

As of March 31, 2001, the gross notional or contractual amounts of derivative financial instruments used for trading purposes are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|-------------------------------|--------------------|------------------------------|
| | 2001 | 2001 |
| Interest rate: | | |
| Swap agreements | ¥26,409,188 | \$213,149 |
| Futures and forward contracts | 507,785 | 4,098 |
| Options held | 260,013 | 2,099 |
| Options written | 377,234 | 3,045 |
| Foreign exchange: | | |
| Swap agreements | 380,099 | 3,068 |
| Futures and forward contracts | 660,501 | 5,331 |
| Options held | 4,156 | 34 |
| Options written | 3,656 | 29 |
| Equity: | | |
| Swap agreements | 76,860 | 620 |
| Futures and forward contracts | 689,104 | 5,562 |
| Options held | 664,407 | 5,362 |
| Options written | 742,422 | 5,992 |
| Other | 8,811 | 71 |
| Total | ¥30,784,236 | \$248,460 |

The notional or contractual amount of derivatives reflects the level of activity in these instruments and do not represent the amount of market or credit risks. Daiwa's exposure to credit risk on derivative instruments is generally limited to the net replacement cost, which is measured by the fair value of the product in a gain position.

The remaining maturities of notional or contractual amounts outstanding for derivatives financial instruments are as follows:

| | 2001 (Millions of Yen) | | | | |
|----------------------------------|------------------------|-------------------|-------------------|-------------------------|--------------------|
| | Less than 1 year | 1 to 3 years | 3 to 5 years | Greater than 5 years | Total |
| Swap agreements | ¥ 9,234,031 | ¥7,542,512 | ¥4,726,559 | ¥5,363,045 | ¥26,866,147 |
| Futures and forward contracts | 1,857,216 | 174 | — | — | 1,857,390 |
| Options held | 899,378 | 29,198 | — | — | 928,576 |
| Options written | 1,085,333 | 33,924 | 4,055 | — | 1,123,312 |
| Other | 1,408 | 2,703 | 4,700 | — | 8,811 |
| Total | ¥13,077,366 | ¥7,608,511 | ¥4,735,314 | ¥5,363,045 | ¥30,784,236 |
| Percent of total | 42.5 | 24.7 | 15.4 | 17.4 | 100.0 |

| | 2001 (Millions of U. S. Dollars) | | | | |
|----------------------------------|----------------------------------|-----------------|-----------------|-------------------------|------------------|
| | Less than 1 year | 1 to 3 years | 3 to 5 years | Greater than 5 years | Total |
| Swap agreements | \$ 74,528 | \$60,876 | \$38,148 | \$43,285 | \$216,837 |
| Futures and forward contracts | 14,990 | 1 | — | — | 14,991 |
| Options held | 7,259 | 236 | — | — | 7,495 |
| Options written | 8,760 | 273 | 33 | — | 9,066 |
| Other | 11 | 22 | 38 | — | 71 |
| Total | \$105,548 | \$61,408 | \$38,219 | \$43,285 | \$248,460 |

The fair value and the average monthly fair value of derivatives financial instruments held or issued for trading purposes as of March 31, 2001, are as follows:

| | 2001 (Millions of Yen) | | | |
|-------------------------------|------------------------|-----------------|------------------------------|-----------------|
| | Fair value at year-end | | Average month-end fair value | |
| | Assets | Liabilities | Assets | Liabilities |
| Swap agreements | ¥263,934 | ¥252,488 | ¥153,629 | ¥139,072 |
| Futures and forward contracts | 8,826 | 8,329 | 13,467 | 5,316 |
| Options held | 43,022 | — | 31,715 | — |
| Options written | — | 40,049 | — | 25,376 |
| Other | 29 | 9 | 28 | 40 |
| Total | ¥315,811 | ¥300,875 | ¥198,839 | ¥169,804 |

| | 2001 (Millions of U. S. Dollars) | | | |
|-------------------------------|----------------------------------|----------------|------------------------------|----------------|
| | Fair value at year-end | | Average month-end fair value | |
| | Assets | Liabilities | Assets | Liabilities |
| Swap agreements | \$2,130 | \$2,038 | \$1,240 | \$1,122 |
| Futures and forward contracts | 72 | 67 | 109 | 43 |
| Options held | 347 | — | 256 | — |
| Options written | — | 323 | — | 205 |
| Other | 0 | 0 | 0 | 0 |
| Total | \$2,549 | \$2,428 | \$1,605 | \$1,370 |

The following table summarizes the credit quality of Daiwa's derivatives by counterparty credit ratings and contract replacement costs (*1) of contracts in a gain position at March 31, 2001.

| Rating (*2) | Millions of Yen | Millions of U. S. Dollars |
|--------------|-----------------|---------------------------|
| | 2001 | 2001 |
| AAA | ¥ 24 | \$ 0 |
| AA | 29,564 | 239 |
| A | 41,765 | 337 |
| BBB | 17,731 | 143 |
| BB | 1,502 | 12 |
| Other (*3) | 97 | 1 |
| Total | ¥90,683 | \$732 |

(*1) Replacement costs, net of collateral, are reported on a net basis when Daiwa considers that a legal right of set-off exists.

(*2) Rating Agency Equivalent

(*3) "Other" indicates counterparties for which no rating was available. It does not necessarily indicate that the counterparty credit rating is below investment grade.

When entering into derivative transactions with counterparties, Daiwa may be subject to bilateral collateral agreements ("Collateral Agreements"). The Company monitors the fair value of its derivative transactions on a daily basis, with additional collateral obtained or refunded as necessary. If these Collateral Agreements allow the counterparty to repledge Daiwa's proprietary securities, such securities pledged are separately recorded on the consolidated balance sheet as securities pledged as collateral. Cash collateral is recorded as a receivable from or payable to the counterparty. Securities collateral received under these Collateral Agreements is not recorded on the consolidated balance sheet.

As of March 31, 2001, Daiwa has pledged ¥17,554 million (\$142 million) and ¥7,967 million (\$64 million) of cash and securities collateral, respectively, and has received ¥6,504 million (\$52 million) and ¥4,600 million (\$37 million) of cash and securities collateral, respectively, under these Collateral Agreements. These cash and securities may be resold or repledged.

Derivative financial instruments used for non-trading purposes

Daiwa enters into derivative contracts, such as foreign exchange forwards, interest rate swaps and currency swaps to mitigate risks associated with its long-term loans or debt by hedging interest rate or exchange rate exposure of such financial instruments for the purpose of asset and liability management.

Gains and losses on these non-trading derivatives are deferred and recognized over the life of the derivative contract. Additionally, gains and losses resulting from early termination of these derivatives are also deferred and recognized over the underlying asset or liability. If the underlying asset or liability is terminated prior to its maturity, gains and losses on the hedging derivative are immediately recognized in the consolidated statement of earnings.

As of March 31, 2001, the notional amounts of derivatives used for non-trading purposes are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|---------------------------|-----------------|---------------------------|
| | 2001 | 2001 |
| Foreign exchange forwards | ¥ 42,159 | \$340 |
| Interest rate swaps | 68,956 | 557 |
| Currency swaps | 12,231 | 99 |
| Total | ¥123,346 | \$996 |

Fair value of financial instruments

Most of Daiwa's financial instruments are reported in the consolidated balance sheet at market or fair value. Except for long-term borrowings, long-term notes payable and convertible bonds, the carrying amounts of other financial instruments approximate its fair values because of the short term nature of these instruments and/or because variable interest rates are applied to these instruments. Fair value for long-term borrowings is estimated using discounted cash flows.

The fair value of Daiwa's long-term notes payable, subordinated borrowings and convertible bonds is based on current market prices, or based on a discounted cash flow model if market prices are not available. The fair value of Euro Medium Term Notes included in long-term notes payable, excludes the value of features that link the payments or redemption values to interest rates, foreign currency rates or the performance of a specific equity index (e.g., the Nikkei 225) – see Note 9. The fair value of Global Medium Term Notes, included in long-term notes payable, includes the value of features that convert these medium-term borrowings to achieve LIBOR based funding – see Note 9.

The following table shows the estimated fair values of these financial instruments at March 31, 2001.

| | Millions of Yen | | Millions of U. S. Dollars | |
|-------------------------|-----------------|------------|---------------------------|------------|
| | 2001 | | 2001 | |
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Long-term debt: | | | | |
| Long-term borrowings | ¥235,086 | ¥237,273 | \$1,897 | \$1,915 |
| Long-term notes payable | 303,827 | 310,819 | 2,452 | 2,509 |
| Convertible bonds | 135,695 | 164,050 | 1,096 | 1,324 |
| Total | ¥674,608 | ¥712,142 | \$5,445 | \$5,748 |
| Subordinated borrowings | ¥ 41,030 | ¥ 43,977 | \$ 331 | \$ 355 |

Derivatives used for non-trading purposes are principally accounted for on an accrual basis. Fair value for non-trading derivatives is estimated using a discounted cash flow pricing model. The following table shows the estimated fair values of these financial instruments at March 31, 2001.

| | Millions of Yen | | Millions of U.S. Dollars | |
|---------------------------|-----------------|-------------|--------------------------|-------------|
| | 2001 | | 2001 | |
| | Assets | Liabilities | Assets | Liabilities |
| Foreign exchange forwards | ¥ 214 | ¥ 24 | \$ 2 | \$ 0 |
| Interest rate swaps | 1,966 | 1,208 | 16 | 10 |
| Currency swaps | 865 | 207 | 7 | 2 |

Concentrations of credit risk

Daiwa is engaged in various trading and brokerage activities in which counterparties primarily consist of broker-dealers, banks, and other financial institutions. In the event counterparties do not fulfill their obligations, Daiwa may be exposed to credit risk. The risk of default depends on the creditworthiness of the counterparty or issuer of the financial instrument. It is Daiwa's policy to review, as necessary, the credit standing of each counterparty.

Concentrations of credit risk from financial instruments, including contractual commitments, exist when groups of issuers or counterparties have similar business characteristics or are engaged in similar activities which would cause their ability to meet their contractual commitments, in a similar manner, by adverse changes in the economy or other market conditions. Daiwa's largest single concentration of credit risk is with securities issued by the Japanese government, of which Daiwa directly owns ¥796,239 million (\$6,426 million) and has received as collateral ¥1,389,675 million (\$11,216 million) at March 31, 2001.

Risk management

Daiwa's two domestic securities subsidiaries, Daiwa Securities and Daiwa SBCM ("Securities subsidiaries"), enter into trading activities to meet customer needs, for its proprietary trading activities, as a broker and end-user. These trading assets and trading liabilities include (1) cash securities such as stocks and bonds, (2) financial derivatives traded on exchanges such as futures and options based on stock price indices, bonds and interest rates, and (3) financial derivatives traded over the counter such as currency and interest rate swaps, foreign exchange forward contracts, bonds with options, currency options, forward rate agreements and OTC equity derivatives.

The principal risks inherent in trading in these markets are market risk and credit risk. Market risk represents the potential for loss from changes in the value of financial instruments due to price and interest rate fluctuations in the markets. To manage its market risk, the securities subsidiaries determine the risk amount and profitability of each instrument by the use of a value-at-risk model. Credit risk represents the potential loss arising from the failure of the counterparty to fulfill its contractual obligations. The securities subsidiaries assess the credit risk of their counterparties by applying internal credit rating and monitor their exposure in terms of notional amount and credit exposure.

Daiwa SBCM has established five risk management policies: active management participation, system of internal supervision, sound management by setting risk limits; risk management assuming emergency; and transparency in risk management process. By complying with these five policies, Daiwa SBCM expects that risks associated with trading activities will be adequately controlled within a range which management is willing to assume.

5. Securities Financing Transactions

Daiwa is engaged in secured borrowing and lending transactions to finance trading inventory, to obtain securities for settlement, and to fulfill its customers' needs. As of March 31, 2001, receivables and payables under agreements to resell or repurchase and securities borrowed or loaned are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|---|-------------------|------------------------------|
| | 2001 | 2001 |
| Securities purchased under agreements to resell | ¥1,845,731 | \$14,897 |
| Securities borrowed | 1,023,054 | 8,257 |
| Total | ¥2,868,785 | \$23,154 |
| Securities sold under agreements to repurchase | ¥2,451,630 | \$19,787 |
| Securities loaned | 867,748 | 7,004 |
| Total | ¥3,319,378 | \$26,791 |

Under these securities financing transactions, Daiwa either receives or pledges securities. As of March 31, 2001, the market values of securities received and pledged under such securities financing transactions are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|-------------------------------------|-----------------|------------------------------|
| | 2001 | 2001 |
| Market value of securities received | ¥5,659,563 | \$45,678 |
| Market value of securities pledged | 5,532,478 | 44,653 |

Market value of securities received in the table above includes those borrowed with no collateral, in the amount of ¥579,223 million (\$4,675 million).

Daiwa receives collateral securities as part of its these securities financing transactions and of other transactions. Daiwa has the right to resell or repledge many of these collateralized securities, which were not recorded in the consolidated balance sheet in accordance with industry practice.

As of March 31, 2001, Daiwa has the right to sell or repledge ¥5,664,162 million (\$45,716 million) of securities it has received under the securities financing transactions mentioned above or as a collateral under derivative transactions, in addition to those received as collateral under customer margin transactions. Most of these repledged securities are used to secure repurchase agreements, to enter into securities lending transactions or to deliver to counterparties to cover short positions. As of March 31, 2001, ¥4,381,168 million (\$35,361 million) of securities was either sold or repledged.

Included in securities pledged, ¥1,272,649 million (\$10,272 million) of securities are of proprietary positions. These securities are separately recorded on the consolidated balance sheet as securities pledged as collateral, as Daiwa's counterparties have the right by contract or custom to sell or repledge the securities pledged.

6. Pledged Assets and Collateral

Information regarding pledged assets at March 31, 2001, other than those disclosed in Notes 4 and 5, are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|----------------|-----------------|------------------------------|
| | 2001 | 2001 |
| Trading assets | ¥435,869 | \$3,518 |
| Investments | 41,496 | 335 |
| Property | 53,393 | 431 |
| Other assets | 7,810 | 63 |
| Total | ¥538,568 | \$4,347 |

Trading assets and investments are pledged to clearing organizations for securing securities settlement. Property and other assets are pledged to secure bank loans.

7. Investments

Investments at March 31, 2001 consists of the following:

| | Millions of Yen | Millions of U. S. Dollars |
|---|-----------------|------------------------------|
| | 2001 | 2001 |
| Equity securities | ¥109,502 | \$ 884 |
| Debt securities | 9,433 | 76 |
| Venture capital investments and investment partnerships | 61,398 | 496 |
| Funds in trust and other | 119,377 | 963 |
| Total | ¥299,710 | \$2,419 |

Net unrealized losses from these investments reported in the consolidated statement of earnings as of March 31, 2001, were ¥62,529 million (\$505 million).

The proceeds and gross realized gains and losses from the sale of investments are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|-----------------------|-----------------|------------------------------|
| | 2001 | 2001 |
| Proceeds | ¥42,745 | \$345 |
| Gross realized gains | 11,210 | 90 |
| Gross realized losses | 5,321 | 43 |

8. Property, Equipment and Leasehold improvements

Property and equipment, net of accumulated depreciation and amortization, at March 31, 2001 consisted of the following:

| | Millions of Yen | Millions of U. S. Dollars |
|--------------------------------------|-----------------|---------------------------|
| | 2001 | 2001 |
| Land | ¥ 87,198 | \$ 704 |
| Buildings | 94,423 | 762 |
| Equipment and leasehold improvements | 30,015 | 242 |
| Software | 33,917 | 274 |
| Other | 7,999 | 64 |
| Total | ¥253,552 | \$2,046 |

In prior years, based on a comprehensive review of the long-lived assets, Daiwa recognized impairment loss of ¥164,195 million (\$1,325 million) on certain land and buildings. Based on further review during the year ended March 31, 2001, no additional assets were deemed to be impaired.

Included in land and buildings is approximately ¥31 billion (\$250 million) in real estate properties that Daiwa holds for domestic third party leasing purposes. On October 26, 2001, Daiwa decided to withdraw from its domestic third party real estate leasing business and sell most of such properties. Management anticipates that the liquidation proceeds will approximate current book value.

9. Short-term Borrowings, Long-term Debt and Subordinated Borrowings

Short-term borrowings

Daiwa maintains borrowing facilities with banks and other financial institutions together with the issuance of commercial paper to support general liquidity needs. Short-term borrowing at March 31, 2001 consisted of the following:

| | Millions of Yen | Millions of U. S. Dollars |
|---|-----------------|---------------------------|
| | 2001 | 2001 |
| Commercial paper | ¥516,300 | \$4,167 |
| Bank loans | 369,539 | 2,983 |
| Loans from other financial institutions | 114,115 | 921 |
| Total | ¥999,954 | \$8,071 |

Daiwa's weighted average interest rates on its short-term borrowings, which include bank and other loans and commercial paper, was 0.72 % at March 31, 2001.

Long-term debt

Long-term debt consists of borrowings from financial institutions and Japanese yen denominated bonds and notes with both floating and fixed interest rates. Long-term debt may have risk exposures, including both interest rate and currency. From the viewpoint of asset and liability management, Daiwa uses non-trading derivatives to reduce this risk exposures.

Included in long-term debt, in the accompanying consolidated balance sheet, Daiwa issues medium-term notes under two programs referred to as the Euro Medium Term Note Program and Global Medium Term Note Program. Under both programs medium term notes are offered to investors in a customized form to meet the requirements of customers.

Notes issued under the Euro Medium Term Note Program, authorized at ¥200 billion (\$1.6 billion), include features whereby payments and redemption values are linked to interest rates, foreign currency exchange rates or the performance of specific equity indices (e.g., the Nikkei 225). Such notes may also contain provisions where Daiwa or the holder has the option to redeem the notes at specified dates prior to maturity. Such options may be exercised depending on the market level of interest rates, foreign currency exchange rates, specify equity indices, etc. For risk management purposes these derivative features are separately accounted for and are included as part of Daiwa's trading positions. The market risk inherent in these derivative positions is managed as part of Daiwa's overall trading position.

Notes issued under the Global Medium Term Note Program, authorized at \$5,000 million, include features whereby most of the relevant interest rate exposures are hedged by separate derivative instruments to achieve LIBOR based funding. Currency risk is also hedged by separate derivative instruments. These derivative positions are accounted for on an accrual basis to match the related interest expense of the underlying note.

Increase of MTN Program Facility

Pursuant to the resolution of the Board of Directors' meeting on November 5, 2001, the facility to issue Euro Medium Term Note Program was increased. On November 16, 2001, Daiwa SMBC increased its MTN Program facility from ¥200 billion, as mentioned above, to ¥400 billion. Outstanding notes under this program increased to ¥186,306 million (\$1,504 million) as of November 30, 2001.

Long-term debt at March 31, 2001 consisted of the following:

| | Millions of Yen 2001 | Millions of U. S. Dollars 2001 |
|--|-------------------------|--------------------------------------|
| Convertible bond payable in yen, convertible into common stock at ¥3,035.90 per share : 1.5% due 2002 | ¥ 19,440 | \$ 157 |
| Convertible bond payable in yen, convertible into common stock at ¥2,367.00 per share : 1.4% due 2003 | 36,269 | 293 |
| Convertible bond payable in yen, convertible into common stock at ¥1,094.00 per share : 0.5% due 2006 | 79,986 | 646 |
| Bond payable in yen, 1.4% due 2005 | 100,000 | 807 |
| Warrant bond payable in yen, 1.37% due 2004 * | 8,400 | 68 |
| Notes payable in yen issued by subsidiaries : | | |
| 4.8% Euro-yen bond due 2002 | 2,978 | 24 |
| 2.0% Euro-yen bond due 2002 | 80,000 | 646 |
| Euro medium-term notes issued by a subsidiary, Maturities through 2013 | 77,600 | 626 |
| Global medium-term notes issued by foreign subsidiaries, Maturities through 2008 | 34,574 | 279 |
| Borrowings from financial institutions at interest rates ranging From 0.3% to 4.3%, maturities through 2008 | 235,086 | 1,897 |
| Others | 275 | 2 |
| Total | ¥674,608 | \$5,445 |

* This detachable warrant bond was issued for the purpose providing an incentive warrant plan - see Note 11.

| | Millions of Yen | Millions of U. S. Dollars |
|-----------------------------|-----------------|------------------------------|
| | 2001 | 2001 |
| Fixed rate obligations* | ¥459,379 | \$3,708 |
| Floating rate obligations** | 103,055 | 832 |
| Medium-term notes | 112,174 | 905 |
| Total | ¥674,608 | \$5,445 |

* Fixed-rate obligations denominated in Japanese yen will mature between 2001 to 2008 and bear interest at rates ranging from 0.5% to 4.3%.

** Floating interest rates are generally based on inter-bank offered rates or long-term prime interest rates.

The effective weighted average interest rates for long-term debt, after taking into account the impact of interest rate and currency swaps was 1.47% as of March 31, 2001.

The aggregate annual maturities of long-term debt are as below:

| | Millions of Yen | Millions of U. S. Dollars |
|---------------------|-----------------|------------------------------|
| | 2001 | 2001 |
| 2002 | ¥134,149 | \$1,083 |
| 2003 | 137,304 | 1,108 |
| 2004 | 114,414 | 923 |
| 2005 | 15,062 | 122 |
| 2006 | 112,270 | 906 |
| 2007 and thereafter | 161,409 | 1,303 |
| Total | ¥674,608 | \$5,445 |

Subordinated borrowings

Subordinated borrowings are available for computing net worth under the net capital adequacy requirements of the Financial Services Agency in Japan. As of March 31, 2001, the interest rate on subordinated borrowings in the amount of ¥40 billion (\$323 million), due 2004, was 2.5%. The interest rate exposure for the remaining balance of ¥1 billion (\$8 million), due 2005, is hedged by derivative financial instruments to achieve LIBOR based funding.

Credit facilities

Daiwa has a committed, senior unsecured revolving credit facilities totaling ¥190 billion (\$1,533 million) under agreements with several banks. These agreements contain covenants requiring Daiwa to keep specified levels of net worth or credit ratings, as defined in the agreements. There was no utilization under this facility during the year ended March 31, 2001.

Daiwa monitors the credit quality of the banks and renews annually or semi-annually the amounts and terms of these credit facilities.

10. Retirement Benefits

Retirement benefits for employees

Daiwa has various retirement benefit plans for eligible employees as follows:

a. Unfunded plan

Prior to the year ended March 31, 2001, in connection with the Company's reorganization to the holding company structure, the Company and certain domestic consolidated subsidiaries canceled all their employees' retirement benefit plans, both unfunded and funded, and liquidated their plan assets in order to pay retirement benefits to entitled employees in the amount which would be required if they involuntarily terminated their employment as of the dates when the plan assets had been liquidated. Subsequent to the Company's reorganization to the holding company structure, Daiwa provides an unfunded plan to its employees in return for services rendered each year, where the amount to be contributed to the individual employee's account is defined rather than the amount of pension benefits the employee is to receive. Under this unfunded plan, pension benefits are accumulated on an annual basis by contribution of Daiwa and earns a guaranteed hypothetical return at a rate of which Daiwa predetermines each year. Contributions to this unfunded plan are included in accrued employee compensation and benefits in the consolidated balance sheet. The amount of benefit expense recognized for this unfunded plan was ¥5,099 million (\$41 million) for the year ended March 31, 2001. The balance of the unfunded plan included in accrued employee compensation and benefits in the consolidated balance sheet as of March 31, 2001 was ¥7,309 million (\$59 million).

b. Closed funded plan

In connection with the reorganization, the funded plan has been changed to a closed funded plan since April 1, 1999 primarily for existing vested retired employees.

Retirement benefits as of March 31, 2001 consisted of the following:

| | Millions of Yen | Millions of U. S. Dollars |
|--|-----------------|---------------------------|
| | 2001 | 2001 |
| Change in accumulated benefit obligations: | | |
| Benefit obligation at beginning of year | ¥ 9,827 | \$79 |
| Interest cost | 289 | 2 |
| Benefits paid | (791) | (6) |
| Benefit obligation at the end of year | 9,325 | 75 |
| Change in fair value of plan assets: | | |
| Fair value of plan assets at beginning of year | 9,827 | 79 |
| Actual return on plan assets | (762) | (6) |
| Benefits paid | (791) | (6) |
| Fair value of plan assets at the end of year | 8,274 | 67 |
| Funded status | (1,051) | (8) |
| Unrecognized net actuarial loss | 838 | 7 |
| Net accrued pension liabilities | (213) | (1) |
| Minimum pension liability adjustment | (838) | (7) |
| Accrued benefit cost | ¥(1,051) | \$ (8) |

Due to the nature of this closed funded plan, future compensation levels are not required to be taken into account for the purpose of calculating the projected benefit obligation. Thus, the accumulated benefit obligation equals the projected benefit obligation.

The provisions of SFAS No. 87 requires the recognition of an additional minimum liability for which the accumulated benefit obligation exceeds the plan assets. This liability has been recorded is accrued employee compensation and benefits in the consolidated balance sheet. The total amount of additional minimum liability has been recorded as a component of accumulated other comprehensive loss, net of tax, at March 31, 2001.

The following expense relate to the closed funded plan is included in the consolidated statement of earnings for the year ended March 31, 2001.

| | Millions of Yen | Millions of U. S. Dollars |
|--|-----------------|---------------------------|
| | 2001 | 2001 |
| Interest cost on accumulated benefit obligations | ¥ 289 | \$ 2 |
| Expected return on plan assets | (286) | (2) |
| Amortization of net actuarial loss | 210 | 2 |
| Net periodic pension cost | ¥ 213 | \$ 2 |

The actuarial assumptions used in calculating the projected benefit obligations at March 31, 2001 are as follows:

| | 2001 |
|--------------------------------|------|
| Discount rate | 3.0% |
| Expected return on plan assets | 3.0% |

c. Multiemployers' pension plan

The Company and its certain domestic consolidated subsidiaries are members of a industry-wide non-contributory welfare pension plan administered by the Securities Companies' Welfare Pension Fund, in conjunction with the contributory governmental welfare pension plan. The plan asset for the non-contributory welfare pension plan and the contributory governmental welfare pension plan is not controlled or administered by Daiwa. Amounts contributed to the plan and charged to pension expense were approximately ¥2,080 million (\$17 million) for the year ended March 31, 2001.

For the past several years, the plan's fund has experienced a low rate of performance due to adverse conditions in Japan's fund management environment, including low interest rates and declining stock prices in the Japanese market. Management estimated, based on analysis of currently available information, Daiwa's portion of the difference between the projected future benefit obligation and the fair value of the plan assets has become material. As such, Daiwa had established a reserve for this potential unfunded obligation of ¥28,442 million (\$230 million) as of March 31, 2001.

On September 29, 2001, the Company and its certain domestic consolidated subsidiaries withdrew from this non-contributory welfare pension plan. Please refer to Note 18 "Subsequent Event."

Retirement benefits for directors

Daiwa recognizes retirement benefits for directors on an accrual basis. Directors' retirement benefits of ¥1,889 million (\$15 million) are included in accrued employee compensation and benefits of the accompanying consolidated balance sheet as of March 31, 2001.

11. Employee Incentive Plans

The Company accounts for its stock option plan using the intrinsic value method prescribed by APB No. 25, as permitted by SFAS No. 123. Under the provisions of APB No. 25, compensation cost for stock options is measured as the excess, if any, of the quoted market price of the Company's common stock at the date of grant over the amount an employee must pay to acquire the stock.

Stock option plan

On June 25, 1998, the shareholders of the Company approved a stock option plan granted to Daiwa's directors and key employees to purchase treasury shares of the Company. The Company had been authorized to purchase up to 6 million shares in connection with this stock option plan. Options were granted on March 30, 1999, and are exercisable during the period from July 1, 2000 to June 20, 2003, at the exercise price of ¥667 (\$5.3).

Pursuant to APB No. 25, no compensation expense was recognized under this plan.

The activity of this stock options plan for the year ended March 31, 2001 is set forth below:

| | Number of shares | Weighted Average Exercise Price Yen | Weighted Average Remaining Life Years |
|----------------------------------|------------------|---|---|
| Outstanding at beginning of year | 5,004,000 | ¥667 | 3.22 |
| Granted | — | — | — |
| Exercised | 1,382,000 | 667 | — |
| Forfeited or Expired | 33,000 | — | — |
| Outstanding at end of year | 3,589,000 | ¥667 | 2.22 |

Incentive warrant plan

The Company also provides an incentive warrant plan to Daiwa's eligible employees and directors. Under this plan, the Company granted warrants to purchase 6,216,000 shares by repurchasing warrants attached to a warrant bond issued on August 24, 2000. These warrants will be exercisable during the period from September 2, 2002 to August 23, 2004, at an exercise price of ¥1,345 (\$10.9) per share.

Pursuant to APB No. 25, the Company recognized compensation expense of ¥44 million (\$355 thousand) related to this plan.

The fair value of warrants granted during the year ended March 31, 2001 was ¥322 (\$2.6) per share. Fair value was estimated as of the grant date based on a Black-Scholes option pricing model using the following assumptions:

| | 2001 |
|-------------------------|---------|
| Risk-free interest rate | 1.06% |
| Expected life | 4 years |
| Expected volatility | 30.0% |
| Dividend yield | 0.95% |

The activity of this plan for the year ended March 31, 2001 is set forth below:

| | Number of shares | Weighted Average | Weighted Average |
|----------------------------------|------------------|------------------|------------------|
| | | Exercise Price | Remaining Life |
| | | Yen | Years |
| Outstanding at beginning of year | — | — | — |
| Granted | 6,216,000 | ¥1,345 | 3.40 |
| Exercised | — | — | — |
| Forfeited or Expired | — | — | — |
| Outstanding at end of year | 6,216,000 | ¥1,345 | 3.40 |

Pro forma effect of SFAS No. 123

Had the Company elected to apply the fair value method prescribed by SFAS No. 123 for the stock option plan and the incentive warrant plan, the net income and earnings per share as of March 31, 2001 would be as follows:

| | Millions of Yen | Millions of |
|----------------------------|-----------------|---------------|
| | | U. S. Dollars |
| Net income | | |
| As reported | ¥36,595 | \$295 |
| Pro forma | 34,593 | 279 |
| | Yen | U. S. Dollars |
| Basic earnings per share | | |
| As reported | ¥27.57 | \$0.22 |
| Pro forma | 26.06 | 0.21 |
| Diluted earnings per share | | |
| As reported | 26.43 | 0.21 |
| Pro forma | 25.00 | 0.20 |

12. Income Taxes

The components of the provision for income taxes reflected on the consolidated statement of earnings are as follows:

| | Millions of Yen | Millions of |
|----------------------------------|-----------------|---------------|
| | 2001 | U. S. Dollars |
| | 2001 | 2001 |
| Current: | | |
| Domestic | ¥48,074 | \$388 |
| Foreign | 800 | 6 |
| Total | 48,874 | 394 |
| Deferred: | | |
| Domestic | (5,429) | (44) |
| Foreign | (51) | (0) |
| Total | (5,480) | (44) |
| Total provision for income taxes | ¥43,394 | \$350 |

A reconciliation of statutory income tax rate in Japan to Daiwa's effective income tax rate is as follows:

| | 2001 |
|---|--------|
| Statutory income tax rate | 42.1 % |
| Impact of: | |
| Valuation allowance | 6.4 |
| Lower tax rate applicable to income of foreign subsidiaries | (5.1) |
| Other, net | (3.3) |
| Effective income tax rate | 40.1 % |

Deferred income taxes reflect the net tax effects of temporary differences between the financial reporting and tax bases of assets and liabilities. These temporary differences result in taxable or deductible amounts in future years and are measured using the tax rates and laws that will be in effect when such differences are expected to reverse. Details of deferred tax assets and liabilities as of March 31, 2001 are as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|--|-----------------|---------------------------|
| | 2001 | 2001 |
| Deferred tax assets: | | |
| Net operating losses carry forward | ¥ 71,910 | \$ 580 |
| Inter-company profit | 52,585 | 424 |
| Impairment loss | 35,272 | 285 |
| Employee Compensation and benefit plans | 19,809 | 160 |
| Other | 31,354 | 253 |
| Gross deferred tax assets | 210,930 | 1,702 |
| Less: valuation allowance* | (114,113) | (921) |
| Total deferred tax assets | 96,817 | 781 |
| Deferred tax liabilities | | |
| Unrealized gain on investment securities | 15,121 | 122 |
| Other | 4,806 | 38 |
| Total deferred tax liabilities | 19,927 | 160 |
| Net deferred tax assets | ¥ 76,890 | \$ 621 |

* The valuation allowance mainly relates to deferred tax assets of net operating losses carried forward for tax purposes that are not expected to be realized.

Net deferred tax assets and liabilities at March 31, 2001 are reflected in the accompanying consolidated balance sheet under the following captions:

| | Millions of Yen | Millions of U. S. Dollars |
|--|-----------------|---------------------------|
| | 2001 | 2001 |
| Deferred income taxes | ¥91,414 | \$738 |
| Income taxes payable and deferred income taxes | 14,524 | 117 |
| Net deferred tax assets | ¥76,890 | \$621 |

Net operating losses carried forward are available to reduce future income taxes. Certain subsidiaries have recognized deferred tax assets from net operating losses carried forward totaling ¥71,910 million (\$580 million) as of March 31, 2001. Daiwa's operating losses expire in various years after 2002.

Cumulative undistributed earnings of foreign subsidiaries were approximately ¥17,830 million (\$144 million) as of March 31, 2001. No deferred tax liabilities have been provided for these undistributed earnings. Except to the extent such earnings can be repatriated tax-efficiently, they are permanently invested abroad.

13. Other Commitments and Contingent Liabilities

Litigation

In the normal course of its business, Daiwa is subject to ongoing legal risk including lawsuits and other legal proceeding. The management of Daiwa believes that the ultimate resolution of such litigation will not, in the aggregate, have a material adverse effect on Daiwa's consolidated financial statements.

Commitments and guarantees

As provided in the following table, as of March 31, 2001, Daiwa enters into contractual commitments to extend credit and has guarantees principally to banks for housing loans of its employees.

| | Millions of Yen | Millions of U. S. Dollars |
|--------------|-----------------|------------------------------|
| | 2001 | 2001 |
| Commitments | ¥1,771 | \$14 |
| Guarantees | 6,774 | 55 |
| Total | ¥8,545 | \$69 |

Additionally, a subsidiary of Daiwa engaged in the business of credit card loan has commitments to extend credit for consumer loans in the amount of ¥10,828 million (\$87 million). Commitments to extend credit arise from agreements to extend to customers unused lines of credit on certain credit cards.

Leases

Daiwa has obligations under capital and operating lease agreements, principally for office space and equipment. Presented below is a schedule of minimum future rentals under operating leases with initial or remaining terms exceeding one year:

| | Millions of Yen | Millions of U. S. Dollars |
|---------------------|-----------------|------------------------------|
| | 2001 | 2001 |
| 2002 | ¥13,534 | \$109 |
| 2003 | 11,340 | 92 |
| 2004 | 8,855 | 72 |
| 2005 | 8,304 | 67 |
| 2006 | 7,728 | 62 |
| 2007 and thereafter | 30,485 | 246 |
| Total | ¥80,246 | \$648 |

Certain lease agreements contain renewal options and escalation clauses resulting from increased assessments for real estate taxes and other charges. Rent expense during the year ended March 31, 2001 was ¥24,477 million (\$198 million).

14. Shareholders' Equity

Under the Commercial Code of Japan, certain issuance of common shares, including conversions of debt issued and exercise of warrants, are required to be credited to the common stock account for at least the greater of par value or 50% of the proceeds. The Commercial Code of Japan permits, upon approval of the Board of Directors, transfer of amounts from additional paid-in capital to the common stock account. Also under the Commercial Code of Japan, a plan for appropriation of retained earnings proposed by the Company's Board of Directors must be approved at a shareholders' meeting which is held within three months from the end of each fiscal year, as prescribed by the Articles of Incorporation of the Company.

Changes in retained earnings for the fiscal year reflected in the accompanying consolidated statement of changes in shareholders' equity represent the results of such appropriations approved by the shareholders.

In addition, under the Commercial Code of Japan, the Company has transferred 50% of the conversion proceeds of convertible debt to common stock and the remainders to the additional paid-in capital.

15. Earnings Per Share

Earnings per share is calculated as follows:

| | 2001 |
|--|---------------|
| Weighted average common shares outstanding | 1,327,472,109 |
| Effect of dilutive securities: | |
| Stock options | — |
| Stock incentive warrant | — |
| Convertible bonds | 73,114,031 |
| Diluted shares | 1,400,586,140 |

| | Millions of Yen | Millions of U. S. Dollars |
|---------------------------------------|-----------------|---------------------------|
| | 2001 | 2001 |
| Net income applicable to common stock | ¥36,595 | \$295 |
| Effect of dilutive securities | 419 | 3 |
| Adjusted for diluted computation | ¥37,014 | \$298 |

| | Yen | U. S. Dollars |
|----------------------|--------|---------------|
| | 2001 | 2001 |
| Net income per share | | |
| Basic | ¥27.57 | \$0.22 |
| Diluted | 26.43 | 0.21 |

16. Regulatory Requirements and Dividends Limitation

Daiwa Securities and Daiwa SBCM, registered broker-dealers, are subject to capital adequacy requirements under the government ordinance, prescribed by the Financial Services Agency. Pursuant to this rule, the minimum required net worth, which includes subordinated liabilities and other adjustments for illiquid assets, is expected to exceed 140% of the aggregate amount of risk-based assets, which are determined based on various categories of risk weights assigned to different types of assets and off-balance sheet exposures, as defined. As of March 31, 2001, the capital adequacy ratios of Daiwa Securities and of Daiwa SBCM are 251.3% and 364.7%, respectively.

A subsidiary located in the United States of America (“DSA”) is subject to the Securities Exchange Commission (“SEC”) Uniform Net Capital Rule 15c3-1 (the “Rule”), which requires the maintenance of minimum net capital. DSA has elected to use the alternative method, permitted by the Rule, which requires that DSA maintain minimum net capital, as defined, equal to the greatest of \$250,000 or 2% of aggregate debit balances arising from customer transactions, as defined, or 4% of the funds required to be segregated pursuant to the Commodities Exchange Act, and the regulations thereunder. At March 31, 2001, DSA had net capital of \$190 million, which is \$186 million in excess of the minimum net capital required under the Rule.

A subsidiary in the United Kingdom (“DSEL”), a registered broker-dealer, is subject to the capital requirements of the Securities and Futures Authority (“SFA”) of the United Kingdom. Other subsidiaries are also subject to various regulatory requirements that may limit cash dividends and advances to Daiwa and that establish minimum capital requirements. At March 31, 2001, these subsidiaries were in compliance with all applicable regulatory capital adequacy requirements.

The amount of retained earnings available for dividends under the Commercial Code of Japan is based on the amount recorded in the Company’s statutory books of account, which are maintained in accordance with generally accepted accounting principles in Japan. The adjustments incorporated in the consolidated financial statements but not recorded in the statutory books of account have no effect on the determination of retained earnings available for dividends under the Commercial Code of Japan. The balance of the total amount of retained earnings available for dividends in the Company’s statutory book of account as of March 31, 2001 amounted to ¥432,041 million (\$3,487 million).

Additionally the Securities and Exchange Law of Japan requires all securities companies to maintain a special purpose reserve at a prescribed level. The reserves Daiwa Securities and Daiwa SBCM have provided in its statutory books are ¥1,975 million (\$16 million) in total, which is reversed and included in the retained earnings of the accompanying consolidated balance sheet.

The Commercial Code of Japan provides that an amount equivalent to at least 10% of cash dividends paid and other cash outlays resulting from appropriation of retained earnings be appropriated to a legal reserve until such reserve equals 25% of the issued capital. The reserve the Company has provided in its statutory books is ¥45,335 million (\$366 million) as of March 31, 2001, which is included in the retained earnings of the accompanying consolidated balance sheet. There are no dividend limitations due to the requirement of the provision, because the Company has provided the reserve at more than the maximum level required. The Commercial Code of Japan also provides that both additional paid-in capital and the legal reserve are not available for cash dividends but may be used to reduce a capital deficit by resolution of the shareholders or may be capitalized by resolution of the Board of Directors.

17. Segment and Geographic Information

Segment information

Daiwa organizes its operating segments based on a combination of products, customer types and geographic factors. Daiwa organizes its operating segments based on products and services or by type of customer in Japan. Daiwa's domestic operations are segmented according to four primary lines of businesses: retail securities business, wholesale securities businesses, asset management and other. The retail securities and wholesale securities businesses are conducted by Daiwa Securities and Daiwa SBCM, respectively. Daiwa Asset Management carries out the asset management business. Daiwa's overseas subsidiaries are considered separate operating units and the businesses within the region are delegated to carry out diversified business activities. Daiwa's primary overseas operations include business conducted by Daiwa Securities SBCM Europe Limited, headquartered in London, Daiwa Securities SBCM Hong Kong Limited in Hong Kong and Daiwa Securities America Inc. in New York.

The business segment information, presented below, is based on Japanese GAAP and represents the financial information presented to and used by executive management in deciding the allocation of resources and in assessing performance. Since the following segment information is not consistent with the accompanying consolidated financial as prepared on a basis of US GAAP, a reconciliation is provided for the segments' total ordinary income and income before income tax. This reconciliation includes elimination of inter-segment allocation of net operating revenues and ordinary income which are reflected in the Eliminations column.

"Net operating revenues" below, a term defined by the "Uniform Accounting Standards of Securities Companies" (set by the board of directors of the Japan Securities Dealers' Association, September 28, 2001), includes "Commissions," "Net gains on trading," "Net gains on operational investment securities," "Interest and dividend income," "Other sales revenues," "Interest expenses" and "Cost of sales" under Japanese GAAP. "Ordinary income" includes "Net operating revenues," "Selling, general & administrative expenses," "Non-operating income" and "Non-operating expenses" measured under Japanese GAAP.

| | 2001 (Millions of Yen) | | | | | | | | |
|--|----------------------------|-------------------------------|---------------------------|------------|---------------------|----------|----------------|--------------|------------|
| | Domestic Operations | | | | Overseas Operations | | | | |
| | Retail Securities Business | Wholesale Securities Business | Asset Management Business | Others | America | Europe | Asia & Oceania | Eliminations | Total |
| Net operating revenues | ¥177,633 | ¥ 218,478 | ¥ 66,981 | ¥ 75,893 | ¥ 24,897 | ¥ 20,965 | ¥ 5,644 | ¥ (123,677) | ¥ 466,814 |
| Selling, general & administrative expenses | 153,639 | 94,993 | 57,910 | 39,903 | 13,742 | 16,173 | 4,827 | (94,239) | 286,948 |
| Ordinary income | 24,356 | 123,640 | 10,315 | 27,785 | 11,254 | 5,233 | 811 | (25,598) | 177,796 |
| Year-end total assets | ¥586,654 | ¥5,626,580 | ¥108,115 | ¥1,971,504 | ¥1,817,123 | ¥591,305 | ¥96,287 | ¥(1,547,344) | ¥9,250,224 |

| | 2001 (Millions of U. S. Dollars) | | | | | | | | |
|--|----------------------------------|-------------------------------|---------------------------|----------|---------------------|---------|----------------|--------------|----------|
| | Domestic Operations | | | | Overseas Operations | | | | |
| | Retail Securities Business | Wholesale Securities Business | Asset Management Business | Others | America | Europe | Asia & Oceania | Eliminations | Total |
| Net operating revenues | \$1,434 | \$ 1,763 | \$541 | \$ 612 | \$ 201 | \$ 169 | \$ 46 | \$ (998) | \$ 3,768 |
| Selling, general & administrative expenses | 1,240 | 767 | 467 | 322 | 111 | 131 | 39 | (761) | 2,316 |
| Ordinary income | 197 | 998 | 83 | 224 | 90 | 42 | 7 | (206) | 1,435 |
| Year-end total assets | \$ 4,735 | \$45,412 | \$873 | \$15,912 | \$14,666 | \$4,773 | \$777 | \$(12,489) | \$74,659 |

The reconciliation of ordinary income and total assets for reportable segments to the consolidated operating income and identifiable assets are described below:

| | Millions of Yen | Millions of U. S. Dollars |
|---|-----------------|------------------------------|
| | 2001 | 2001 |
| Ordinary income for reportable segments | ¥177,796 | \$1,435 |
| Impact of: | | |
| Valuation & sales loss on investment securities | (64,164) | (518) |
| Losses on sales of loans receivable | (2,942) | (24) |
| Provision for allowance for bad debt | (1,600) | (13) |
| Amortization of goodwill | (1,519) | (12) |
| Compensated absences | (462) | (4) |
| Valuation & sales profits on property | 1,807 | 15 |
| Others | (655) | (5) |
| Income before income taxes for the consolidated statements of earnings | ¥108,261 | \$ 874 |

| | Millions of Yen | Millions of U. S. Dollars |
|---|-----------------|------------------------------|
| | 2001 | 2001 |
| Total assets for reportable segments | ¥9,250,224 | \$74,659 |
| Impact of: | | |
| Securities received | (1,556,172) | (12,560) |
| Impairment loss in long-lived assets | (158,440) | (1,279) |
| Scope of consolidation | 9,963 | 80 |
| Leasing assets | 9,015 | 73 |
| Others | 377 | 3 |
| Total assets for the consolidated balance sheet | ¥7,554,967 | \$60,976 |

The difference of net revenue between segment amounts and consolidated amounts primarily consist of valuation loss recognized on investment securities.

Geographic information

The Company's net revenue and long-lived assets are generally allocated based on the country of domicile of the legal entity providing service as follows:

| | Millions of Yen | Millions of U. S. Dollars |
|--------------------|-----------------|------------------------------|
| | 2001 | 2001 |
| Net revenue: | | |
| Japan | ¥357,054 | \$2,882 |
| U.S. | 14,629 | 118 |
| Others | 41,969 | 339 |
| Total | ¥413,652 | \$3,339 |
| Long-lived assets: | | |
| Japan | ¥229,318 | \$1,851 |
| U.S. | 1,943 | 16 |
| Others | 28,755 | 232 |
| Total | ¥260,016 | \$2,099 |

Japan and the United States of America are the countries whose revenues from external customers are material. Almost all the revenues of Japan and the United States of America are derived from customers of the segment's domicile. The basis for attributing revenues from external customers to individual countries is principally the location of the foreign subsidiaries.

SFAS No. 131 requires disclosure of revenues from external customers for each product and service as an enterprise-wide information. The consolidated statements of earnings in which the revenues are categorized based on the nature of business, include the required information. No single customer accounted for 10% or more of the total net revenues for the year ended March 31, 2001.

18. Subsequent Event

Withdrawal from the non-contributory welfare pension plan

On September 29, 2001, the Company and most of its domestic consolidated subsidiaries withdrew from the non-contributory welfare pension plan. After taking into consideration the payment made to the Securities Companies' Welfare Pension Fund upon withdrawal, Daiwa recorded a gain amounting to ¥13,691 million (\$111 million) for the reversal of the voluntary reserve, as described in Note 10. The difference between Daiwa's estimation and actual amount charged by the Securities Companies' Welfare Pension Fund to Daiwa upon withdrawal was principally due to the difference in discounted rates used in the calculation of the projected future obligation.



ANDERSEN

Report of Independent Public Accountants

To the Shareholders and the Board of Directors of Daiwa Securities Group Inc.:

We have audited the accompanying consolidated balance sheet of Daiwa Securities Group Inc.(a Japanese corporation) and subsidiaries as of March 31, 2001, and the related consolidated statements of earnings, comprehensive income, shareholders' equity and cash flows for the year ended March 31, 2001, expressed in yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Daiwa Securities Group Inc. and subsidiaries as of March 31, 2001, the results of its operations and its cash flows for the year ended March 31, 2001 in conformity with accounting principles generally accepted in the United States of America.

Also, in our opinion, the U.S. dollars amounts in the accompanying consolidated financial statements have been translated from yen on the basis set forth in Note.1.

Arthur Andersen

Tokyo, Japan

November 30, 2001