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Consolidated Balance Sheets

Daiwa Securities Group Inc.
March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 1)
ASSETS	2006	2005	2006
Cash and cash deposits :			
Cash and cash equivalents	¥ 392,350	¥ 338,697	\$ 3,353,419
Cash segregated as deposits for regulatory purposes	297,878	153,516	2,545,966
Other deposits	15,540	59,992	132,821
	705,768	552,205	6,032,206
Receivables:			
Loans receivable from customers	3,113	4,723	26,607
Loans receivable from other than customers (Note 9)	56,886	71,064	486,205
Trading receivables, net	—	9,420	—
Receivables related to margin transactions (Note 3)	563,538	312,145	4,816,564
Other	157,690	191,371	1,347,786
Less: Allowance for doubtful accounts	(294)	(328)	(2,513)
	780,933	588,395	6,674,649
Collateralized short-term financing agreements (Note 4)	6,274,506	5,348,916	53,628,248
Trading assets (Notes 5 and 9)	6,162,243	5,242,320	52,668,736
Private equity and other securities (Notes 6 and 9)	382,421	142,547	3,268,556
Deferred tax assets (Note 14)	29,488	21,916	252,034
Property and equipment, at cost	232,284	234,920	1,985,334
Less: Accumulated depreciation	(105,753)	(97,300)	(903,872)
	126,531	137,620	1,081,462
Other assets:			
Software	42,608	42,103	364,171
Lease deposits	23,538	23,410	201,179
Investment securities (Notes 6 and 9)	269,854	193,202	2,306,444
Long-term loans receivable	11,865	11,676	101,410
Other (Note 9)	90,987	83,198	777,675
Less: Allowance for doubtful accounts	(1,851)	(8,546)	(15,821)
	437,001	345,043	3,735,058
	¥ 14,898,891	¥ 12,378,962	\$ 127,340,949

See accompanying notes.

	Millions of yen		Thousands of U.S. dollars (Note 1)
LIABILITIES AND SHAREHOLDERS' EQUITY	2006	2005	2006
Borrowings:			
Short-term borrowings (Notes 9 and 12)	¥ 1,795,321	¥ 2,295,929	\$ 15,344,624
Commercial paper	234,210	200,220	2,001,795
Long-term debt (Notes 9 and 12)	1,146,912	949,718	9,802,667
	3,176,443	3,445,867	27,149,086
Payables:			
Payables to customers and counterparties (Note 11)	250,765	288,688	2,143,291
Time deposits received	—	3,240	—
Trading payables, net	302,573	—	2,586,094
Payables related to margin transactions (Notes 3 and 9)	197,483	141,972	1,687,889
Other (Note 13)	43,300	21,183	370,094
	794,121	455,083	6,787,368
Collateralized short-term financing agreements (Note 4)	4,744,007	3,877,731	40,547,068
Trading liabilities (Note 5)	4,879,189	3,658,544	41,702,470
Accrued and other liabilities:			
Income taxes payable	73,779	10,596	630,590
Deferred tax liabilities (Note 14)	41,907	7,177	358,179
Accrued bonuses	41,714	22,811	356,530
Retirement benefits (Note 13)	20,295	20,273	173,462
Other	91,411	37,704	781,291
	269,106	98,561	2,300,052
Statutory reserves (Note 15)	7,025	5,650	60,043
Total liabilities	13,869,891	11,541,436	118,546,087
Minority interests	236,719	189,194	2,023,239
Contingent liabilities (Note 16)			
Shareholders' equity (Notes 17 and 18):			
Common stock, no par value;			
Authorized — 4,000,000 thousand shares			
Issued — 1,332,460 thousand shares as of March 31, 2006	138,828	138,432	1,186,564
Capital surplus	118,339	117,941	1,011,444
Retained earnings	476,216	362,949	4,070,222
Net unrealized gain on securities, net of tax effect	72,694	35,674	621,316
Translation adjustments	864	(5,877)	7,385
Treasury stock, at cost	(14,660)	(787)	(125,308)
Total shareholders' equity	792,281	648,332	6,771,623
	¥ 14,898,891	¥ 12,378,962	\$ 127,340,949

Consolidated Statements of Operations

Daiwa Securities Group Inc.

Years ended March 31, 2006, 2005 and 2004

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2006	2005	2004	2006
Operating revenues:				
Commissions (Note 20)	¥ 309,189	¥ 216,387	¥ 194,163	\$ 2,642,641
Net gain on trading (Note 21)	224,912	151,118	120,195	1,922,325
Net gain on private equity and other securities	21,539	12,763	8,676	184,094
Interest and dividend income	245,211	105,428	96,366	2,095,821
Service fees and other sales	44,809	33,641	34,414	382,983
	845,660	519,337	453,814	7,227,864
Interest expense	231,572	103,677	77,331	1,979,248
Cost of service fees and other sales	34,729	25,228	24,048	296,829
Net operating revenues (Note 19)	579,359	390,432	352,435	4,951,787
Selling, general and administrative expenses (Notes 19 and 22)	325,199	275,544	259,915	2,779,479
Operating income (Note 19)	254,160	114,888	92,520	2,172,308
Other income (expenses):				
Provision for statutory reserves, net (Note 15)	(1,374)	(518)	(1,241)	(11,744)
Other, net (Note 23)	5,570	(1,767)	(14,353)	47,607
	4,196	(2,285)	(15,594)	35,863
Income before income taxes and minority interests	258,356	112,603	76,926	2,208,171
Income taxes (Note 14):				
Current	77,676	11,933	15,170	663,897
Deferred	392	28,234	5,638	3,350
	78,068	40,167	20,808	667,247
Minority interests	(40,340)	(19,771)	(13,481)	(344,786)
Net income	¥ 139,948	¥ 52,665	¥ 42,637	\$ 1,196,138
			yen	U.S. dollars (Note 1)
Per share amounts:				
Net income	¥ 103.90	¥ 39.03	¥ 31.66	\$ 0.89
Diluted net income	98.61	37.36	30.28	0.84
Cash dividends applicable to the year	34.00	13.00	10.00	0.29

See accompanying notes.

Consolidated Statements of Shareholders' Equity

Daiwa Securities Group Inc.

Years ended March 31, 2006, 2005 and 2004

	Number of shares of common stock (thousands)	Millions of yen					
		Common stock	Capital surplus	Retained earnings	Net unrealized gain on securities, net of tax effect	Translation adjustments	Treasury stock, at cost
Balance at March 31, 2003	1,331,735	¥ 138,432	¥ 117,786	¥ 297,404	¥ 1,824	¥ (11,321)	¥ (2,406)
Net income				42,637			
Cash dividends paid				(7,970)			
Net gains on sales of treasury stock (Note 17)			154				
Decrease in retained earnings due to addition of a consolidated subsidiary				(1,291)			
Net unrealized gain on securities, net of tax effect					25,474		
Translation adjustments						1,731	
Change in treasury stock, net							1,716
Balance at March 31, 2004	1,331,735	138,432	117,940	330,780	27,298	(9,590)	(690)
Net income				52,665			
Cash dividends paid				(19,960)			
Conversion of convertible bonds	1	0	1				
Bonuses to directors				(536)			
Net unrealized gain on securities, net of tax effect					8,376		
Translation adjustments						3,713	
Change in treasury stock, net							(97)
Balance at March 31, 2005	1,331,736	138,432	117,941	362,949	35,674	(5,877)	(787)
Net income				139,948			
Increase in retained earnings due to merger of a consolidated subsidiary				608			
Cash dividends paid				(26,611)			
Conversion of convertible bonds	724	396	396				
Bonuses to directors				(678)			
Net gains on sales of treasury stock (Note 17)			2				
Net unrealized gain on securities, net of tax effect					37,020		
Translation adjustments						6,741	
Change in treasury stock, net							(13,873)
Balance at March 31, 2006	1,332,460	¥ 138,828	¥ 118,339	¥ 476,216	¥ 72,694	¥ 864	¥ (14,660)

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	Thousands of U.S. dollars (Note 1)					
	Common stock	Capital surplus	Retained earnings	Net unrealized gain on securities, net of tax effect	Translation adjustments	Treasury stock, at cost
Balance at March 31, 2005	\$1,183,179	\$1,008,043	\$3,102,128	\$304,906	\$ (50,231)	\$ (6,726)
Net income			1,196,138			
Increase in retained earnings due to merger of a consolidated subsidiary			5,196			
Cash dividends paid			(227,444)			
Conversion of convertible bonds	3,385	3,385				
Bonuses to directors			(5,796)			
Net gains on sales of treasury stock (Note 17)		16				
Net unrealized gain on securities, net of tax effect				316,410		
Translation adjustments					57,616	
Change in treasury stock, net						(118,582)
Balance at March 31, 2006	\$1,186,564	\$1,011,444	\$4,070,222	\$621,316	\$7,385	\$(125,308)

See accompanying notes

Consolidated Statements of Cash Flows

Daiwa Securities Group Inc.

Years ended March 31, 2006, 2005 and 2004

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2006	2005	2004	2006
Cash flows from operating activities:				
Net income	¥ 139,948	¥ 52,665	¥ 42,637	\$ 1,196,138
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Depreciation and amortization	22,641	22,129	21,530	193,513
Provision for doubtful accounts, net	226	2,289	680	1,932
Provision for retirement benefits, net	23	1,402	2,979	197
Statutory reserves, net	1,374	518	1,241	11,744
Losses (gains) related to investment securities	(11,060)	(2,687)	208	(94,530)
Losses (gains) related to fixed assets	11,838	(351)	13,015	101,179
Gain on change in stake in subsidiary	(4,725)	—	—	(40,385)
Deferred income taxes	392	28,234	5,638	3,350
Minority interests	40,340	19,771	13,481	344,786
Changes in operating assets and liabilities:				
Receivables and payables related to margin transactions	(195,882)	(28,087)	(88,369)	(1,674,205)
Other receivables and other payables	(29,270)	77,878	(30,291)	(250,171)
Private equity and other securities	(192,645)	(44,197)	(6,944)	(1,646,538)
Trading assets and liabilities	615,610	111,198	1,224,767	5,261,624
Collateralized short-term financing agreements	(63,704)	(1,183,394)	(1,369,799)	(544,479)
Other, net	33,684	(76,044)	45,007	287,897
Total adjustments	228,842	(1,071,341)	(166,857)	1,955,914
Net cash flows provided by (used in) operating activities	368,790	(1,018,676)	(124,220)	3,152,052
Cash flows from investing activities:				
Increase in time deposits	(10,685)	(53,041)	—	(91,325)
Decrease in time deposits	55,201	—	—	471,803
Payments for purchases of property and equipment	(12,526)	(7,786)	(8,147)	(107,060)
Proceeds from sales of property and equipment	719	5,315	6,144	6,145
Payments for purchases of intangible fixed assets	(24,312)	—	—	(207,795)
Payments for purchases of investment securities	(51,554)	(35,693)	(36,972)	(440,632)
Proceeds from sales of investment securities	43,604	99,469	107,541	372,684
Decrease in long-term loans receivable	358	149	1,067	3,060
Other, net	(1,757)	(18,689)	2,154	(15,017)
Net cash flows provided by (used in) investing activities	(952)	(10,276)	71,787	(8,137)

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2006	2005	2004	2006
Cash flows from financing activities:				
Increase (decrease) in short-term borrowings	¥ (446,190)	¥ 759,982	¥ (66,936)	\$ (3,813,590)
Increase (decrease) in long-term debt	58,496	14,788	(16,295)	499,966
Proceeds from issuance of notes	505,358	225,875	318,832	4,319,299
Payments for redemption of bonds and notes	(401,374)	(97,102)	(112,675)	(3,430,547)
Payments of cash dividends	(26,612)	(19,960)	(7,970)	(227,453)
Payments of cash dividends to minority shareholders	(9,177)	(168)	(2,328)	(78,436)
Other, net	(3,446)	454	1,779	(29,453)
Net cash flows provided by (used in) financing activities	(322,945)	883,869	114,407	(2,760,214)
Effect of exchange rate changes on cash and cash equivalents	7,429	3,819	(4,915)	63,496
Net increase (decrease) in cash and cash equivalents	52,322	(141,264)	57,059	447,197
Cash and cash equivalents at beginning of year	338,697	480,123	422,684	2,894,846
Increase in cash and cash equivalents due to merger of a consolidated subsidiary	1,331	—	—	11,376
Increase (decrease) in cash equivalents due to addition (exclusion) of a consolidated subsidiary	—	(162)	380	—
Cash and cash equivalents at end of year	¥ 392,350	¥ 338,697	¥ 480,123	\$ 3,353,419
Supplemental information on cash flows:				
Cash paid during the year for:				
Interest	¥ 222,153	¥ 103,440	¥ 74,077	\$ 1,898,744
Income taxes	11,405	13,690	1,749	97,479

See accompanying notes.

Notes to Consolidated Financial Statements

Daiwa Securities Group Inc.
Three years ended March 31, 2006, 2005 and 2004

1. Basis of financial statements

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

- Daiwa Securities Co. Ltd. (“Daiwa Securities”)
- Daiwa Securities SMBC Co. Ltd. (“Daiwa Securities SMBC”)
- Daiwa Asset Management Co. Ltd. (“Daiwa Asset Management”)
- Daiwa Institute of Research Ltd. (“DIR”)
- NIF SMBC Ventures Co., Ltd. (“NIF SMBC”)
(NIF Ventures Co., Ltd., a consolidated subsidiary of the Company changed its name to NIF SMBC Ventures Co., Ltd. following the merger of SMBC Capital Co., Ltd. on October 1, 2005.)

Daiwa Securities is the retail-securities arm of Daiwa. This company operates through a network of 115 branches as well as non-face-to-face channels, including internet and a full-fledged call center to provide on-line and telephone-based securities-related services. Daiwa Securities SMBC is the wholesale-securities company of Daiwa, a 60%-owned joint venture with Sumitomo Mitsui Financial Group, Inc. Daiwa Asset Management is the asset management company of Daiwa. In addition, Daiwa has several overseas consolidated subsidiaries, mainly engaged in the securities business.

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 asset and capital management, principal finance, venture capital, and research through a network in major capital markets and other services.

The Company and domestic consolidated subsidiaries maintain their official accounting records in yen. The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with generally accepted accounting principles in Japan (“Japanese GAAP”), which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards. The accounts of overseas consolidated subsidiaries are maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries of domicile.

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

The translations of the yen amounts into U.S. dollars are included solely for the convenience of the reader, using the prevailing exchange rate at March 31, 2006, which was ¥117 to U.S. \$1. The convenience translations should not be construed as representations that the yen amounts have been, could have been, or could be, converted into U.S. dollars at this or any other rate of exchange.

2. Significant accounting policies

Consolidation — The consolidated financial statements include the accounts of the Company and significant companies which are controlled by the Company through substantial ownership of more than 50% of the voting rights (excluding companies owned for the purpose of operating principal finance and venture capital business, and not for the purpose of affiliation to the group.) or through ownership of at least 40% and less than 50% of the voting rights and the existence of certain conditions evidencing control by the Company of the decision-making body of such companies.

In addition to investments in companies in excess of 20% (excluding companies owned for the purpose of operating principal finance and venture capital business and not for the purpose of affiliation to the group through personnel management, financial resources, technology, transactions, etc.), certain companies for which the Company has at least 15% and less than 20% of the voting rights and in cases where the Company has the ability to exercise significant influence over operating and financial policies of the investees are accounted for using the equity method.

Material inter-company balances, transactions and profits have been eliminated in consolidation.

Statements of cash flows — For purposes of consolidated statements of cash flows, the Company defines cash equivalents as highly liquid investments with original maturities of three months or less.

Trading assets and trading liabilities — Trading assets and liabilities including securities and financial derivatives for trading purposes held by a securities company are recorded on a trade date basis at fair value in the consolidated balance sheets. Gains and losses including unrealized gains and losses related to transactions for trading purposes are reported as “Net gain on trading” in the accompanying consolidated statements of operations. Fair value is determined based on market prices, quoted prices, internal pricing models (utilizing indicators of general market conditions or other economic measurements), or management’s estimates of amounts to be realized on settlement, assuming current market conditions and an orderly disposition over a reasonable period of time. Securities owned for non-trading purpose,

shown in the accompanying consolidated balance sheets as “Private equity and other securities” and “Investment securities”, are discussed below.

Securities other than trading assets and trading liabilities — Daiwa examines the intent of holding each securities and classifies those securities as (a) securities intended to be held for trading purposes by non-securities companies, (b) debt securities intended to be held to maturity (“held-to-maturity debt securities”), (c) all other securities not classified in any of the above categories (“available-for-sale securities”).

Securities intended to be held for trading purposes by non-securities companies are carried at fair value with recognizing unrealized gains or losses included in consolidated statements of operations.

Held-to-maturity debt securities are stated at amortized cost. Available-for-sale securities with market value are stated at market value, based on quoted market prices. Realized gains and losses on sale of such securities are computed using the moving-average cost. Unrealized gains and losses on these securities are reported, net of tax effect, as a separate component of the consolidated shareholders’ equity.

Available-for-sale securities for which a market value is not available, are stated at the moving-average cost.

If the market value of available-for-sale securities declines significantly, such securities are considered to be impaired and the difference between market value and the carrying amount is recognized as a loss in the period of the decline. For available-for-sale securities, which do not have readily available market value, if the net book value declines significantly and if such decline is considered to be other than temporary, the difference between the carrying amount and the net book value is recognized as a loss in the period of the decline. Impaired losses on these securities are reported in the consolidated statements of operations.

Of those securities with no fair value, investments in limited partnerships and similar partnerships which are regarded as equivalent to securities by the Article 2 (2) of Securities Exchange Act

Notes to Consolidated Financial Statements

Daiwa Securities Group Inc.

Three years ended March 31, 2006, 2005 and 2004

in 2004, share of net income of the partnership has been reflected on consolidated statements of operations and share of net unrealized gains and losses held by the partnerships are directly recorded into consolidated shareholders' equity.

Derivatives used for non-trading purpose — Daiwa states derivative financial instruments at fair value and recognizes changes in the fair value as gains or losses unless the derivative financial instruments are used for hedging purposes. Valuation gains or losses on hedging instruments are mainly deferred as assets or liabilities until the gains or losses on the underlying hedged instruments are realized. Interest received or paid on interest swaps for hedging purposes is accrued without being market-to-market. The premium or discount on foreign exchange forward for hedging purpose is allocated to each fiscal term without being marked-to-market.

Collateralized short-term financing agreements — Collateralized short-term financing agreements consist of securities purchased under agreements to resell ("resell transactions") or securities sold under agreements to repurchase ("repurchase transactions"), and securities borrowed or loaned. Repurchase transactions and resell transactions are carried at their contractual amounts. Securities borrowed or loaned are recorded at the amount of cash collateral advanced or received.

Provision for doubtful accounts — Provisions for doubtful accounts are provided based on the actual historical default rate for normal loans, and based on individually assessed amounts for doubtful and default loans.

Property and equipment — Property and equipment are stated at cost. Impairment losses recognized have been deducted from the acquisition costs. The Company and domestic consolidated subsidiaries compute depreciation principally by the declining-balance method over estimated useful lives. Depreciation for buildings purchased in Japan after April 1, 1998 is computed by the straight-line method. In overseas consolidated subsidiaries, depreciation is mainly computed by the straight-line method.

(Additional Information)

The removal of the headquarters of the Company and some

consolidated subsidiaries has been resolved. The useful lives of buildings and equipment for those headquarters are shortened up to planned the removal date. Extraordinary depreciation expenses of ¥4,439 million (\$37,941 thousand) was recorded as other expense, due to application of shortened useful lives. "Income before income taxes and minority interests" decreased by that amount as a result.

Intangible fixed assets — Intangible fixed assets are generally amortized under the straight-line method. The Company and domestic consolidated subsidiaries compute amortization over estimated useful lives, and over internally estimated useful lives (5 years) for software of in-house use.

Deferred assets — Stock issue costs and bond issue costs are expensed in a lump sum when incurred.

Bonuses — The Company and domestic consolidated subsidiaries follow the Japanese practice of paying bonuses to employees twice a year in June and December, and thus, accrued employees' bonuses represent liabilities estimated as of the balance sheet date. Bonuses to directors and corporate executive officers of the Company, which are subject to approval at the Compensation Committee, represent liabilities estimated as of the balance sheet date. Compensation Committee sets policies for deciding compensation for individual directors and corporate executive officers and determines compensation content for each individual. The Chairman of the Board chairs the committee, while three out of five committee members are outside directors. Bonuses to directors of consolidated subsidiaries, which are subject to approval at the shareholders' meeting, are accounted for as an appropriation of retained earnings.

Retirement benefits for employees — Daiwa has various benefit plans for eligible employees such as unfunded plan and closed funded plan.

Income taxes — Income taxes consist of corporation, enterprise and inhabitants taxes. The provision for income taxes is computed based on the pre-tax income of each of the Company and consolidated subsidiaries with certain adjustments, if necessary.

Income tax consequences of amounts that will become taxable or deductible in future years are recorded as deferred tax assets and liabilities, which are generally raised from the difference in value of assets and liabilities for statutory accounting and tax accounting. Daiwa recognizes deferred tax assets to the extent of amounts reasonably expected to be realized in future.

The Company and NIF SMBC, as parent companies, have filed consolidated tax returns since the previous year. Daiwa Securities SMBC, as parent company, has filed consolidated tax returns since the year ended March 31, 2003.

Translation of foreign currencies — The Company and domestic consolidated subsidiaries translate assets and liabilities in foreign currencies into yen at the year-end exchange rate.

Translation of foreign currency financial statements — Financial statements of overseas consolidated subsidiaries are translated into yen on the basis of the year-end exchange rates for assets and liabilities except that “Retained earnings” are translated at his-

torical rates. Income and expenses are translated at the average exchange rates of the applicable year. The resulting differences are reported as “Translation adjustments” in “Shareholders’ equity” in the accompanying consolidated balance sheets.

Net income per share — Net income per share of common stock is based on the average number of common shares outstanding.

Diluted net income per share is computed based on the average number of common shares outstanding for the year with an adjustment for dilutive convertible bonds based on the number of shares of common stock that would have been issued provided that the outstanding dilutive convertible bonds were converted at the beginning of the year.

Reclassification — Certain reclassifications have been made in the 2005 and 2004 consolidated financial statements to conform to the presentation for 2006.

3. Margin transactions

Margin transactions at March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Assets:			
Customers’ margin loans	¥ 359,331	¥ 126,687	\$ 3,071,208
Cash deposits as collateral for securities borrowed	204,207	185,458	1,745,356
	¥ 563,538	¥ 312,145	\$ 4,816,564
Liabilities:			
Payable to securities finance companies	¥ 7,570	¥ 2,981	\$ 64,702
Proceeds of securities sold for customers’ accounts	189,913	138,991	1,623,187
	¥ 197,483	¥ 141,972	\$ 1,687,889

Customers’ margin loans are stated at amounts equal to the purchase amounts of the relevant securities, which are collateralized by customers’ securities and customers’ deposits. Proceeds of securities sold for customers’ accounts are stated at the sales amounts.

Notes to Consolidated Financial Statements

Daiwa Securities Group Inc.

Three years ended March 31, 2006, 2005 and 2004

4. Collateralized short-term financing agreements

Collateralized short-term financing agreements at March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Assets:			
Securities purchased under agreements to resell	¥ 2,184,881	¥ 1,575,907	\$ 18,674,192
Securities borrowed	4,089,625	3,773,009	34,954,056
	¥ 6,274,506	¥ 5,348,916	\$ 53,628,248
Liabilities:			
Securities sold under agreements to repurchase	¥ 2,811,293	¥ 2,006,465	\$ 24,028,147
Securities loaned	1,932,714	1,871,266	16,518,921
	¥ 4,744,007	¥ 3,877,731	\$ 40,547,068

5. Trading assets and trading liabilities

Trading assets and trading liabilities at March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Trading assets:			
Equities	¥ 371,948	¥ 332,397	\$ 3,179,039
Government, corporate and other bonds	4,005,132	4,187,216	34,231,897
Investment trusts	95,498	130,575	816,221
Commercial paper, certificates of deposits and others	18,635	40,360	159,274
Option transactions	908,197	46,303	7,762,369
Futures and forward transactions	156,934	16,162	1,341,313
Swap agreements	607,483	490,546	5,192,162
Other derivatives	1,127	659	9,636
Credit reserves	(2,711)	(1,898)	(23,175)
	¥ 6,162,243	¥ 5,242,320	\$ 52,668,736
Trading liabilities:			
Equities	¥ 99,551	¥ 98,690	\$ 850,866
Government, corporate and other bonds	3,216,833	3,094,627	27,494,302
Investment trusts	5,471	3,316	46,763
Option transactions	1,007,981	69,551	8,615,222
Futures and forward transactions	67,232	13,463	574,629
Swap agreements	480,973	378,513	4,110,877
Other derivatives	1,148	384	9,811
	¥ 4,879,189	¥ 3,658,544	\$ 41,702,470

6. Securities other than trading assets and trading liabilities

Securities other than trading assets and trading liabilities is composed of “Private equity and other securities” and “Investment securities” in the accompanying consolidated balance sheets.

Cost and market value of securities intended to be held for trading purposes by non-securities companies as of March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		
	Cost	Market value	Difference
March 31, 2006	¥ 3,205	¥ 3,543	¥ 338
March 31, 2005	¥ —	¥ —	¥ —

	Thousands of U.S. dollars		
	Cost	Market value	Difference
March 31, 2006	\$ 27,397	\$ 30,279	\$ 2,882

Cost/amortized cost and market value of held-to-maturity debt securities as of March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		
	Cost/amortized cost	Market value	Difference
Government bonds, local government bonds at March 31, 2006	¥ 2,509	¥ 2,502	¥ (7)
Government bonds, local government bonds at March 31, 2005	¥ 2,126	¥ 2,118	¥ (8)

	Thousands of U.S. dollars		
	Cost/amortized cost	Market value	Difference
Government bonds, local government bonds at March 31, 2006	\$ 21,446	\$ 21,384	\$ (62)

Cost and market value of available-for-sale securities as of March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		
	Cost	Market value	Difference
March 31, 2006:			
Equities	¥ 82,493	¥ 203,127	¥ 120,634
Government, corporate and other bonds	150	158	8
Other	13,719	15,474	1,755
	¥ 96,362	¥ 218,759	¥ 122,397

March 31, 2005:			
Equities	¥ 74,394	¥ 137,744	¥ 63,350
Government, corporate and other bonds	150	153	3
Other	13,698	14,111	413
	¥ 88,242	¥ 152,008	¥ 63,766

	Thousands of U.S. dollars		
	Cost	Market value	Difference
March 31, 2006:			
Equities	\$ 705,069	\$ 1,736,132	\$ 1,031,063
Government, corporate and other bonds	1,282	1,350	68
Other	117,257	132,254	14,997
	\$ 823,608	\$ 1,869,736	\$ 1,046,128

Notes to Consolidated Financial Statements

Daiwa Securities Group Inc.

Three years ended March 31, 2006, 2005 and 2004

Securities for which a market value is not readily available as of March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Equities	¥ 245,399	¥ 53,210	\$ 2,097,432
Government, corporate and other bonds	349	501	2,982
Investments in limited partnerships	132,751	84,622	1,134,622
Other	22,631	19,065	193,427
	¥ 401,130	¥ 157,398	\$ 3,428,463

In addition to the above, equity securities of non-consolidated and affiliated companies amounting to ¥26,334 million (\$225,076 thousand) at March 31, 2006 and ¥24,217 million at March 31,

2005, respectively, were included in "Investment securities" in the accompanying consolidated balance sheets.

7. Derivatives for non-trading purposes

Net unrealized gains (losses) of derivatives for non-trading purposes at March 31, 2006 and 2005 (excluding hedging transactions) consisted of the followings:

	Millions of yen		
	Contract amount	Market value	Unrealized gains (losses)
March 31, 2006:			
Currency swap	¥ 11,289	¥ 17	¥ 17
Foreign exchange forward	801	24	24

March 31, 2005:

Currency swap	¥ 11,237	¥ 1	¥ 1
Foreign exchange forward	52	(0)	(0)

	Thousands of U.S. dollars		
	Contract amount	Market value	Unrealized gains
March 31, 2006:			
Currency swap	\$ 96,489	\$ 146	\$ 147
Foreign exchange forward	6,843	201	201

8. Risk management information concerning trading transactions

The two domestic securities subsidiaries, Daiwa Securities and Daiwa Securities SMBC (“Securities subsidiaries”), enter into transactions involving trading assets and liabilities to meet customer needs, and for their proprietary trading activities, as a broker and an end-user. These trading assets and liabilities include (1) shares 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. As to market risk,

Daiwa Securities SMBC determines the balance of risk and profit or loss on each instrument and uses a value-at-risk method to manage this risk. Credit risk represents the potential for loss arising from the failure of the counter-party in a transaction to fulfill its terms and conditions. Securities subsidiaries assess the credit risk of their counter-parties applying internal credit rating and monitor their exposure by measuring notional principal and credit exposure.

Daiwa Securities SMBC has established five risk management policies: Active management participation, system of internal supervision, sound management by risk limit setting, risk management assuming emergency, and transparency in risk management process. By ensuring these five policies, Daiwa Securities SMBC expects that risks associated with trading activities are well controlled within a range of risk that the management is willing to assume.

9. Pledged assets

At March 31, 2006, short-term borrowings amounting to ¥1,045,300 million (\$8,934,188 thousand) and payables related to margin transactions amounting to ¥7,570 million (\$64,701

thousand) and long-term debt amounting to ¥30 million (\$256 thousand) were secured by the following assets:

	Millions of yen	Thousands of U.S. dollars
Loans receivable from other than customers	¥ 42,633	\$ 364,385
Trading assets	997,506	8,525,690
Private equity and other securities	24	205
Investment securities	99,672	851,896
Other assets – other	3,457	29,547
	¥ 1,143,292	\$ 9,771,723

In addition to above, securities borrowed amounting to ¥384,371 million (\$3,285,226 thousand) were pledged as guarantee at March 31, 2006.

Total fair value of the securities pledged as collateral at March 31, 2006 consisted of the following:

	Millions of yen	Thousands of U.S. dollars
Securities loaned	¥ 5,613,009	\$ 47,974,438
Other	932,368	7,968,961
	¥ 6,545,377	\$ 55,943,399

Total fair value of the securities received as collateral at March 31, 2006 consisted of the following:

	Millions of yen	Thousands of U.S. dollars
Securities borrowed	¥ 8,251,239	\$ 70,523,407
Other	578,268	4,942,464
	¥ 8,829,507	\$ 75,465,871

Notes to Consolidated Financial Statements

Daiwa Securities Group Inc.

Three years ended March 31, 2006, 2005 and 2004

10. Lease transactions

Financial leases, whose ownership does not transfer to the lessee at the end of the lease term are not capitalized and are accounted for in the same manner as operating leases. Certain infor-

mation concerning such non-capitalized finance leases and operating leases at March 31, 2006 and 2005 is summarized as follows:

Lessee:	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Non-capitalized finance leases:			
Total assets under non-capitalized finance leases	¥ 7,685	¥ 9,573	\$ 65,682
Accumulated depreciation	4,584	4,869	39,180
Future lease payments in respect of non-capitalized leases	3,181	4,791	27,190
Due within one year	1,501	1,807	12,826
Operating leases:			
Future lease payments in respect of operating leases	¥ 9,000	¥ 11,284	\$ 76,923
Due within one year	1,999	1,922	17,086
		Millions of yen	Thousands of U.S. dollars
Lessor:			
	2006	2005	2006
Operating leases:			
Future lease receipts in respect of operating leases	¥ 1,803	¥ 1,105	\$ 15,409
Due within one year	387	233	3,309

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11. Payables to customers and counterparties

Payables to customers and counterparties at March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Cash received for customers' accounts	¥ 131,335	¥ 92,574	\$ 1,122,522
Cash deposits received from customers	99,225	53,303	848,075
Other	20,205	142,811	172,694
	¥ 250,765	¥ 288,688	\$ 2,143,291

12. Bank borrowings and long-term debt

As is customary in Japan, in the case of unsecured bank borrowings, security must be given under certain conditions if requested by a lending bank. The bank has the right to offset cash deposited by the borrower against any debt or obligation that

becomes due, and in the case of default and certain other specified events, against all debts payable to the bank. No such request has been made and no such right has been exercised.

Long-term debt at March 31, 2006 and 2005 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Bond payable in yen: 1.4% due 2005	¥ —	¥ 100,000	\$ —
Bond payable in yen: 0.95% due 2008	120,000	120,000	1,025,641
Bond payable in yen: 1.3% due 2011	70,000	—	598,291
Bond payable in yen: 2.08% due 2016	30,000	—	256,410
Convertible bond payable in yen, convertible into common stock at ¥1,094.00 per share: 0.5% due 2006	79,193	79,986	676,863
Euro medium-term notes issued by the Company and the domestic consolidated subsidiary with various rates and maturities through 2035	677,159	569,429	5,787,686
Euro medium-term notes issued by overseas consolidated subsidiaries with various rates and maturities through 2007	2,608	6,108	22,290
Yen subordinated loan due 2006	82,000	20,000	700,855
Borrowings	85,952	54,195	734,631
	¥ 1,146,912	¥ 949,718	\$ 9,802,667

The conversion price and exercise price shown above are subject to adjustment in certain circumstances.

The aggregate annual maturities of long-term debt as of March 31, 2006 are as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars
2007	¥ 159,401	\$ 1,362,399
2008	56,391	481,972
2009	144,522	1,235,236
2010	7,436	63,555
2011	119,691	1,022,998
2012 and thereafter	659,471	5,636,507
	¥ 1,146,912	\$ 9,802,667

Daiwa has unused commitment line amounting to ¥85,106 million (\$727,398 thousand) under agreements with several banks at March 31, 2006.

13. Retirement benefits

Retirement benefits for employees

Retirement benefit plans for eligible employees are discussed below:

- **Unfunded plan**

The Company and most of domestic consolidated subsidiaries provide an unfunded defined contribution plan to their employees in return for services rendered each year, where the amount to be contributed to the individual employee's account is defined by the plan. Contributions by the Company and most of domestic consolidated subsidiaries under the unfunded defined contribu-

tion plan are accumulated on an annual basis and earn a guaranteed hypothetical return at a rate predetermined by the Company and most of domestic consolidated subsidiaries each year. Accumulated contribution plus interest to this unfunded plan are included in "Retirement benefits" in the consolidated balance sheets as of March 31, 2006 and 2005, in the amount of ¥17,980 million (\$153,672 thousand) and ¥16,121 million, respectively. Benefit expenses recorded in the consolidated statements of operations for the years ended March 31, 2006, 2005 and 2004 were ¥2,864 million (\$24,481 thousand), ¥2,946 million and ¥3,278 million, respectively.

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• Closed funded plan

The Company and domestic consolidated subsidiaries closed their defined benefit plan as of April 1, 1999 and accordingly, no new employees have been added to the plan and no service cost has been charged for the plan. The effect on the consolidated financial statements was immaterial.

Retirement benefits for directors

Directors' retirement benefits in consolidated subsidiaries of ¥383 million (\$3,275 thousand) and ¥1,100 million are included in "Retirement benefits" in the accompanying consolidated balance sheets as of March 31, 2006 and 2005, respectively. Benefit expenses recorded in the consolidated statements of operations for the years ended March 31, 2006, 2005 and 2004 were ¥174 million (\$1,487 thousand), ¥439 million and ¥368 million, respectively.

The board of the Company resolved to abolish the retirement gratuities system for retiring directors in May 2004. In June 2004, the shareholders' meeting of the Company approved the payments of retirement allowance to directors who were nominated

for re-election. The payments will be made in accordance with standards prescribed by the Company and service rendered to the Company during their respective terms of office up to the end of the shareholders' meeting. The payments will be made at the time of their respective retirements from the Board of Directors.

The board of certain consolidated subsidiaries resolved to abolish the retirement gratuities system for retiring directors in March 2005. In June 2005, the shareholders' meetings of such consolidated subsidiaries approved the payments of retirement allowance to directors who were nominated for reelection. The payments will be made in accordance with standards prescribed by consolidated subsidiaries and service rendered to consolidated subsidiaries during their respective terms of office up to the end of the shareholders' meetings. The payments will be made at the time of their respective retirements from the Board of Directors. In consequence, consolidated subsidiaries' directors' retirement benefits of ¥437 million (\$3,743 thousand) were reclassified from "Retirement benefits" to "Payables: Other" in the accompanying consolidated balance sheet as of March 31, 2006.

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14. Income taxes

The Company and domestic consolidated subsidiaries are subject to a number of taxes levied on income. The compounded statutory tax rate in Japan were approximately 40.7%, 40.7% and 42.1% for the years ended March 31, 2006, 2005 and 2004, respectively.

After the clarification of the local tax law, the new tax rate for the year beginning on April 1, 2004 was finalized at approximately 40.7%. Taking into account the finalized income tax rates, the Company and domestic consolidated subsidiaries used the tax

rates of approximately 40.7% for current and non-current items at March 31, 2004 for the calculation of deferred tax assets and liabilities. Due to the change in the tax rates, "Deferred tax assets" increased by ¥158 million and "Income taxes: Deferred" and "Net unrealized gain on securities, net of tax effect", decreased by ¥260 million and ¥101 million, respectively, compared with what would have been recorded under the previous local tax law.

Overseas consolidated subsidiaries are subject to income taxes of the countries in which they operate.

Details of deferred tax assets and liabilities at March 31, 2006 and 2005 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Deferred tax assets:			
Net operating losses carried-forward	¥ 25,656	¥ 46,059	\$ 219,284
Write-down of investment securities	10,637	13,232	90,912
Temporary difference of investment in consolidated subsidiaries	—	51,979	—
Expenses for real estate business reorganization	—	913	—
Employees' retirement benefits	8,026	8,231	68,603
Employees' compensation and bonuses	15,278	7,931	130,584
Provision for doubtful accounts	2,423	4,406	20,707
Impairment losses on fixed assets	7,248	—	61,948
Enterprise tax payable	8,338	—	71,261
Allowance for possible investment losses	5,426	—	46,373
Other	10,308	21,347	88,106
Gross deferred tax assets	93,340	154,098	797,778
Less: Valuation allowance	(51,824)	(107,348)	(442,937)
Total deferred tax assets	41,516	46,750	354,841
Deferred tax liabilities	53,935	32,011	460,986
Net deferred tax assets (liabilities)	¥ (12,419)	14,739	\$ (106,145)

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The Company and certain consolidated subsidiaries provided valuation allowance to reflect the estimated unrealized amount of gross deferred tax assets.

A reconciliation of the difference between the statutory income tax rate and the effective income tax rate reflected in the consolidated statements of operations for the years ended March 31, 2006, 2005 and 2004 were as follows:

	2006	2005	2004
Japanese statutory income tax rate	40.7%	40.7%	42.1%
Valuation allowance	(9.0)	(7.0)	(12.5)
Permanent difference (Non-deductible)	0.3	1.2	1.3
Permanent difference (Non-taxable)	(0.3)	(0.6)	(0.9)
Lower tax rate applicable to income of overseas consolidated subsidiaries	(0.6)	(0.8)	(1.7)
Adjustment of unrealized intercompany profit	0.6	3.8	—
Other, net	(1.5)	(1.6)	(1.2)
Effective income tax rate	30.2%	35.7%	27.1%

15. Statutory reserves

The Securities and Exchange Law of Japan requires a securities company to set aside a reserve in proportion to its securities transactions and other related trading to cover possible customer losses incurred by default of the securities company on securities transactions.

16. Contingent liabilities

At March 31, 2006, Daiwa had contingent liabilities amounting to ¥2,507 million (\$21,427 thousand), mainly arising as guarantors of employees' borrowings.

17. Shareholders' equity

In principle, the Commercial Code of Japan ("Code") requires a company to credit entire amount of issued shares to common stock (and preferred stock, if any); however, a company may classify the amount not exceeding one-half of the entire issued amount of shares as additional paid-in capital, which is included in capital surplus with a resolution of the Board of Directors.

According to the Code, a company should save 10% of cash dividends and other cash appropriated as legal earnings reserve until its amount together with capital surplus become up to one quarter of common stock (and preferred stock, if any). The legal earnings reserve is allowed to eliminate or reduce a deficit with a resolution of the shareholders' meeting or may be capitalized with a resolution of the Board of Directors. The excess amount of legal earnings reserve of one quarter of capital requirement is available for appropriation with a resolution of shareholders' meeting. The legal earnings reserve is included in retained earnings in the accompanying consolidated balance sheets.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Code. The total amount of retained earnings available for dividends in the Company's statutory book of account as of March 31, 2006 amounted to ¥254,294 million (\$2,173,454 thousand).

The Article 293-5 of the Code permits a company to distribute profits by way of interim dividends if the articles of incorporation of a company so provide. The Company's articles of incorporation were amended by the resolution at the shareholders' meeting held on June 23, 2004 in order to permit the Company to implement interim dividends. Interim cash dividends of ¥12 (\$0.10) per share amounting to ¥15,967 million (\$136,467

thousand) were approved by the Board of Directors held on October 28, 2005. Using the newly introduced committee system, the Board of Directors is to determine the year-end dividends. Year-end cash dividends of ¥22 (\$0.19) per share amounting to ¥29,065 million (\$248,426 thousand) were approved by the Board of Directors held on May 18, 2006.

The shareholders of the Company approved a stock incentive plan on June 23, 2004. The plan provides for the issuance of up to 4,500 thousand shares in the form of options to directors and key employees. The options may be exercised during the period from July 1, 2006 until August 31, 2011, and the exercise price is determined at the grant date. On the same day, the shareholders' meeting of the Company approved a change in the articles of incorporation so that the Company may be entitled to repurchase its shares by the resolution of its Board of Directors.

The each shareholders of the Company on June 24, 2005 and June 24, 2006 approved a stock incentive plan. There are two kinds of stock subscription rights as stock options to directors, executive officers and employees. The first is the stock subscription rights that were issued free to directors and executive officers of the Company and subsidiaries, and the amount paid in upon exercise of such subscription rights is ¥1 per share. The second is the stock subscription rights that shall be issued to employees of the Company, and of affiliated companies, and to directors and executive officers of the Company's affiliated companies, excluding the persons to whom the first stock subscription rights were issued. The amount paid in upon exercise of such subscription rights shall be determined based on the market price of the Company's common stock at the time of the issuance of such subscription rights.

18. Capital adequacy requirements

In Japan, a securities company is subject to risk-based capital adequacy rules established and administered by the Financial Services Agency. Securities subsidiaries report their capital adequacy ratio as defined pursuant to these rules. The authorities will take certain administrative measures if such ratio declines below

140%. Capital adequacy ratios of Daiwa Securities were 323.6% (unaudited) and 351.3% (unaudited) for March 31, 2006 and 2005, respectively, and those of Daiwa Securities SMBC were 336.3% (unaudited) and 355.6% (unaudited) for March 31, 2006 and 2005, respectively.

19. Segment information

Daiwa operates predominantly in a single industry segment. Daiwa primary business activities include (1) trading in securities and derivatives, (2) brokerage of securities and derivatives, (3) underwriting and distribution of securities, (4) other business related to securities transactions and (5) private offering of securities.

A summary of revenues by geographic area for the years ended March 31, 2006, 2005 and 2004 and a summary of total assets by geographic area at March 31, 2006 and 2005 were as follows:

	Millions of yen					
	Japan	America	Europe	Asia & Oceania	Elimination or unallocated	Consolidated
Year ended March 31, 2006:						
Net operating revenues:						
Outside customer	¥ 541,666	¥ 5,528	¥ 21,673	¥ 10,492	¥ —	¥ 579,359
Inter-segment	1,530	8,758	12,085	1,606	(23,979)	—
Total	543,196	14,286	33,758	12,098	(23,979)	579,359
Selling, general and administrative expenses	294,984	11,920	23,679	8,472	(13,856)	325,199
Operating income	¥ 248,212	¥ 2,366	¥ 10,079	¥ 3,626	¥ (10,123)	¥ 254,160
At March 31, 2006:						
Total assets by geographic area	¥ 12,239,342	¥ 2,807,087	¥ 1,145,934	¥ 72,881	¥ (1,366,353)	¥ 14,898,891
Year ended March 31, 2005:						
Net operating revenues:						
Outside customer	¥ 353,827	¥ 3,971	¥ 25,378	¥ 7,256	¥ —	¥ 390,432
Inter-segment	(2,370)	6,641	5,027	1,278	(10,576)	—
Total	351,457	10,612	30,405	8,534	(10,576)	390,432
Selling, general and administrative expenses	244,543	10,595	24,203	6,781	(10,578)	275,544
Operating income	¥ 106,914	¥ 17	¥ 6,202	¥ 1,753	¥ 2	¥ 114,888
At March 31, 2005:						
Total assets by geographic area	¥ 10,078,853	¥ 2,098,376	¥ 811,192	¥ 62,560	¥ (672,019)	¥ 12,378,962
Year ended March 31, 2004:						
Net operating revenues:						
Outside customer	¥ 314,190	¥ 7,749	¥ 23,956	¥ 6,540	¥ —	¥ 352,435
Inter-segment	1,389	3,468	3,413	1,132	(9,402)	—
Total	315,579	11,217	27,369	7,672	(9,402)	352,435
Selling, general and administrative expenses	232,269	10,197	20,413	6,111	(9,075)	259,915
Operating income	¥ 83,310	¥ 1,020	¥ 6,956	¥ 1,561	¥ (327)	¥ 92,520

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Thousands of U.S. dollars

	Japan	America	Europe	Asia & Oceania	Elimination or unallocated	Consolidated
Year ended March 31, 2006:						
Net operating revenues:						
Outside customer	\$ 4,629,626	\$ 47,248	\$ 185,236	\$ 89,677	\$ —	\$ 4,951,787
Inter-segment	13,073	74,859	103,296	13,721	(204,949)	—
Total	4,642,699	122,107	288,532	103,398	(204,949)	4,951,787
Selling, general and administrative expenses	2,521,232	101,882	202,387	72,411	(118,433)	2,779,479
Operating income	\$ 2,121,467	\$ 20,225	\$ 86,145	\$ 30,987	\$ (86,516)	\$ 2,172,308
At March 31, 2006:						
Total assets by geographic area	\$ 104,609,759	\$ 23,992,195	\$ 9,794,307	\$ 622,914	\$ (11,678,226)	\$ 127,340,949

Geographic overseas revenues for the years ended March 31, 2006, 2005 and 2004 were as follows:

Millions of yen

	America	Europe	Asia & Oceania	Total
Year ended March 31, 2006:				
Overseas revenue	¥ 10,313	¥ 19,370	¥ 11,016	¥ 40,699
Net operating revenues				579,359
% of Net operating revenues	1.8%	3.3%	1.9%	7.0%
Year ended March 31, 2005:				
Overseas revenue	¥ 8,552	¥ 21,149	¥ 8,890	¥ 38,591
Net operating revenues				390,432
% of Net operating revenues	2.2%	5.4%	2.3%	9.9%
Year ended March 31, 2004:				
Overseas revenue	¥ 10,945	¥ 20,353	¥ 8,249	¥ 39,547
Net operating revenues				352,435
% of Net operating revenues	3.1%	5.8%	2.3%	11.2%

Thousands of U.S. dollars

	America	Europe	Asia & Oceania	Total
Year ended March 31, 2006:				
Overseas revenue	\$ 88,143	\$ 165,556	\$ 94,151	\$ 347,850
Net operating revenues				4,951,787
% of Net operating revenues	1.8%	3.3%	1.9%	7.0%

20. Commissions

Commissions derived from each department for the years ended March 31, 2006, 2005 and 2004 were as follows:

										Millions of yen					
										Total					
										Equity	Fixed income (Bond)	Investment trust	Investment banking	Others	Total
Year ended March 31, 2006:															
Brokerage	¥	118,262	¥	923	¥	336	¥	—	¥	—	¥	119,521			
Underwriting		—		—		—		64,314		—		64,314			
Distribution		—		—		41,799		2,032		—		43,831			
Other		1,955		2,279		40,269		16,389		20,631		81,523			
	¥	120,217	¥	3,202	¥	82,404	¥	82,735	¥	20,631	¥	309,189			
Year ended March 31, 2005:															
Brokerage	¥	81,919	¥	1,464	¥	159	¥	—	¥	—	¥	83,542			
Underwriting		—		—		—		54,744		—		54,744			
Distribution		—		—		19,688		3,598		—		23,286			
Other		1,968		2,800		25,793		12,828		11,426		54,815			
	¥	83,887	¥	4,264	¥	45,640	¥	71,170	¥	11,426	¥	216,387			
Year ended March 31, 2004:															
Brokerage	¥	78,194	¥	1,242	¥	209	¥	—	¥	—	¥	79,645			
Underwriting		—		—		—		46,094		—		46,094			
Distribution		—		—		21,904		1,662		—		23,566			
Other		1,867		3,977		20,933		8,049		10,032		44,858			
	¥	80,061	¥	5,219	¥	43,046	¥	55,805	¥	10,032	¥	194,163			

										Thousands of U.S. dollars					
										Total					
										Equity	Fixed income (Bond)	Investment trust	Investment banking	Others	Total
Year ended March 31, 2006:															
Brokerage	\$	1,010,782	\$	7,891	\$	2,874	\$	—	\$	—	\$	1,021,547			
Underwriting		—		—		—		549,691		—		549,691			
Distribution		—		—		357,254		17,367		—		374,621			
Other		16,713		19,478		344,177		140,080		176,334		696,782			
	\$	1,027,495	\$	27,369	\$	704,305	\$	707,138	\$	176,334	\$	2,642,641			

21. Net gain on trading

Net gain on trading for the years ended March 31, 2006, 2005 and 2004 were as follows:

										Millions of yen	Thousands of U.S. dollars		
										2006	2005	2004	2006
Stock and other	¥	124,271	¥	56,105	¥	50,024					\$	1,062,145	
Bond, forex and other		100,641		95,013		70,171						860,180	
(Bond and other)		(39,026)		(62,407)		(47,267)						(333,554)	
(Forex and other)		(61,615)		(32,606)		(22,904)						(526,626)	
	¥	224,912	¥	151,118	¥	120,195					\$	1,922,325	

Notes to Consolidated Financial Statements

Daiwa Securities Group Inc.

Three years ended March 31, 2006, 2005 and 2004

22. Selling, general and administrative expenses

Major components of selling, general and administrative expenses for the years ended March 31, 2006, 2005 and 2004 were summarized as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2005	2004	2006
Employees' compensation and benefits	¥ 171,062	¥ 142,751	¥ 136,964	\$ 1,462,067
Commissions and brokerage	31,508	19,607	14,573	269,298
Communications	18,646	18,174	17,444	159,371
Occupancy and rental	32,659	32,697	32,519	279,138
Data processing and office supplies	17,273	16,805	14,899	147,636
Taxes other than income taxes	8,072	6,756	5,617	68,991
Depreciation and amortization	22,641	22,129	21,530	193,510
Other	23,338	16,625	16,369	199,468
	¥ 325,199	¥ 275,544	¥ 259,915	\$ 2,779,479

23. Other income (expenses)

Details of "Other, net" in the accompanying consolidated statements of operations for the years ended March 31, 2006, 2005 and 2004 were as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2005	2004	2006
Gains on sales of investment securities	¥ 10,030	¥ 5,559	¥ 6,704	\$ 85,728
Write-down of investment securities	(499)	(3,472)	(2,691)	(4,265)
Valuation losses on fixed assets	—	(114)	(58)	—
Gains or losses on sale or disposal of fixed assets	(548)	465	(159)	(4,687)
Losses on sales of loans receivable	—	(7,595)	(557)	—
Reversal of stock purchase warrant	—	502	—	—
Multiemployer pension plan settlement cost in consolidated subsidiaries	—	(188)	—	—
Provision for doubtful accounts	—	(1,639)	(648)	—
Equity in earnings of affiliates	1,528	1,894	90	13,064
Impairment losses on fixed assets	(6,851)	—	(12,797)	(58,554)
Losses on liquidation of affiliates	—	(51)	(4,221)	—
Expenses related to merger, integration or relocation of branches	—	—	(2,473)	—
Expenses for reorganization of overseas banking subsidiary	—	(779)	(595)	—
Gain on charge in stake in subsidiary	4,725	—	—	40,388
Contribution to the Securities Market Infrastructure Improvement Fund	(200)	—	—	(1,709)
Loss on litigation settlement	(1,279)	—	—	(10,933)
Foreign exchange loss from overseas subsidiary capital reduction	(1,564)	—	—	(13,364)
Extraordinary depreciation	(4,439)	—	—	(37,941)
Other	4,667	3,651	3,052	39,880
	¥ 5,570	¥ (1,767)	¥ (14,353)	\$ 47,607

For the purpose of identifying impairment of fixed assets, the Company and domestic consolidated subsidiaries grouped their fixed assets principally according to the unit on which decisions for investment are made. The recoverability of book values of the fixed assets was evaluated for each asset group. As a result, fixed assets listed below were identified as being impaired and their book values were reduced to their estimated recoverable amounts. The breakdown of impairment losses recognized in the year ended March 31, 2006, 2005 and 2004 were as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2005	2004	2006
Fixed assets to be held and used	¥ 6,201	¥ —	¥ 9,103	\$ 53,000
Fixed assets to be disposed of by sale	650	—	3,694	5,553
Total	¥ 6,851	¥ —	¥ 12,797	\$ 58,554

The book values of fixed assets to be held and used were reduced to their estimated recoverable amounts based on mainly the present values of expected cash flows using the discount rates of 5% to 8%.

The book values of fixed assets to be disposed of by a sale were reduced to net realizable values based on mainly publicly-assessed values.

24. Subsequent events

Stock incentive plan — The shareholders of the Company approved the issuance of the stock subscription rights as stock options on June 24, 2006. In accordance with Articles 236, 238 and 239 of the Corporation Law, the stock subscription rights were issued free to directors and executive officers of the Company and subsidiaries, and the amount paid in upon exercise of such subscription rights is ¥1 per share.

Independent Auditors' Report



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

We have audited the accompanying consolidated balance sheets of Daiwa Securities Group Inc. and consolidated subsidiaries as of March 31, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended March 31, 2006, 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 audits.

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

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In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Daiwa Securities Group Inc. and subsidiaries as of March 31, 2006 and 2005, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2006, in conformity with accounting principles generally accepted in Japan.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2006 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1 to the consolidated financial statements.

KPMG AZSA & Co.

Tokyo, Japan

June 26, 2006