AOZORA BANK, LTD.

AOZORA

2004

AOZORA BANK, LTD.
Annual Report
Year Ended March 31, 2004

Profile

In January 2001, the Bank changed its name to Aozora Bank, Ltd. Cerberus NCB Acquisition, L.P., became the majority shareholder of the Bank in September 2003. Mr. Edward G. Harshfield was appointed the new Chairman at that time, and Mr. Hirokazu Mizukami was appointed President in December 2003. Further outside appointments to senior positions within the Bank have been made during 2004. In April 2004, a new organizational structure was implemented to improve customer focus within each of the Bank's business groups and to facilitate product development and business growth.

Under the new organizational structure, the Bank will reduce the time to market for an enhanced product range that enables its customers to achieve their business goals.

The Bank has expanded into diversified markets and products to improve the amount and quality of earnings, while maintaining sound and transparent management and corporate governance systems.

AOZORA

Established .... April 1957

Capital stock .... ¥419.8 billion

Total assets .... ¥5,188.1 billion

Consolidated capital adequacy ratio (domestic standard) 15.66%

Number of employees (Bank only) 1,345

Branch network .... Japan: 18 branches
Overseas: 3 representative offices

Head office .... 3-1, Kudan-minami 1-chome, Chiyoda-ku, Tokyo 102-8660, Japan

Note: Branch network is as of July 20, 2004.

Long-Term Credit Ratings

JCR	A–
R&I	BBB+
Moody's	Baa1
Standard & Poor's	BBB–
Fitch Ratings	BBB–

(As of March 31, 2004)

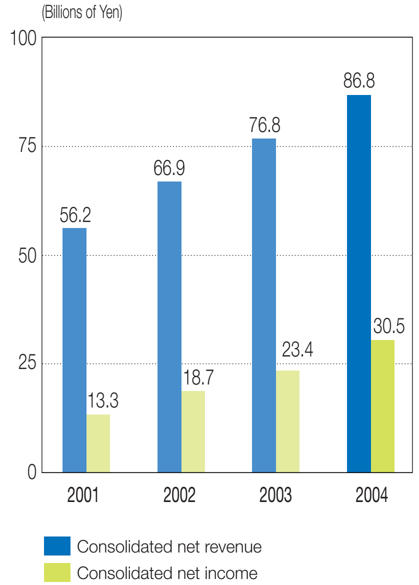
Note: In this annual report, yen amounts stated in millions of yen have been truncated. Amounts expressed in billions of yen have been rounded to the nearest ¥0.1 billion.

Contents

Financial Highlights

Earnings Growth

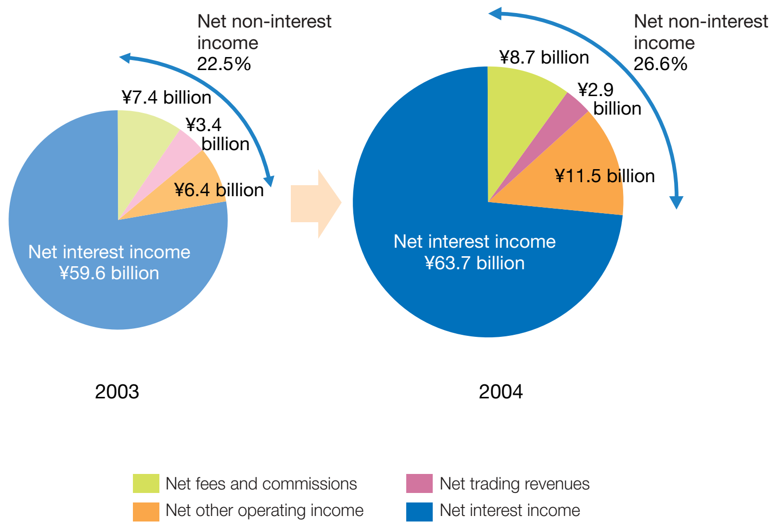
(Years Ended March 31)



Note: Consolidated net income for the fiscal year ended March 31, 2001, excludes a one-off ¥85.0 billion gain on sales of equity securities.

Earnings Quality Continues to Improve

(Years Ended March 31)



Consolidated

(Millions of Yen)

	2004	2003	2002	2001
Operating income (Note 1)	113,788	109,748	106,700	275,730
Ordinary profit (Note 1)	7,606	8,920	14,355	99,116
Net income (Note 1)	30,530	23,376	18,703	98,331
Capital stock	419,781	419,781	419,781	419,781
Total stockholders' equity	526,848	497,514	477,046	460,876
Total assets	5,176,005	5,885,642	5,684,072	6,163,766
Debentures	1,054,973	1,470,126	1,468,193	2,479,408
Deposits (Note 2)	2,588,030	2,537,175	2,164,641	1,771,373
Loans and bills discounted	2,965,552	3,258,693	3,297,993	3,089,490
Securities	964,964	1,350,036	1,054,019	721,477
Basic net income per share (yen) (Note 1)	9.54	7.02	5.37	35.80
Total stockholders' equity per share (yen)	85.63	75.29	68.07	62.36
Consolidated capital adequacy ratio (domestic standard)	15.66%	13.30%	14.05%	15.13%
Tier I ratio (domestic standard)	15.01%	12.51%	12.88%	13.36%
Return on equity (ROE) (Note 3)	11.86%	9.79%	8.24%	42.55%

Notes: 1. In the fiscal year ended March 31, 2001, operating income, ordinary profit and net income included a one-off ¥85.0 billion gain on sales of equity securities, carried out as a measure to strengthen the Bank's capital base when it returned to private ownership.

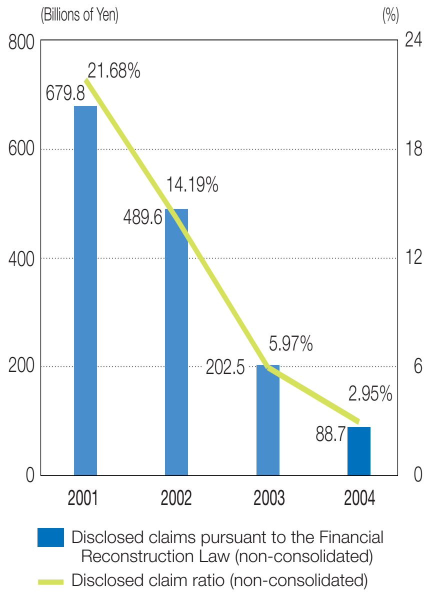
2. Includes negotiable certificates of deposit (NCDs)

3. ROE = $$\frac{\text{(Net income – Dividends paid on preferred stock)}}{\left\{\left(\begin{matrix}\text{Total stockholders' equity}\\ \text{at beginning of term}\end{matrix} - \begin{matrix}\text{Number of preferred shares}\\ \text{outstanding at beginning of term}\end{matrix} \times \begin{matrix}\text{Issue}\\ \text{price}\end{matrix}\right) + \left(\begin{matrix}\text{Total stockholders' equity}\\ \text{at end of term}\end{matrix} - \begin{matrix}\text{Number of preferred shares}\\ \text{outstanding at end of term}\end{matrix} \times \begin{matrix}\text{Issue}\\ \text{price}\end{matrix}\right)\right\} \div 2} \times 100$$

For the fiscal year ended March 31, 2001, no adjustments were made relating to preferred shares as total stockholders' equity at beginning of term was nil (¥0).

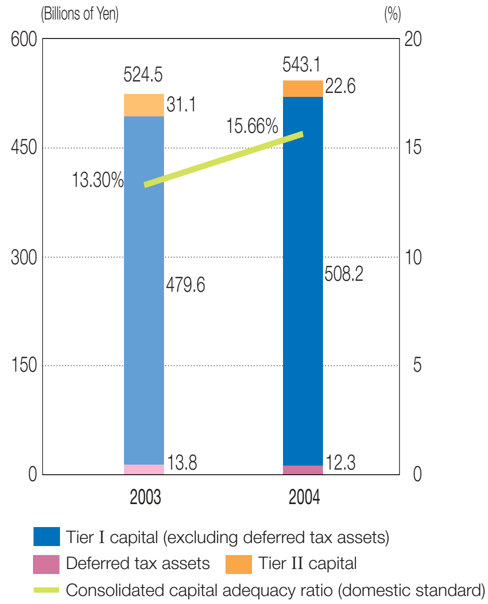
Credit Quality Continues to Improve

(At March 31)



Strong Capital Base

(At March 31)



Non-Consolidated

(Millions of Yen)

	2004	2003	2002	2001
Operating income (Note 1)	105,335	101,633	100,984	270,720
Business profit before general loan-loss reserve	42,463	33,479	25,925	16,795
Ordinary profit (Note 1)	7,309	7,437	13,706	98,971
Net income (Note 1)	31,854	22,875	18,563	99,690
Capital stock	419,781	419,781	419,781	419,781
Total stockholders' equity	527,582	496,918	476,166	459,690
Total assets	5,188,071	5,895,314	5,687,366	6,174,922
Debentures	1,058,973	1,473,126	1,470,193	2,472,528
Deposits (Note 2)	2,607,081	2,555,905	2,177,240	1,778,939
Loans and bills discounted	2,969,770	3,271,087	3,304,379	3,092,049
Securities	971,763	1,356,754	1,060,690	727,758
Net income per share (yen) (Note 1)	10.01	6.84	5.32	36.31
Total stockholders' equity per share (yen)	85.89	75.08	67.76	61.94
Capital adequacy ratio (domestic standard)	15.65%	13.26%	14.00%	15.10%
Tier I ratio (domestic standard)	14.99%	12.47%	12.83%	13.32%
Return on equity (ROE) (Note 3)	12.44%	9.58%	8.21%	43.37%

Notes: 1. In the fiscal year ended March 31, 2001, operating income, ordinary profit and net income included a one-off ¥85.0 billion gain on sales of equity securities, carried out as a measure to strengthen the Bank's capital base when it returned to private ownership.

2. Includes negotiable certificates of deposit (NCDs)

3. $$\text{ROE} = \frac{\text{(Net income – Dividends paid on preferred stock)}}{\left\{\left(\begin{array}{c}\text{Total stockholders' equity}\\\text{at beginning of term}\end{array} - \begin{array}{c}\text{Number of preferred shares}\\\text{outstanding at beginning of term}\end{array} \times \begin{array}{c}\text{Issue}\\\text{price}\end{array}\right) + \left(\begin{array}{c}\text{Total stockholders' equity}\\\text{at end of term}\end{array} - \begin{array}{c}\text{Number of preferred shares}\\\text{outstanding at end of term}\end{array} \times \begin{array}{c}\text{Issue}\\\text{price}\end{array}\right)\right\} \div 2} \times 100$$

For the fiscal year ended March 31, 2001, no adjustments were made relating to preferred shares as total stockholders' equity at beginning of term was nil (¥0).

Joint Message from the Chairman and President

Mr. Hirokazu Mizukami, *President,* and Mr. Edward G. Harshfield, *Chairman*

We were honored to assume the leadership of Aozora Bank during the past year, a year of consolidation, change and strong financial performance. In September 2003, Cerberus NCB Aqcuisition, a U.S.-based investment group became the majority shareholder of the Bank. Subsequently, we were appointed to the senior management positions of the Bank. Since then, we have focused on the development and implementation of strategic plans for the Bank in order to ensure the achievement of a position of sustainable competitive advantage and superior performance. To achieve this, our priority is to understand and service the requirements of customers, while simultaneously addressing the needs and requirements of our regulators, shareholders and staff. We believe that Aozora Bank can continue to grow by utilizing its strong capital, funding and liquidity positions to enhance the development and delivery of new products for existing and new customers and markets. We are excited by the opportunities presented to Aozora Bank to grow, prosper and regain its position as a leading Japanese financial institution and are pleased to present the annual report for the fiscal year ended March 31, 2004, which reflects the Bank's continuing ability to achieve its targeted level of performance. We would also like to take this opportunity to thank our customers, staff and shareholders for their continuing strong support in achieving the results of which Aozora is capable.

Non-Consolidated Performance in the Fiscal Year Ended March 31, 2004

Income before income taxes increases 60.9%

Income before income taxes for the period was ¥31.2 billion, an increase of 60.9% over the previous fiscal year, while net income of ¥31.9 billion exceeded the target in the Business Revitalization Plan and was 39.3% higher than the previous fiscal year.

Net revenue increases 13.1%, net non-interest income up 48.4%

Net revenue for the period increased 13.1% from the previous fiscal year, to ¥81.6 billion. Within this amount, net non-interest income increased 48.4%, to ¥18.9 billion, thus broadening the revenue base and improving the overall quality of income. General and administrative expenses increased just 1.2% from the previous fiscal year reflecting tight cost control measures. The resultant business profit before general loan-loss reserve was up 26.8% from the previous fiscal year, to ¥42.5 billion.

Total credit-related expenses for the period amounted to ¥6.5 billion, compared with a gain of ¥1.4 billion in the previous fiscal year, as more stringent credit analysis and tightened criteria have taken effect. Credit quality continued to improve as evidenced by the reduction in the disclosed claim ratio pursuant to the Financial Reconstruction Law, which fell from 5.97% as at March 31, 2003, to 2.95% as at March 31, 2004. The right to transfer non-performing assets under the put option expired during the period and management is confident that all loans eligible under this arrangement were concluded in a professional manner. Several specific, and now ongoing, reviews of credit quality have been performed internally with the assistance of independent advisors, and management has concluded that the internal credit rating of customers is accurate. Operationally, the internal rating determines both the credit reserve levels as well as the credit and interest rate guidelines for individual customers and groups of related customers. Management is pleased with the progress thus far in managing the loan portfolio toward full compliance with these internal credit and pricing guidelines, while still achieving earnings targets and without unduly disrupting our customers' businesses. Credit concentrations to individual borrowers have been selectively reduced toward guideline levels primarily through mutual agreements with our customers. The reduction of significant concentrations is an important risk management priority, requiring that we work with our customers as much as possible to ensure that their financial needs continue to be met and that the Bank has taken the appropriate level of overall credit risk.

Total assets at the end of the period were ¥5,188.1 billion, down by 12.0% from the previous fiscal year-end. This reflects the progress made in reducing credit risks related to substandard borrowers, borrowers unwilling to meet the internal pricing guidelines or where the Bank has considered concentrations of credit risk to be excessive. In addition, securities investment positions decreased by 28.4%, which reflects management's execution of its plan to reduce interest rate risk. We are pleased that the Bank has been able to increase its earnings and strengthen its capital position, while simultaneously reducing the overall level of such assets and risks.

Total stockholders' equity at the end of the period was ¥527.6 billion, an increase of 6.2% from the end of the previous fiscal year.

The non-consolidated capital adequacy ratio (domestic standard) at the end of the year was 15.65%, including a Tier 1 ratio (domestic standard) of 14.99%, well above the minimum 8% ratio recommended by the Bank for International Settlements (BIS) for banks with international operations, which shows that Aozora Bank has a strong capital position to support future growth. The Tier 1 ratio adjusted for the removal of deferred tax assets was 14.64%.

Management Priorities and Strategy

History of management strategy since privatization

When the Bank was privatized in 2000, a Business Revitalization Plan was developed and approved by the Financial Reconstruction Commission (FRC). The plan prescribed performance targets and operational constraints designed to ensure the Bank's overall success, while safeguarding the government's investment. The Business

Revitalization Plan is an integral part of the management strategy, and we reaffirm our commitment to meet or exceed the performance targets, while operating within FRC agreements.

In April 2003, the Trinity Plan was announced as the Bank's major strategy. This plan's key goals were the re-listing the Bank's shares and the attainment of a credit rating that would place the Bank in the upper echelon of Japanese banks. We reaffirm that we remain broadly committed to these goals.

Current management strategy

We believe that to achieve the goals of the Business Revitalization and Trinity plans we must revitalize the fundamental aspects of the Bank's business, focusing on customers, corporate governance, shareholder returns and staff management.

Customers

We value our institutional, corporate and retail clients of all sizes and are committed to creating and delivering a broad range of financial products that enable our customers to achieve their business goals. We are targeting customers with sound credit standings, growth potential and those who require financial assistance to restructure and revitalize their businesses.

We plan to increase our corporate customer base by creatively expanding our product range and targeting large, medium-sized and small corporations according to their needs. We are seeking to broaden and diversify our credit exposure to the corporate sector by relying less on large loans to individual companies and concentrations in certain sectors. We will increase the number of our corporate customers by expanding our business with small and medium-sized companies. Our enhanced product range will include structured loans, deposits, security and derivative products to enable our client companies to fund their operations, manage their cash and hedge against market fluctuations. We are expanding our current efforts by providing financial assistance for corporate restructurings, mergers and acquisitions, divestitures, management buy-outs, securitization of future cash flows, capital and debt restructuring and asset-backed funds, including real estate investment trusts.

Aozora Bank has a long history of working with other financial institutions in Japan, especially regional banks. We will further develop these relationships by developing products and services as well as partnering with financial institutions to achieve mutually improved performance. We will continue to offer loan and debenture products, but will also work to partner with our financial institution clients to source higher yielding assets, diversify their credit and market risk concentrations and provide liquidity through securitization of their performing and non-performing assets. We are working to help our financial institution clients source products that are attractive to their corporate and retail clients. By strengthening and developing existing relationships with our domestic financial institution customers into strategic business risk-sharing partnerships we will achieve a steady expansion of our client base and create a win-win situation for our customers, their customers and ourselves.

Deposits from retail customers are an important part of our continued financial success and stability. We will continue to provide retail customers with competitive deposit products and improve the ease with which they do business with us through the expansion of telephone banking, automated teller machine (ATM) and Internet banking capabilities. We are also developing other loan, investment and insurance products for our retail customers.

Corporate governance

We are committed to maintaining compliance with the laws and regulations in every jurisdiction in which we operate. We are committed to assessing the impact and likelihood of all types of risk on our business, then designing, implementing and monitoring internal controls to mitigate the impact of those risks.

Shareholders

Creating shareholder value by deploying resources and managing risks to provide sustained superior returns at least equal to the targets defined in the Business Revitalization Plan in the short to medium term, and at global best practice hurdle rates in the long term is a major goal of the Bank. Maximizing shareholder returns by building a sustainable domestic franchise built upon strong, trust-based customer relationships and investing in diversified asset pools with appropriate risk-return ratios are the keys to creating value.

Staff

We are committed to providing our staff with opportunities for career advancement and remuneration that fairly reflect their abilities and contribution to the achievement of the Bank's objectives. We are investing in technology and reviewing all internal processes to eliminate inefficiency and facilitate growth. This should result in an improvement in the quality of work enjoyed by our staff, while allowing them to provide more professional value to the firm.

New Organizational Structure

Management strategies and priorities clearly emphasize the importance of our customers. To these ends, a new organizational structure was established in April 2004. The key features of the new structure are identified below.

Customer-focused business groups with dedicated marketing departments have been created. Financial products have been realigned into the new business groups based upon the target client group for the product. The new business groups are the Corporate Banking Group, the Financial Institution Group, the Retail Banking Group, the Special Finance Group and the Financial Markets Group. The first three of these groups now have dedicated sales, marketing and relationship staff in the branches so that a single business head coordinates the product development and sales activities for each type of customer. We expect this structure to improve the effectiveness and time to market for customer products.

In addition, business support activities have been re-organized under the newly created positions of Chief Financial Officer, Chief Credit Officer and Chief Technology Officer, all of whom report to the Office of the Chief Executive. We have recently recruited external heads for these key roles and expect the combination of relevant external experience (including an understanding of industry best practices and change management), with the high quality of existing staff and managers to transform the internal infrastructure of the Bank. Our objective is to install global best practice policies and processes for all risk management, finance and administrative activities in the Bank. We are developing the technology infrastructure to make the Bank more robust, interactive, flexible and scaleable. Systems and processes are being reviewed and redesigned to reduce risk and to improve quality and productivity.

We believe the reorganization of our business support functions will catalyze our ability to pursue and meet our overall strategic objectives.

In summary, it has been a very busy year for all associated with Aozora Bank. We are sincerely appreciative of the hard work, dedication and thoughtfulness of all our staff and the support of our Board of Directors, shareholders and customers, and we are looking forward to continued improvements in the future.

August 2004

Edward G. Harshfield
Chairman

Hirokazu Mizukami
President

For Corporate Clients

For corporate clients, as well as providing a stable source of funding, Aozora Bank employs a unique problem-solving approach to managing client relationships. The Bank converts assets—built up through its lending, securitization and revitalization business operations—into financial products, and then provides the products and know-how accumulated through that process to its clients, their respective business partners and other investors. Consequently, rather than offering a "one size fits all" service, we provide financing and management solutions optimal to the specific needs of each client.

Providing a Diverse Lineup of Funding and Investment Methods

The Bank has traditionally provided stable funding solutions through its corporate lending activities. In addition to lending, for such purposes as investment in plant and equipment and so on, we offer tailored solutions that draw on a broad lineup of products—including loan syndications and loan/derivative combinations—to meet a diverse range of client needs. As corporate borrowers continue to diversify their funding methods, the Bank has responded by developing and offering optimal financing products and by striving to further enhance its solutions-driven approach.

Loans

In our credit risk assessment process, from a risk-return perspective we not only take into account tangible asset-based collateral but also accurately assess such factors as the client's technical capabilities as well as the originality and competitive advantage of their business model. Through these assessments and by also emphasizing clients' cash flow generating capabilities, we have created a system for working with clients to provide the optimal mix of fund-raising methods.

Loan Syndication

Through syndicated loans, we not only help our clients obtain a new funding source but also help them achieve positive recognition as corporations with a high level of financial management sophistication. As more corporate borrowers diversify their funding sources, Aozora Bank has strengthened its syndicated loan-related services for corporate clients, steadily increasing the number of transactions for which it has acted as lead arranger. Utilizing its close ties with regional financial institutions, the Bank has developed significant capabilities as a lead arranger. We are also focusing on arranging syndicated loans for regional small and medium-sized corporations in cooperation with our regional financial institution clients. In addition to arranging syndicated loans, the Bank also provides agent services for loan administration.

Securitization

To help our clients achieve greater diversity in their funding sources, Aozora Bank assists companies in the securitization of various types of financial claims. These include accounts receivable, notes receivable, leaseholds, credit card loans, automobile loans, installments and medical fees. We are also meeting client needs in such areas as reduction of financing costs through the utilization of the creditworthiness of financial claims held by the client, and balance sheet streamlining. We have bolstered our specialist staff in this area of operations, enabling us to accumulate know-how and use advanced techniques to strengthen our product development capabilities. Our subsidiary, Aozora Trust Bank, Ltd., is also working to strengthen the Group's securitization arrangement capabilities by exploiting its expertise in trust operations.

Derivative-Embedded Loans

For clients seeking to lower financing costs and hedge interest rate risk, we offer Marine Blue, a loan product embedded with interest rate derivatives. In addition, we are able to provide customized products that meet particular client needs.

Investment Products

In addition to our traditional debenture and deposit products, to help meet the unique investment needs of each client, we offer an array of products, including Mountain Blue, a deposit product that incorporates interest rate derivatives, and Aqua Blue, a foreign currency-denominated special time deposit.

Risk Hedging Products

The Bank has built an effective system for providing clients with timely information and products to help them effectively manage their exposure to a variety of risk types, and is actively developing new risk management products. The Bank provides a range of foreign exchange and interest rate derivatives, including forward exchange contracts, currency options and interest rate swaps and options. In addition, we are focusing on the provision of credit derivatives in response to growing client demand for assistance with management of credit risk exposure.

Other Products and Services

Private placement bonds allow a company not only to diversify its funding sources and enable it to accumulate know-how useful in any future public funding, but also to enhance its position in the finance and investment community. For these reasons, private placement bonds have become a popular fund-raising method among small to medium-sized corporate clients. In addition to acting as trustee of private placement bonds, the Bank supports its clients by inviting potential investors to participate in bond placements.

As another flexible means of meeting clients' funding needs, the Bank also provides its expertise in the area of commercial paper (CP) underwriting and CP-based financing proposals.

To satisfy clients' financing needs through bond issuance in the capital markets, Aozora Bank acts as trustee of private placement and public bonds, including the private placement bonds of small to medium-sized companies guaranteed by the Credit Guarantee Corporation. This trustee service has been developed through the Bank's extensive experience and expertise accumulated as an authorized issuer of and registration agency for bank debentures. In addition, we arrange bond offerings and provide trustee services for asset-backed securities (ABS), the market for which has been expanding rapidly in recent years as a new financing tool for corporations.

Supporting Business Revitalization

Aozora Bank supports corporate revitalization by helping clients unlock hidden value in existing businesses and through the incubation of new businesses, on either a whole company or business unit level. This process includes spotlighting and evaluating stagnant businesses and dormant assets within companies.

Specifically, the Bank provides leveraged finance and debtor-in-possession (DIP) finance as well as advisory services for the formulation of corporate recovery plans. The purchase of problem loans and the provision of non-recourse finance are also included within our range of services. In addition, we provide support for company start-ups, buyouts and business restructuring. This may include arranging financing on an individual project basis for content business development.

Leveraged Finance

Leveraged finance—a financing method that utilizes the cash flows projected in a company's business plan and the estimated value of the target business—plays a crucial role in business revitalization. This area includes management buyouts (MBOs)—used for strategic restructuring as well as to spin off the profitable divisions and subsidiaries of bankrupt companies—and capital restructuring for business regeneration. Aozora Bank entered the leveraged finance field much earlier than many other domestic financial institutions, and, since then, we have built up our competitive position to become one of the leading banks in this area. As demand for leveraged finance expertise grows, we will continue to respond flexibly to client needs.

Recovery Support

For clients needing to respond to a rapidly changing operating environment, the Bank offers a full lineup of business recovery services. In addition to providing a range of corporate advisory services, including the formulation of business recovery plans and assistance in finding new business sponsors, we also provide various types of lending, short-term working capital financing essential for business continuity (DIP finance), and medium- and long-term lending premised on a sound recovery plan.

Our loan servicer subsidiary, AOZORA Loan Services Co., Ltd., provides support to financial institutions in the disposal of problem loans, and makes business recovery plan proposals to obligors of loans purchased by AOZORA Loan Services, thereby revitalizing the borrower's business.

Aozora Bank also provides expertise and detailed know-how in the liquidation and disposal of overseas assets. For clients reorganizing their overseas operations, we undertake purchases of overseas-based distressed assets and loans to overseas subsidiaries and assist with the divestiture of joint venture shareholdings.

Real Estate Finance

The Bank has been active in the non-recourse financing field—also referred to as real estate securitization—from an early stage. Under this method of financing, unlike ordinary lending to corporate clients, the lender relies on cash flows generated by the subject assets—real estate. In recent years, against the background of a broad shift toward the separation of property ownership, management and utilization activities, many companies are actively looking for ways to remove their real estate assets from their balance sheets. Reasons for such moves by corporations include preparation for the adoption of accounting standards relating to the impairment of fixed assets. In addition, since more investors now consider real estate assets that generate stable cash flows in a similar light to other financial products, the non-recourse finance market is rapidly expanding. This trend is epitomized by the introduction of Japanese real estate investment trusts (J-REITs) in September 2001, with the number of publicly listed J-REITs now exceeding 10.

As well as collaborating with a wide range of participants in the real estate finance industry and providing primary lending and investments from a neutral position, the Bank has built up a strong track record in financing proposals and successfully executed transactions for corporate clients. The Bank will continue to meet the diverse needs of its clients in the area of real estate ownership, management and utilization by offering a lineup of value-added services.

Private Equity

Buyout Funds

The Bank actively supports the business restructuring efforts of its clients through the provision of merger and acquisition (M&A) advisory services and the use of buyout funds. Specifically,

through the Business Succession and Second Founding Fund, which is managed by JABOC, Ltd., the Bank is involved in providing services to various parties. These include profitable small and medium-sized firms that are unable to find suitable successors for retiring founders, and divisions or subsidiaries of large corporations that are looking to be spun off as independent operations. The Bank has contributed to the successful completion of a number of such transactions. In the area of industry-focused buyout funds, we have jointly established IDA Capital Inc., which manages Japan's first buyout fund specializing in restructuring in the information systems industry.

Venture Capital Investment

The Bank provides value-added support and tailored lending solutions to venture companies. In addition, through Aozora Investment Co., Ltd., we have achieved a solid track record in the appraisal and incubation of new companies possessing strong technology and growth potential.

Other Financing

Hospital Project Finance

Aozora Bank has developed an analytical assessment method that is specifically designed for the management of medical institutions. This has been achieved through the first benchmarking survey covering major hospitals throughout Japan. Based on such know-how, we provide financial advisory services to medical institution clients and make proposals that employ a diverse range of financing schemes. Through these efforts, we have accomplished significant results in the area of hospital project finance.

Ship Finance

The Bank provides finance for the construction and purchase of bulk carriers, chemical tankers and other ocean-going vessels, which, in recent years, have increasingly been chartered by non-Japanese shipping lines. Our ship finance group has built up considerable know-how in effectively meeting ship financing needs.

For Financial Institution Clients

It is our aim to become even more finely attuned to meeting the unique needs of each of our financial institution clients through the development of new and original financial products and the provision of asset management products. We are also focusing on collaboration with financial institution clients in such areas as loan syndication and business revitalization proposals targeting the corporate customers of these clients. Furthermore, we will continue to provide reliable solutions that address management issues faced by our clients, including measures in line with the Action Program Concerning Enhancement of Relationship Banking Functions.

Providing a Diverse Range of Financial Products

Aozora Bank is able to meet a diverse range of needs to help clients manage their asset portfolios. In the lending field, we offer loan syndication and derivative-embedded loan products, and, in the asset management area, we provide debenture products, securitized financial products and deposit products that incorporate a variety of derivatives.

Loan Syndication

As more corporate borrowers diversify their funding sources, Aozora Bank is arranging an increasing number of syndicated loans for corporate clients. For our financial institution clients, this not only provides opportunities for participation in loan syndication, it also allows them to gain geographic and industry diversification in their loan portfolio. In addition, we are able to make joint proposals for syndicated loans to corporate customers of our financial institution clients, which may include arrangement services for nationwide loan syndications and post-closing agency services for managing loans.

Securitization and Privately Placed Funds

To meet client needs in the area of investment diversification, the Bank provides a variety of securitized financial products. The Bank, together with its subsidiary Aozora Trust Bank, structures and provides a variety of securitized products, including beneficial interests in trusts, collateralized loan obligations (CLOs) and asset-backed securities (ABS). We also offer a variety of privately placed funds with various risk profiles.

Derivative-Embedded Asset Management Products

In response to growing investment needs as a result of Japan's low interest rate environment, we offer a special time deposit called Mountain Blue, which incorporates derivatives that cover a variety of interest rate scenarios, and credit-linked products, which incorporate credit derivatives.

In addition, the Bank is engaged in providing high value-added services in association with regional banks; we provide regional banks' corporate customers with derivatives products that are guaranteed by these regional banks.

OVERVIEW OF OPERATIONS

Debentures and Other Products

In addition to the Bank's traditional debenture products, we provide a wide range of asset management products that utilize our detailed and accurate market information resources. These products include public bonds, CP, government-guaranteed bonds and municipal bonds.

Offering Solutions to Specific Management Issues

Aozora Bank helps its clients address the issue of disposal of non-performing assets through the purchase of problem loans held by financial institution clients. The Bank also provides clients with timely information and products to help them effectively manage their exposure to a variety of risk types.

Helping Clients Revitalize Their Asset Base

To address clients' needs in the area of disposal of problem loans, the Bank's subsidiary, AOZORA Loan Services Co., Ltd., provides support for financial institution clients in the disposal of non-performing loans through the purchase of such loans held by these clients. It also provides support for regional financial institutions to help them improve the quality of their loan asset portfolios through a range of advisory services, including the formulation of business recovery plans and business strategies for clients to whom the regional institution has a particular risk exposure.

In addition, the Bank provides expertise and detailed know-how in the liquidation and disposal of overseas assets. Services include the purchase of non-resident distressed assets held by clients.

Risk Management

The Bank has built an effective system for providing clients with timely information and products to help them effectively manage their exposure to a variety of risk types, and is actively developing new risk management products. In addition to providing interest rate swaps and options, we are bolstering our capabilities in the provision of credit derivatives in response to growing client demand for assistance with the management of credit risk exposure.

To help clients improve their credit portfolio management, the Bank provides a wide variety of products and services. These include various means of converting loan assets to a source of liquidity, such as the purchase of sound loan assets, and providing loan participation. The Bank also provides credit derivatives.

In the area of risk management advisory services, we will continue to provide a comprehensive lineup of services based on client demand. These include analytical tools for quantifying market and credit risk, as well as consulting services on the building of risk management systems based on the client's particular financial resources and earnings capabilities.

Internet-Related Services

Since its establishment in April 2001, the Bank's subsidiary, Blue Planet Corporation has provided a unique Internet-based service for financial institution clients and their customers and gained a strong reputation for its effective business support tools. The company will strive to further bolster its service lineup and expand its client network. Blue Planet's main services at present are as follows:

- Support services for building a business portal
- Support services for gaining ISO certification
- A reverse-auction electronic bidding system for buying and selling businesses
- An application service provider (ASP) solution for paperless settlements
- An Internet-based account aggregation service

Making Collaborative Proposals to Clients' Corporate Customers

In response to the needs of its regional financial institution clients relating to the Action Program Concerning Enhancement of Relationship Banking Functions, Aozora Bank utilizes its know-how in business revitalization to provide support to its clients' corporate customers on a collaborative basis.

Recovery Support

For companies needing to respond to a rapidly changing operating environment, the Bank offers a full lineup of business recovery services in collaboration with its financial institution clients. In addition to providing a range of related corporate advisory services, we also provide various types of lending, short-term working capital financing essential for business continuity (DIP finance), and medium- and long-term lending premised on a sound recovery plan.

Real Estate Finance

Aozora Bank has been active in the non-recourse financing field from an early stage. Under this method of financing, the lender relies on cash flows generated by the subject assets—real estate. We collaborate with many of the industry's leading arrangers to provide primary lending and investments. We have built up a strong track record in financing proposals and successfully executed transactions for customers of our financial institution clients. The Bank will continue to meet the diverse needs of its clients in the area of real estate ownership, management and utilization by offering a lineup of value-added services.

Private Equity

As well as offering M&A advisory services, the Bank provides business restructuring support through buyout funds managed by JABOC, Ltd., and IDA Capital Inc. Our venture capital subsidiary, Aozora Investment Co., Ltd., is also involved in the incubation of new companies that possess strong technology and growth potential.

Other Financing

Through the Hospital Management Assessment Project, which was set up in September 2002, we have accumulated significant know-how in objectively assessing and analyzing hospital management. Based on this, we work in partnership with our regional financial institution clients to provide financial advisory services to medical institutions and jointly originate syndicated loan transactions.

Our ship finance group provides finance for the construction and purchase of ocean-going vessels. It effectively meets a variety of ship financing needs, including those for vessels chartered by non-Japanese shipping lines.

For Retail Clients

To closely meet the investment and financial planning needs of our retail clients, we offer an advanced range of investment advisory services. As well as utilizing our branch network, we are improving remote channel access through an expansion of our telephone banking services. As well as offering a time deposit product available only through telephone banking, we provide an extensive lineup of investment trusts and personal annuity insurance for individuals. Through a subsidiary, we offer a card loan product. We have also focused on expanding our consulting services.

Asset Management Products

Time Deposits

The Aozora Direct Time Deposit, offered exclusively as a telephone banking product, utilizes remote channels to reduce operational costs, enabling us to offer very competitive interest rates. Also attracting many clients to this product is the convenience with which funds can be deposited and withdrawn. Transactions can be performed through the nationwide Postal Savings ATM network and are not subject to ATM usage fees. We also offer a range of products with various investment periods and amounts.

Debentures

As a debenture-issuing bank, we have a strong track record in meeting the asset management needs of retail clients. We have also launched a new type of debenture called Aozora Super, which is covered by Japan's deposit insurance system. Since the end of April 2003, we offer only custody services for *Warishin* Aozora discounted debentures and *Risshin* Aozora debentures.

Investment Trusts

As of April 2004, we offered a total of 30 investment trust products to meet the diverse investment needs of our clients. These included money market funds (MMFs), corporate and public bond investment trusts, foreign currency MMFs, and investment trusts that invest in bonds and equities in domestic and foreign markets. We also offer clients advice on investment portfolio diversification.

Personal Annuity Insurance

By offering investment-type pension products and fixed annuity products, we are able to meet a broad array of client needs, including those relating to investment, retirement income and estate planning.

Service Channels

Telephone Banking

As well as providing exclusive access to the Aozora Direct Time Deposit product, our telephone banking service also lets customers purchase investment trusts and debentures and take care of normal personal banking procedures, such as account balance inquiries and change of address notifications. Rather than using an automated touch-tone system, our telephone banking service is staffed by a team of specialist operators, meaning even customers that are new to telephone banking will feel at ease. To further increase the attractiveness of our remote banking channels, we intend to continue adding new products and services on a regular basis.

ATM Alliances

To further enhance client convenience, we extended our ATM alliances to include Postal Savings ATMs across Japan, in addition to our existing ATM alliances with the major nationwide banking groups and trust banks. At Postal Savings ATMs, Aozora Bank customers can make deposits and withdrawals seven days a week, without incurring usage fees. Used in conjunction with our telephone banking, our retail clients enjoy an exceptionally high level of convenience.

Asset Management Consulting Services

To strengthen our ability to provide a range of asset management consulting services at our branches, we have put in place a system to encourage and support staff members in obtaining financial planner qualifications. To increase customer convenience in accessing these services we have extended the hours of our asset management consulting services to 5:00 p.m. on weekdays at the Bank's headquarters and all branches.

We have also established the FP Promotion Department at the Bank's headquarters to provide a range of specialist consultation and advisory services to clients in the greater Tokyo metropolitan area. These services cover such areas as asset management, estate planning and business succession, with the aim of providing the information necessary for clients to make the best choices regarding their financial needs.

Aozora Financial Garden

At the Aozora Financial Garden areas within our Tokyo region branches, specialist teams provide a wide range of advisory and consultation services, including those relating to investment, real estate asset management and home loans.

Card Loan Business

Our subsidiary Aozora Card Co., Ltd., commenced operations in April 2002. The company's main line of business is unsecured loans to individuals using the MY ONE loan card, but is also involved in credit guaranty operations for personal loans made by regional financial institutions. MY ONE offers a range of advantages to clients, including high credit limits, low interest rates, 24-hour service and the convenience of a large ATM network. This product is mainly targeted at business people. A key characteristic is the product's high rate of usage through our Internet marketing channel, which we plan to utilize further in future product introductions.

Management Structure

New Organizational Structure

In April 2004, the Bank made changes to its organizational structure. The main objective of this restructuring was to create a more client-focused organization by realigning the product and sales systems into business groups, and to allow senior management to focus on key control and support functions. Management believes the new organizational structure will improve the effectiveness and time to market for new products and further strengthen the corporate governance framework of the Bank.

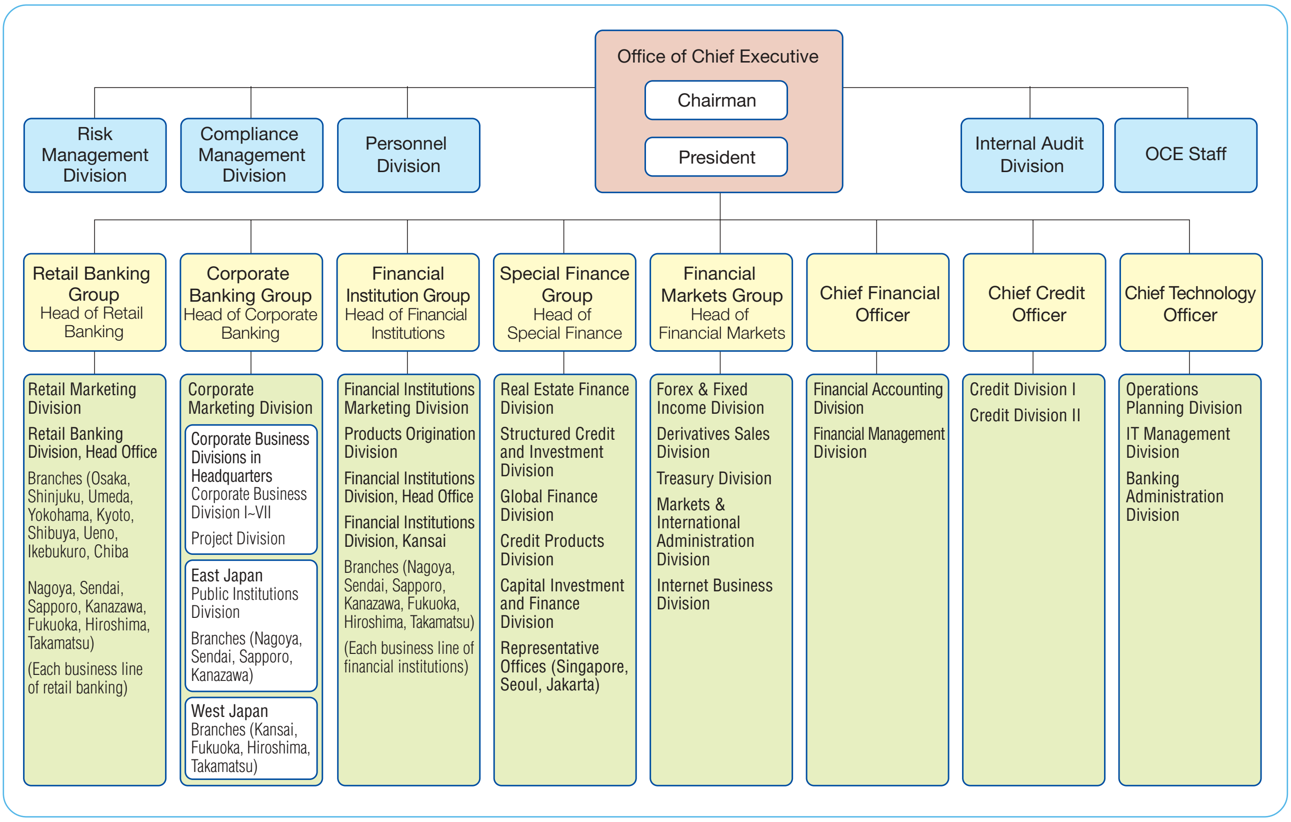
New Business Support Groups

The five core business groups are the Corporate Banking Group, the Financial Institution Group, the Retail Banking Group, the Special Finance Group and the Financial Markets Group. Each business group has its own distinctive and valuable range of products and services, strong client relationships, skilled product specialists and talented sales force focused on understanding and meeting the needs of target clients.

At the same time, the finance, credit management, and technology and operations functions were reorganized under the newly created positions of Chief Financial Officer, Chief Credit Officer and Chief Technology Officer, respectively, giving additional high-level focus to these key control and support functions. Internal audit and risk management continue to be directly overseen by the Chairman and the President.

New Organizational Structure

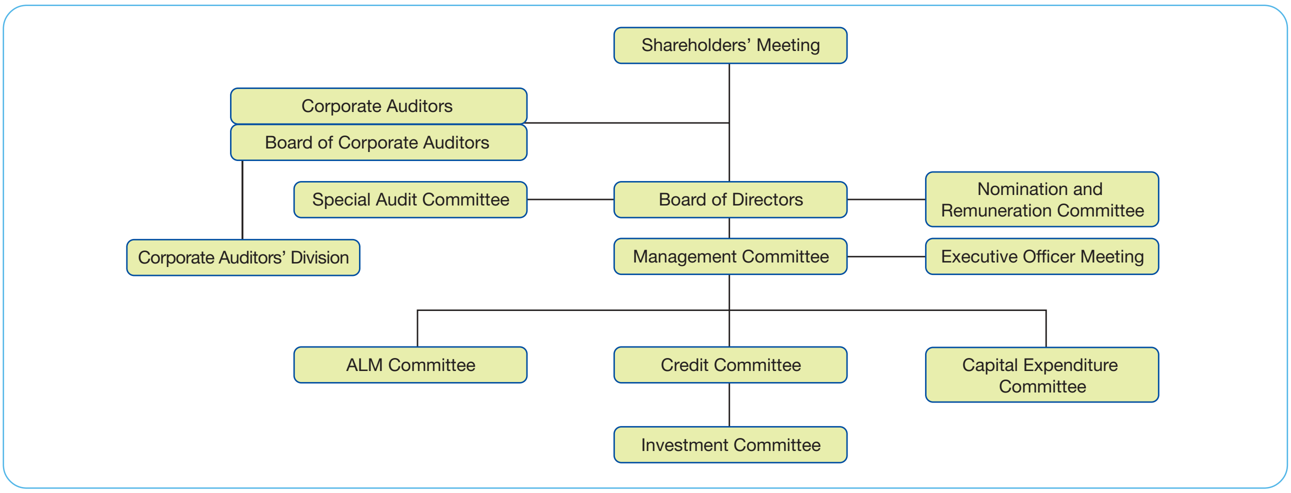
The Bank has established a Management Committee, consisting of the Chairman, the President and the business and support group heads. This committee has assumed the authority and responsibility of the former Executive Committee. The members of the Management Committee have clear lines of responsibility, making it a focused and effective forum to set and manage the strategic agenda of the Bank. The Management Committee has delegated specific authority to three main sub-committees: the Credit Committee, chaired by the Chief Credit Officer; the ALM Committee, chaired by the Chief Financial Officer; and the Capital Expenditure Committee, chaired by the Chief Technology Officer.



(As of August 2004)

Corporate Governance Structure

Organizational Structure



Board of Directors

The Board of Directors, as the highest decision-making body, determines the Bank's basic management policies. It delegates authority for day-to-day operations to the Management Committee, which consists of the Chairman, the President and senior managing executive officers. The Board of Directors, which mainly consists of outside directors elected from various domestic or foreign areas, is able to focus on decision making from a broad strategic perspective.

Management Committee

The Management Committee, which has authority for day-to-day business operations as delegated to it by the Board of Directors, consists of the Chairman, the President and senior managing executive officers. The Management Committee convenes regularly and makes decisions on critical issues. The Executive Officer Meeting, consisting of all executive officers, is a forum for the exchange of information and opinions about day-to-day operations in all the Bank's activities.

Various Other Committees

Asset and Liability Management (ALM) Committee

The main objectives of the ALM Committee, as one of the sub-committees of the Management Committee, is to regularly monitor and review the Bank's position with regard to its balance sheet, liquidity risks, market-related risks, risk capital profitability and risk-based capital, as well as to set up an appropriate management policy.

In principle, the ALM Committee convenes once a month. The Chief Financial Officer chairs the committee, which also consists of the Chairman, the President, executive officers and the general managers in charge of the Risk Management Division, Treasury Division and Financial Management Division.

The ALM Committee makes decisions in the following areas: (1) monthly balance sheet plan, (2) ALM risk management policy, (3) the terms and conditions for debenture issuance and (4) key objectives relating to ALM operations, based on interest rates and market conditions.

Credit Committee

The Credit Committee has final authority for individual credit matters, determines credit policy for large-lot borrowers and decides on important issues concerning the management of the credit portfolio. This helps to ensure an appropriate system of checks and balances for the Bank's business operations and the construction of a credit portfolio that avoids significant concentration in any category.

The committee may delegate a part of these individual credit decisions to the Chief Credit Officer and/or to the

Investment Committee and other similar bodies or individuals with equivalent responsibility. In such situation, the committee delegates authority in accordance with the standards stipulated by the Management Committee.

The committee is chaired by the Chief Credit Officer, and also consists of the Chairman, the President and the general managers of Credit Divisions I and II. In principle, the committee meets weekly.

Capital Expenditure Committee

The Capital Expenditure Committee considers and makes decisions on matters relating to capital expenditure, which includes, but is not limited to, the establishment of new office locations, investment in computer systems and technologies, and the acquisition of real estate, from a management-level point of view.

The committee members include of the Chief Technology Officer, who acts as chairperson, the Chairman, the President and the Chief Financial Officer.

Of the expenditures approved by the committee, those matters deemed particularly important are subject to the approval of the Management Committee.

Board of Corporate Auditors

The Board of Corporate Auditors is convened once a month, and consists of four auditors (three of whom are external). The board deliberates audit-related matters and determines audit-related policies and initiatives, focusing on overall policy.

The role of the auditors is to (1) participate on the Board of Directors and other upper-level management bodies as required under Japan's laws and regulations, (2) inspect the Bank's overall operations and asset position based on the policies and initiatives determined by the Board of Corporate Auditors and (3) inspect operational management systems in close consultation with the external auditor, the Compliance Management Division and the Internal Audit Division among others.

Nomination and Remuneration Committee

The Nomination and Remuneration Committee is an advisory body to the Board of Directors consisting of members chosen from the Board of Directors. It deliberates on the appointment and dismissal of directors and senior managing executive officers and on remuneration for directors and senior managing executive officers.

Special Audit Committee

We have established the Special Audit Committee to enhance the safeguards that are designed to prevent major shareholders from gaining preferential treatment, as well as to ensure independent, sound management. The Special Audit Committee mainly consists of corporate auditors, who audit transactions with major shareholders and their affiliates to avoid the Bank becoming a captive bank. The committee acts in accordance with legal regulations, including the Long-Term Credit Bank Law.

Transactions with major shareholders and their affiliates are disclosed in Aozora Bank's annual reports as well as in its financial statements.

Transactions with Parent Company Groups

(Millions of Yen)

		March 31, 2004	March 31, 2003
Cerberus Group	Number of borrowers	—	—
	Credit balance	—	—
ORIX Group	Number of borrowers	12	12
	Credit balance	26,923	31,605
The Tokio Marine and Fire Insurance Group	Number of borrowers	2	2
	Credit balance	618	812
Total	Number of borrowers	14	14
	Credit balance	27,541	32,417

Notes: 1. Figures for credit balances refer to credit extended by Aozora Bank, its subsidiaries and affiliated companies.
2. The Bank's "parent company groups" refers specifically to major shareholders and their subsidiaries and affiliated companies.
3. Transactions with major shareholders and other firms include loans, customers' liabilities for acceptances and guarantees, CP, equity holdings/interest and derivative transactions.

Policies

Internal Policy

Compliance Policy

The Bank has established internal systems and rules that ensure due compliance with legal requirements and integrity in the conduct of all its operations, striving to foster a corporate culture that places priority on the achievement of these objectives.

Master Policy on Compliance

The Bank has instituted a *Master Policy on Compliance,* which sets forth the internal organization and systems and basic principles needed to maintain compliance with all legal regulations in all aspects of its operations. In addition, the *Compliance Program,* which is updated annually, specifies action guidelines and compliance standards. For the fiscal period ending March 31, 2005, the Bank plans to strengthen its training and educational programs as well as to enhance the effectiveness of its periodic compliance audits to ensure that a culture of compliance with all laws and regulations takes firm root within the organization.

Compliance Organization and System

Primary responsibility for supervising legal and compliance issues at the Bank rests with the Compliance Management Division, which is involved in developing and improving compliance systems and conducting compliance checks that focus on various relevant legal issues. An executive officer of the Bank is appointed as Chief Compliance Officer (CCO) and the general manager of the Compliance Management Division supports the CCO as Executive Compliance Officer. The division provides internal legal consulting services, including the review and authorization of contracts, and is also responsible for formulating, monitoring and revising internal regulations.

Compliance leaders are appointed within all divisions and branches. Their duties include providing consultation services, carrying out compliance audits and promoting awareness of compliance-related issues.

As part of the program to build a fair and honest corporate culture, the Bank has taken two major initiatives. These were (1) the introduction of a system allowing employees to consult directly with auditors and the Bank's legal advisers; and (2) the setting up of a system that enables the Compliance Management Division to independently communicate with employees on compliance issues. To maintain and enhance the corporate identity across the entire Aozora Bank Group, the Bank is working to develop an integrated compliance system covering all its affiliates through such measures as the establishment of an information sharing system on compliance issues.

Compliance Training and Awareness Programs

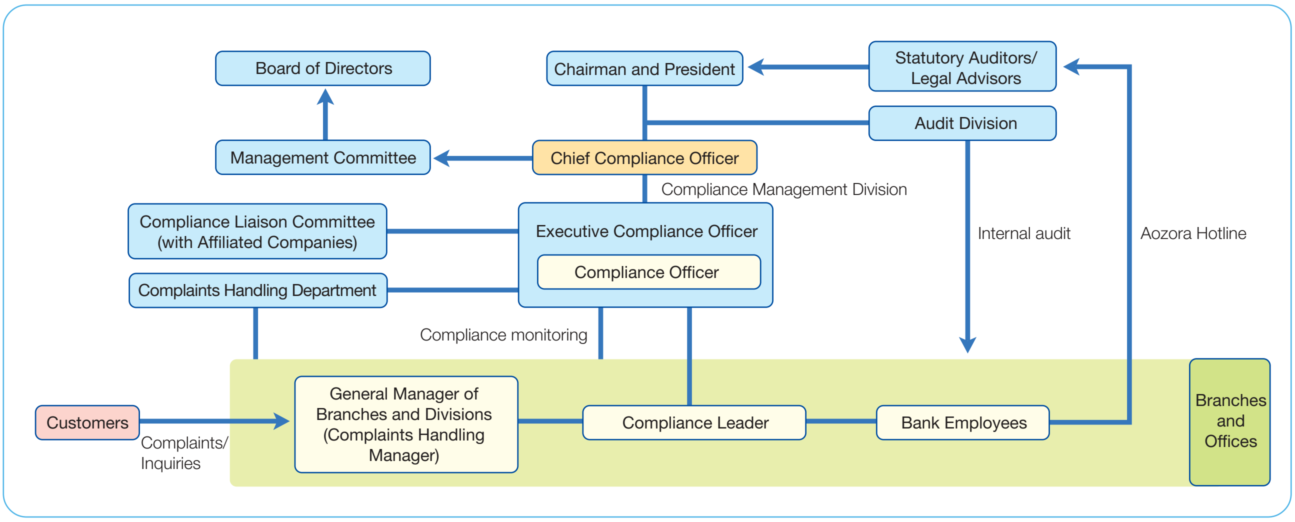
Training programs for compliance leaders and heads of division, which make use of outside lecturers, are conducted annually to ensure a thorough understanding of key compliance issues. In this way, all directors and employees throughout the Bank gain a thorough understanding of current compliance issues.

The Bank has a wide variety of compliance training opportunities that it makes available to new employees and newly appointed department heads, as well as a variety of training programs that promote greater awareness of the importance of compliance throughout the Bank.

Anti-Money Laundering Policy

At Aozora Bank, the Compliance Management Division is

Compliance System



responsible for the implementation of policies relating to customer identification and procedures for notifying the relevant authorities in case of suspicious transactions, as part of the Bank's systems for complying with anti-money laundering regulations. The general manager of the Compliance Management Division is responsible for customer identification and the implementation of related procedures. Each of the Bank's business support groups shares a role in carrying out these procedures. In the case of customer identification pursuant to the Foreign Exchange and Foreign Trade Law, the general manager of the Operations Planning Division is responsible for fulfilling these legal obligations. To avoid the risk of transactions conducted by the Bank being used in terrorist-related activities, the Operations Planning Division disseminates information within the Bank regarding customer identification obligations when conducting foreign exchange transactions.

The Bank will continue to strengthen and expand the scope of its compliance systems among both management and employees.

Internal Audit Policy

At Aozora Bank, the Internal Audit Division, an autonomous body, assesses whether the risk management systems of the business units they audit are functioning adequately and effectively. The Internal Audit Division not only identifies potential problems in clerical procedures and other areas, but also conducts assessments of internal control systems and makes recommendations on improvements to potential problem areas. In this way, the Internal Audit Division works to maintain an appropriate system of checks and balances and ensure sound and appropriate banking operations.

All business operations of the Bank and—subject to legal limitations—those of its subsidiaries and affiliates are subject to internal audits, the results of which are reported to the Board of Directors and to the Management Committee.

Finance Policy

The Finance Division is responsible for ensuring that the financial books and records of the Bank and consolidated Group companies are maintained in a complete, accurate and timely manner. The Finance Division prepares reports on the financial performance and position of the Bank as required by various stakeholders, including shareholders, the Board of Directors, management, regulators, taxation authorities, clients, investors and staff. The Finance Division must also ensure internal controls within the Bank operate effectively to maintain the financial integrity and accuracy of the books and records and financial reports. Furthermore, it must assist senior management in developing, implementing and monitoring progress in the Bank's strategic plans. All decisions made within the Bank to advance credit, invest, spend, procure or develop should be made against clear cost-benefit or risk-reward criteria, and the Finance Division is responsible for the establishment and maintenance of such a framework.

Risk Management System

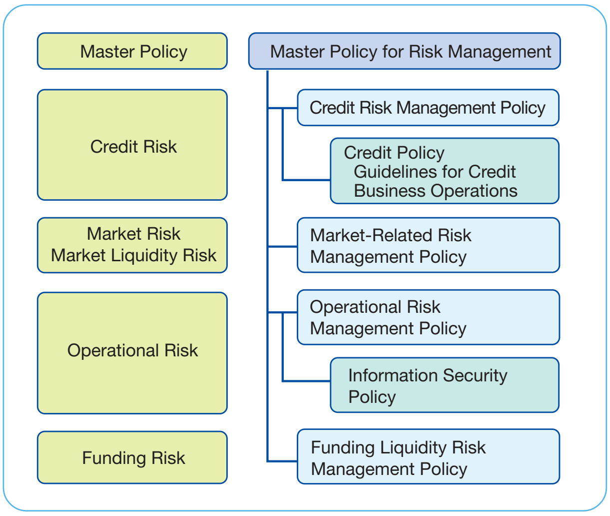
An Overview of Risk Management

Basic Policies

Economic and financial conditions are constantly changing. As a result, the Bank's business operations and the risks associated with those operations are also subject to constant change.

By maintaining and enhancing appropriate risk management systems, the Bank strives to avoid unforeseen losses while taking on risk to a level proportionate to the Bank's financial resources. Within the diverse business operations conducted by the Bank, proper risk management systems allow the Bank to obtain an adequate return for the risk it undertakes and facilitates sound management with a high degree of credibility.

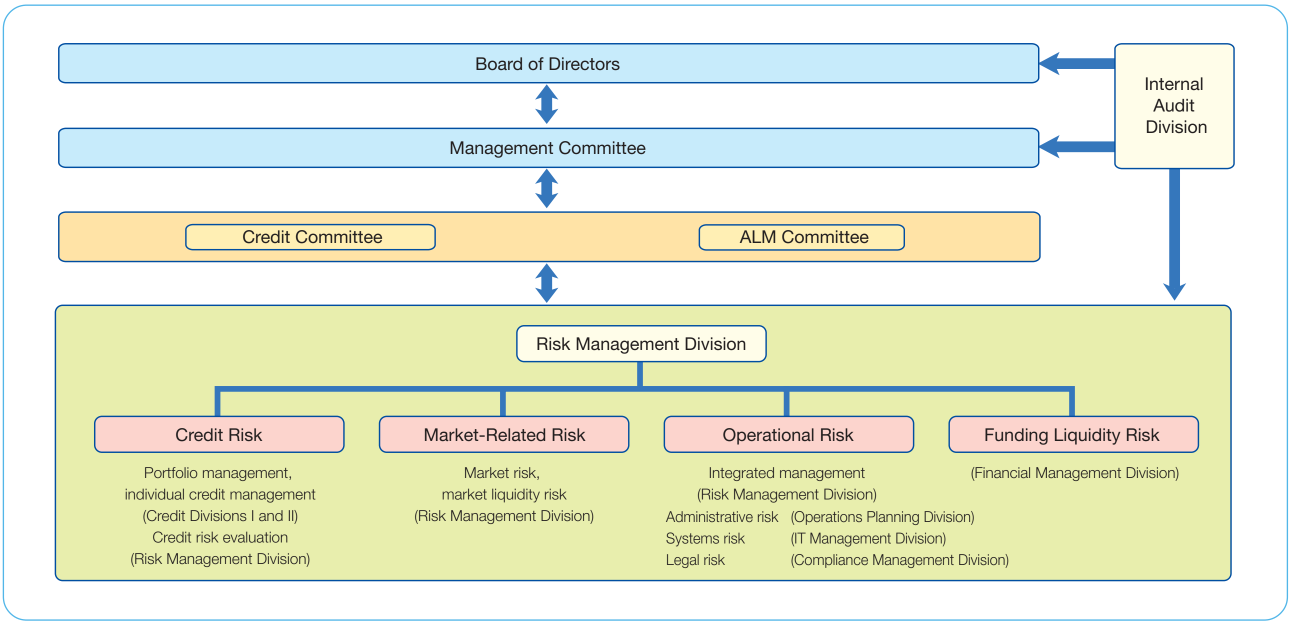
Risk Management Policies



Risk Management System

The Bank's overall risk management policy is clearly explained in the *Master Policy for Risk Management*. As well as determining the basic rules for managing risk, the Board of Directors also sets the risk management framework for the Bank, including capital allocation and the setting of risk limits for the Bank.

Risk Management System



Within this framework, the Risk Management Division is responsible for unifying the risk management stance of the Bank as a whole, while each specialist division manages those risks unique to its business according to their particular characteristics, including credit risk, market risk and operational risk.

In addition, the Internal Audit Division checks the appropriateness and effectiveness of the risk management system.

The Board of Directors, the Management Committee and other committees receive reports on the risk management situation from each risk jurisdiction, as well as from the Internal Audit Division, and they utilize this information in management decision making. These management bodies also act to maintain and enhance the Bank's risk management system.

Quantification of Integrated Risk

In order to understand the different forms of risk comprehensively, risks must be measured by a common yardstick. Aozora Bank employs VaR (Value-at-Risk) to calculate the amount of capital that should be set aside against particular risks. In this way, the Bank undertakes comprehensive management of credit, market and other forms of risk. Risks related to the Bank's affiliates have also been incorporated into this risk management framework.

Risk Capital Allocation System

To improve the profitability and efficiency of the Bank as a whole, the risk capital allocation system sets the amount of capital to be placed at risk by each business unit based on the risk tolerance and expected income of each business unit, according to management and business strategies.

The Board of Directors allocates risk capital (Tier I) to individual business units in line with the requirements of management and business strategies, after setting aside the amount of capital required to maintain minimum capital adequacy and provisions for operational risk.

Each unit is responsible for conducting operations within the risk limit provided by the risk capital allocation. The Risk Management Division monitors the usage of capital by each business unit and reports to senior management.

Credit Risk Management

Credit risk refers to the potential for loss arising from the impairment of asset value due to the deterioration of borrowers' financial condition or their failure to perform their contractual obligations for specific projects.

There are two major components of the Bank's credit risk management. One is the strict credit screening and monitoring of individual transactions. The other is portfolio management, which focuses on eliminating concentration risk and optimizing risk-return profiles. Both contribute to the Bank's efforts to maintain a sound asset base.

Credit Risk Management System

The Credit Committee discusses and makes decisions on important policies and rules relating to credit risk. It also approves credit that meets predetermined criteria and formulates policies for borrowers with large credit balances.

The Credit Committee consists of the Chairman, the President, the Chief Credit Officer and others. Particularly significant decisions are given final approval by the Management Committee or Board of Directors.

Credit Divisions I and II screen individual transactions that involve credit risk, and draft and develop policies and rules from the perspective of credit portfolio operation and management. Independent from the Bank's business operations, the Risk Management Division assigns credit ratings, carries out self-assessment and evaluates risk using quantitative and other methods to maintain a rigorous risk management system.

Credit Rating System

At Aozora Bank, with the exception of individual retail clients, customer credit ratings are determined on the basis of a quantitative assessment of their financial condition and income, along with an assessment of qualitative factors and consistency with borrower categories as determined by the Bank's internal self-assessment standards.

Credit ratings of Japanese corporations, excluding financial corporations, are divided into 15 categories. At the same time, the credit rating system for other companies has been brought into line with these ratings by matching the probability of default (Note) for each category of domestic non-financial corporation with other borrower categories.

Credit ratings are integral to the Bank's credit management. They are utilized in making important decisions on such issues as the scheme for credit approval, the interest rate spread and the credit limit. Credit ratings are also used to conduct the Bank's internal self-assessments and are employed as benchmarks to quantify credit risk.

Note: The definition of the probability of default is based on a broad interpretation of default that encompasses not only legal bankruptcy and delinquency but also a wider range of circumstances and business conditions.

Credit Ratings for Individual Transactions

To properly assess the risk-return profile of each credit, the Bank needs to consider the recovery prospects of individual transactions, in addition to the credit rating of each client, which reflects the overall creditworthiness of the borrower. For this reason, the Bank introduced a system of credit ratings for individual transactions that reflects the probability of recovery of the credit, in addition to credit ratings for each client.

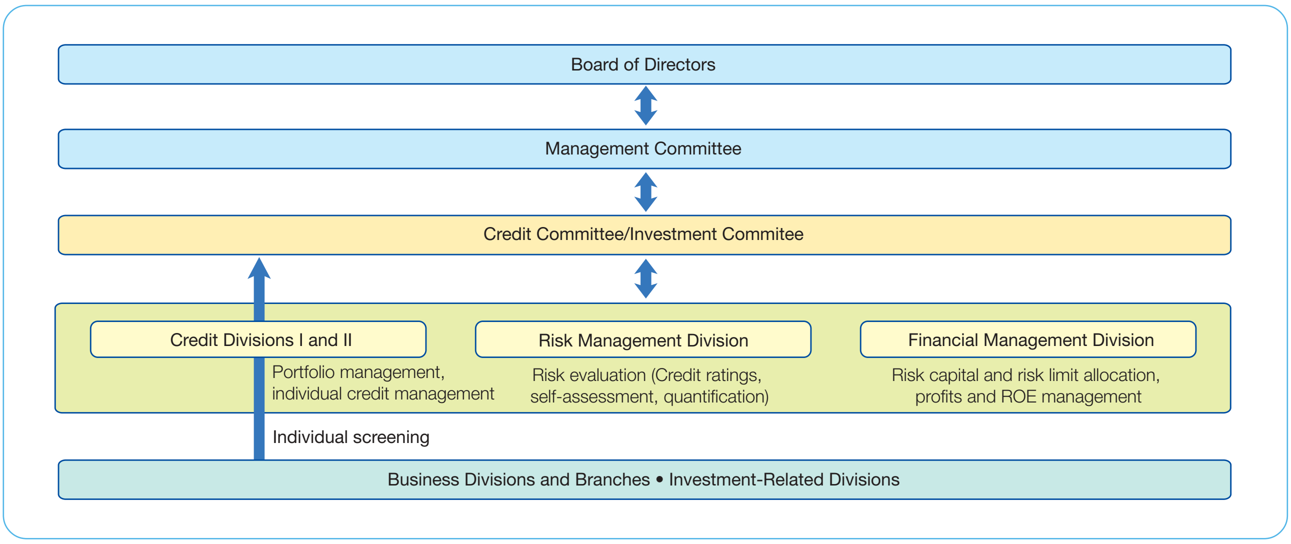
The system of credit ratings for individual transactions employs the borrower credit rating system with an 11-category system of ratings for individual transactions. The ratings for individual transactions take into account such factors as cash flows, which are classified by use of funds, and the method of monitoring cash flow. In addition, the rating system allows the Bank to more adequately take into account the nature and value of collateral and guarantees by including the expected cost of recovery, the change in the guarantor's repayment ability over time and the correlation of the guarantor's repayment ability with that of the borrower. The Bank also applies credit ratings to certain financing schemes, such as structured finance, where collection is independent of a borrower's creditworthiness. These credit ratings are applied using different models for each type of financing scheme.

By employing a system of credit ratings for individual transactions, the Bank is able to offer more appropriate interest rate spreads and lending terms, in full consideration of the credit cost, and thus better control the risk and returns from credit.

Credit Screening and Monitoring of Individual Transactions

At Aozora Bank, business divisions and branches are responsible for preliminary screening. Credit Divisions I and II

Credit Risk Management System



Credit Rating System at a Glance

Borrower categories	Domestic non-financial corporations	Domestic financial institutions	Overseas borrowers	Foreign financial institutions	Countries	Structured finance, etc.		Common probability of default (%)		External rating agencies	Credit research firms
Normal borrowers	A1	F-A1	G-A1	GF-A1	AAA	(Note)		a%			
	A2	F-A2	G-A2	GF-A2	…	…		b%			
	A3						Consistent rating using a common probability of default ⟷		Review consistency with external evaluation ⟷	External rating	External evaluation
	B1										
	B2+	…	…	…	…	…					
	B2-										
	B3+										
	B3-										
Watch list borrowers (excluding special attention borrowers)	C1+										
	C1-	…	…	…	…	…					
	C2										
Special attention borrowers	C3										
Potentially bankrupt borrowers	D1	…	…	…	…	…					
Substantially bankrupt borrowers	D2							100%			
Bankrupt borrowers	E	F-E	G-E	GF-E				100%			

Note: Ratings in the structured finance category include pooled credit (P-A1), real estate securitization (CM-A1), pooled loan assets (CD-A1), project finance (PF-A1) and LBO/MBOs (L-A1).

then conduct secondary screening, which involves a careful review of clients' business plans and verification of the appropriateness of the proposed use of loaned funds. Credit Divisions I and II also review and confirm that the future availability of funds for loan repayment is consistent with the repayment scheme and the duration of the loan.

Credit monitoring is conducted in accordance with the guidelines stipulated in *Lending Regulations* and the *Credit Management Manual.* The Bank carefully monitors the creditworthiness of borrowers and the value of collateral. In this way, the Bank strives to uncover any problems at an early stage, with the aim of preventing loans from becoming non-performing assets.

A firm's creditworthiness, which cannot be completely grasped through publicly disclosed financial statements, affects the firm's market valuation, and changes in a firm's market valuation now have a greater impact on its creditworthiness. For this reason, the Bank constantly monitors such market valuation-related data as credit ratings given by credit rating agencies and stock price changes. This information is used to evaluate credit ratings in a timely manner and modify the customer relationship strategy if necessary.

In relation to these credit screening and monitoring processes, the Internal Audit Division performs internal audits of all divisions and branches through on-site monitoring to ensure adequate credit management.

Portfolio Management and Quantification of Credit Risk

The Bank focuses on maintaining the quality of its entire credit portfolio through portfolio management, in addition to credit risk evaluation and management on an individual borrower and transaction basis.

The Credit Committee holds discussions based on the results of analysis and monitoring of the Bank's credit portfolio, including the diversity of exposures by industry or by internal credit rating and the concentration of exposures to any corporate group. Based on these discussions, the committee is able to make balanced and informed decisions, reflecting the current status of the Bank's portfolio. This procedure also ensures that there is no overconcentration of exposure in any particular industry or corporate group.

QUANTIFYING CREDIT RISK

Portfolio credit risk is dependent on which borrowers default and how these defaults occur. The Bank considers a range of factors affecting portfolio risk. These include the creditworthiness of each borrower based on the Bank's internal credit ratings, exposure amount, losses arising from default and the level of correlation among borrowers (such as parent-subsidiary correlations between those in the same corporate group, and correlations with those in the same industry and different industries. In light of these analyses, the Bank uses a Monte Carlo Simulation to calculate the volume of credit risk for the entire portfolio and for each business unit.

The volume of credit risk is managed through the setting of limits for allocated risk capital.

Market Risk Management

Market risk refers to the potential for loss due to fluctuations in the value of the Bank's assets and liabilities brought about by changes in such market variables as interest rates, stock prices or exchange rates. Market risk is not limited to financial instruments, such as marketable securities, the values of which are directly affected by market fluctuations. All assets and liabilities, including deposits and loans, are subject to market risk.

Aozora Bank performs an analysis of the market risk affecting all assets and liabilities in order to control market risk appropriately throughout the Bank. As a financial institution classified as a global dealer, the Bank has developed a risk management system capable of addressing all aspects of market risk.

Market Risk Management System

Within the framework of integrated risk management, the Board of Directors decides the risk capital allocation for the entire Bank and for each business unit commensurate with market risk exposure. Market risk limits and loss limits are set in accordance with the capital allocation, and these unit limits are further subdivided into specific limits for each business division and department. The Risk Management Division independently and centrally monitors the usage of, and compliance with, risk and loss limits, and reports to the ALM Committee and the Board of Directors.

Quantifying Market Risk

Aozora Bank uses Value-at-Risk (VaR) to quantify market risk and as a basis for setting market risk limits. VaR is a statistical measure of estimated maximum losses that could arise based on historical market data. VaR serves as a common standard of measurement that estimates potential losses that could arise as a result of interest rate, stock price and exchange rate fluctuations.

BACKTESTING

The Bank conducts backtesting to verify the reliability of VaR calculations by comparing daily reported VaR with actual daily gains or losses. The results of the backtesting for trading activities show that the actual daily losses exceeded daily VaR on only three of the 248 business days during the period from April 1, 2003, through March 31, 2004. These results support the reliability of the Bank's VaR model.

STRESS TESTING

The Bank regularly conducts stress tests to prepare for volatile market movements that could exceed statistical estimates. The Bank calculates and analyzes potential losses that could arise from dramatic changes in interest rates, stock prices and exchange rates, or from a collapse of correlations among different risk categories.

Trading Activities

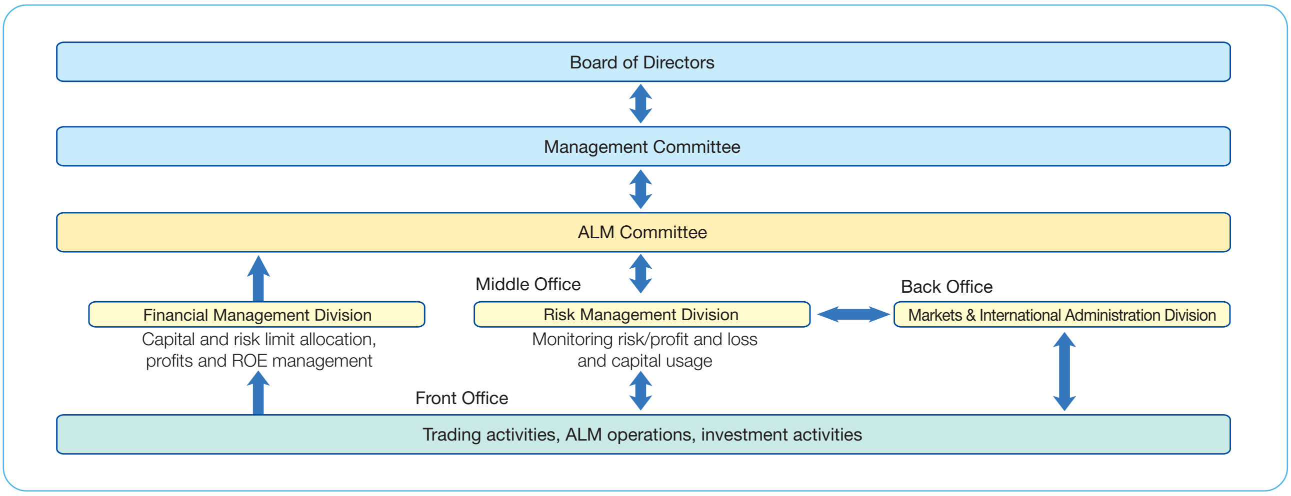
In the fiscal year ended March 31, 2004, the market risk level of trading activities for a VaR model with a one-day holding period and a one-sided confidence interval of 99% was a maximum of ¥189 million, a minimum of ¥49 million and an average of ¥113 million.

Asset-Liability Management (ALM)

The Treasury Division, which is responsible for ALM operations, centrally manages interest rate risk associated with all banking operations, excluding market activities, and market risk associated with securities, funds and derivatives held for ALM purposes. The Board of Directors approves capital allocation and risk limits with respect to ALM operations and the ALM Committee approves monthly management policy.

In the fiscal year ended March 31, 2004, the ALM risk level for a VaR model with a one-day holding period and a one-sided confidence interval of 99% was a maximum of ¥1.2 billion, a minimum of ¥0.8 billion and an average of ¥1.1 billion (weekly basis).

Market Risk Management System



Interest Rate Sensitivity of Yen-Denominated Assets and Liabilities

(Billions of Yen)

	One year or less	One to five years	More than five years	Total
March 31, 2004	(0.3)	0.1	(1.2)	(1.4)
March 31, 2003	(0.2)	(1.7)	(0.5)	(2.4)

Note: 10 bpv: For a 10bpv (0.1%) increase in interest rates, a positive change in the fair value of assets and liabilities suggests that when the interest rate rises, fair value will increase. A negative change in fair value suggests that when interest rates decline, fair value will increase. Off-balance-sheet transactions are included.

Other Operations

The Bank manages market risks associated with other operations, including portfolio investments and cross-holding shares, as part of its risk management framework. Actions include setting limits and taking other steps to mitigate market risk.

VaR for the Entire Bank

(Billions of Yen)

March 31, 2004	Interest rate	Equity	Forex	Total
Trading	0.0	0.0	0.0	0.1
ALM	0.7	0.5	0.0	1.1
Others	0.0	0.7	—	0.7
Total	0.8	1.2	0.0	1.8

Note: The figures for total VaR do not represent the sum of individual components, due to correlations.

Operational Risk Management

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk includes administrative risk, systems risk, legal risk and other risk.

Operational risk includes the potential for inconveniencing clients and causing significant losses. Recognizing the seriousness of these risks, the Bank has formulated the Operational Risk Management Policy, which clearly spells out the Bank's stance on this issue and the systems that have been put in place for managing such risk.

Banking operations involve exposure to a wide range of operational risk, including reputational risk, disaster risk and settlement risk, in addition to the types of risk previously mentioned. To manage these risks, for each type of risk the Bank identifies the organizational units responsible and the risk management systems in place. In addition, the Risk Management Division unifies the risk management systems across the entire Bank and carries out the integrated monitoring of operational risk, using quantitative and other methods.

Administrative Risk Management

Administrative risk is defined as the risk of loss resulting from the failure of directors and employees to handle routine work accurately as well as from accidents and other causes.

The Operations Planning Division formulates administrative procedures and manuals tailored to each business operation, with the aim of enhancing the reliability of routine procedures. The division is also tasked with building an effective administration system by providing guidance on specific processes and holding training seminars, in addition to analyzing the volume of clerical work and reviewing organizational arrangements. The Bank aims to minimize human error arising from administrative processes by continuously reviewing and implementing greater automation, systemization and centralization of routine procedures.

Systems Risk Management

Systems risk is defined as the risk of loss resulting from the failure of computer systems due to internal or external factors, including system crashes, system errors, unauthorized use of computer systems and computer viruses. With the advance in networking and diversification of banking operations, the consequences of system failures for society at large are becoming increasingly serious.

Aozora Bank is making concerted efforts to control systems risk, and has formulated a set of rules for systems risk management. The IT Management Division is making every effort to protect systems from natural disasters and other contingencies to ensure their stable operation. The Bank has also taken various steps to protect computer systems from a wide range of disasters and criminal activities to reduce systems risk.

Systems development and systems operation have been clearly separated to ensure adequate checks and balances between the two divisions.

Legal Risk Management

Legal risk is defined as the risk of: (1) incurring legal penalties or monetary losses resulting from the failure to comply with laws and other applicable regulations and standards; (2) potential losses resulting from lawsuits filed against the Bank by customers or other third parties for damage indemnification; and (3) other legal conflicts.

At Aozora Bank, the Compliance Management Division supervises legal risk management and is responsible for taking proactive measures to prevent: (1) accidents and fraud, which may lead to breaches of laws and other applicable regulations and standards; and (2) lawsuits and other disputes. The Compliance Management Division is also responsible for rapidly identifying potential sources of disputes and lawsuits to facilitate appropriate responses and resolutions, and for taking necessary measures to prevent reoccurrence of such disputes.

Settlement Risk Management

Settlement risk is defined as the risk of loss arising from the failure to finalize settlements as planned. Settlement risk comprises a wide range of risks, such as credit and liquidity risk, administrative risk and systems risk.

A major component of settlement risk is the timing differences that arise between the payment and receipt of funds, and the payment and delivery of securities. This type of risk is not limited to foreign exchange transactions, which arises from the timing of settlements across international time zones, but also occurs within domestic transactions in a variety of contexts.

The Bank has set limits on settlement volumes for foreign exchange transactions by each client, and adopted a policy of reducing settlement volumes by using netting techniques. The Bank is also working to shorten time intervals between the payment and receipt of funds.

Before participating in various settlement systems, the Bank makes sure it thoroughly understands the relevant rules of settlement systems. At the same time, the Bank monitors actual settlement situations in real time in accordance with changes to Real-Time Gross Settlement (RTGS) of the Bank of Japan Financial Network System (BOJ-NET). The Bank is also upgrading its settlement risk management systems by carefully studying the inherent risks of individual financial products and settlement systems.

Information Security Management

Information assets, including personal data, are just as important for a financial institution as tangible assets. However, information assets are vulnerable to a wide range of risks, such as accidents, disasters, system errors, unauthorized use, damage, theft, information leakage and data manipulation. Therefore, protecting information assets by such measures as information leakage prevention is critical to the fulfilment of the Bank's confidentiality obligations to its clients and the safeguarding of the entire organization.

Guided by the Information Security Policy, Aozora Bank, including its consolidated subsidiaries, assesses the exposure of its information assets to various risks and manages these risks to ensure the security of information systems.

The Bank's executive officer responsible for the Compliance Management Division acts as the Chief Information Asset Management Administrator, taking all necessary measures to ensure that the Bank's information assets are secure, and reports on asset security to the Board of Directors.

In addition, the Bank's main headquarters-based divisions, in line with their role of managing information assets, develop security plans and provide guidance to the Information Asset Management Administrator assigned to individual divisions, departments and branches, and resolve problems when they arise. The Compliance Management Division assists the officers responsible for information assets, thus ensuring strict implementation of the control system.

Liquidity Risk Management

There are two types of liquidity risk: funding liquidity risk, which is the risk that the Bank becomes unable to raise the funds necessary for various fund settlements; and market liquidity risk, which is the risk that the Bank becomes unable to unwind trading positions at reasonable market prices due to a number of factors, including market turmoil.

Funding Liquidity Risk Management

The Financial Management Division centrally manages yen and foreign-currency denominated funds and puts limits on funding gaps for specific periods. The division ensures that the Bank's funding capabilities are sufficient to meet its contractual obligations. At the same time, the Risk Management Division ensures that the management process is appropriate and effective through the maintenance of adequate checks and balances. The Board of Directors and other management bodies prepare monthly and semiannual plans for the investment and procurement of funds. The Financial Management Division reports directly to the Bank's senior management on liquidity issues, on a daily basis.

Market Liquidity Risk Management

The Risk Management Division analyzes trading positions relative to market size and reports to the Bank's senior management on market liquidity risk. Trading positions are closely monitored to ensure that they do not become excessive.

Reduction of Problem Loans and Analysis of Assets

Disclosure of Claims under the Financial Reconstruction Law (Improvement of Asset Quality)

The Bank is addressing the reduction of problem loans as one of management's key tasks. Based on stringent internal self-assessment standards, the Bank makes the appropriate write-offs and reserve provisions, and carries out the disposal of problem loans where that is deemed optimal, after considering a course of action for each individual problem loan.

In the fiscal year ended March 31, 2004, disclosed claims under the Financial Reconstruction Law amounted to ¥88.7 billion, a significant reduction compared with the ¥202.5 billion disclosed at the end of the previous period. This decrease was the result of a combination of measures aimed at removing such assets from the Bank's balance sheet, including the collection of problem loans, the sale of some claims and write-offs. As a result, the disclosed claim ratio fell from 5.97% at the end of the previous period to 2.95% as of March 31, 2004. The Bank will continue to pursue the reduction of problem loans.

Disclosed Claims Pursuant to the Financial Reconstruction Law

(Billions of Yen)

	2004	2003	Change
Disclosed claims pursuant to the Financial Reconstruction Law			
Bankrupt and similar credit	17.8	13.5	4.3
Doubtful credit	59.0	93.3	(34.3)
Substandard credit	11.9	95.7	(83.8)
Subtotal (A)	88.7	202.5	(113.8)
Normal credit	2,907.4	3,186.1	(278.7)
Total credit (B)	2,996.1	3.388.6	(392.5)
(A/B)	2.95%	5.97%	(3.02%)

Removal of Doubtful and Bankrupt and Similar Claims from the Balance Sheet

The Bank has endeavored to effectively and rapidly reduce the amount of problem loans on its balance sheet, employing a variety of methods within an economically rational approach. During the fiscal year ended March 31, 2004, claims newly classified as bankrupt and similar or doubtful, within disclosed claims under the Financial Reconstruction Law, totaled ¥96.0 billion, while liquidated and written-off claims in the same two categories amounted to ¥126.0 billion. As a result, total claims in these two categories as of March 31, 2004, fell ¥30.0 billion compared with the end of the previous period. This has been achieved by formulating a disposal plan for each individual obligor, thereby carrying out the disposal of loans in a well-planned manner.

Removal of Doubtful and Bankrupt and Similar Claims from the Balance Sheet

(Billions of Yen)

	2004	2003
Disposals through borrower liquidation	(2.3)	(61.1)
Disposals through borrower reorganization	(1.9)	(0.4)
Reductions due to improvement in borrower performance	—	(35.6)
Loan sales to secondary market	(90.3)	(183.1)
Write-offs	2.5	7.5
Other (recovery, repayment)	(34.0)	(32.4)
Subtotal (A)	(126.0)	(305.0)
Claims newly classified as:		
Bankrupt and similar	3.7	14.2
Doubtful	92.3	70.2
Subtotal (B)	96.0	84.4
Total (A+B)	(30.0)	(220.7)

Notes: 1. Amounts shown are the sum of amounts for the first half and second half of each fiscal period.
2. Disposals through borrower liquidation: discharge and write-off of claims against borrowers undergoing bankruptcy liquidation; Disposals through borrower reorganization: discharge of claims against borrowers undergoing bankruptcy reorganization and abandonment of claims against borrowers undergoing private resolution; Other: recovery through disposal of collateral and improvement in borrower position
3. For claims written off, where the borrower subsequently undergoes legal or private resolution leading to claim discharge or abandonment, the written-off amount is reduced accordingly and then recorded as either a disposal through borrower liquidation or a disposal through borrower reorganization.

Self-Assessments, Write-Offs and Reserves

Self-assessments, which involve an examination of asset quality and probability of collection for each of its assets, are conducted by the Bank based on internal self-assessment standards developed in accordance with the Financial Services Agency's *Financial Inspection Manual*. Self-assessments are the basis on which the Bank carries out the appropriate write-offs and reserve provisions to preserve the soundness of its assets.

Self-assessments divide borrowers into five categories. Assets are then classified into four categories according to the probability of collection, which is assessed by taking into account any underlying collateral, guarantees or other security. (Please refer to page 29 for Definitions of Borrower Categories, Definitions of Asset Classifications and Write-Off and Reserve Provision Rules.)

As of March 31, 2004, reserve provision ratios for each category of borrower, based on self-assessments, were as follows.

Reserve Provision Ratios for Each Category of Borrower, Based on Self-Assessments

(%)

Definition of Borrower Categories	2004	2003
Normal	1.9	1.8
Watch list:		
Other watch list borrowers	17.1	19.7
Substandard borrowers (Ratio of reserve-to-unsecured)	92.2	58.1
Potentially bankrupt (Ratio of reserve-to-unsecured)	85.6	86.9
Substantially bankrupt and bankrupt (Ratio of reserve-to-unsecured)	100.0	100.0

Credit-Related Expenses

In the fiscal year ended March 31, 2004, the Bank recorded losses arising from the write-off of loans, the sale of claims and other measures that were part of its efforts to reduce problem loans. Credit-related expenses amounted to ¥6.5 billion for the period, consisting of the net reversal of reserve provisions due to asset quality improvement and additional reserves set aside, as the credit assessment criteria became more stringent.

Credit-Related Expenses

(Billions of Yen)

	2004	2003
Expenses for the disposal of problem loans	38.9	7.1
Loan write-offs	8.3	11.9
Provision to (reversal of) specific reserve	17.3	(10.2)
Provision for country risk reserve	(0.7)	0.7
Loss on the sale of other receivables and other items	14.0	4.6
Provision to (reversal of) general loan-loss reserve	(32.4)	(8.5)
Credit-related expenses	6.5	(1.4)

Coverage Ratios of Disclosed Claims under the Financial Reconstruction Law

Total disclosed claims under the Financial Reconstruction Law amounted to ¥88.7 billion, while reserve provisions, collateral and guarantees amounted to ¥83.9 billion, resulting in a coverage ratio of 94.6%.

Disclosed Claims Pursuant to the Financial Reconstruction Law (After Partial and Direct Write-Offs, Non-Consolidated Basis)

(Billions of Yen)

	2004	2003
Disclosed claims under the Financial Reconstruction Law (A)	88.7	202.5
Normal credit	2,907.4	3,186.1
Total credit (B)	2,996.1	3,388.6
(A/B)	2.95%	5.97%
Credit secured:		
Reserve for possible loan losses (C)	29.9	60.3
Collateral and guarantees (D)	54.0	113.2
Total (E=C+D)	83.9	173.5
Coverage ratio (E/A)	94.6%	85.7%
Reserve ratio (C/(A-D))	86.1%	67.5%

Note: Reserve for possible loan losses (C) is the sum of provisions to the specific reserve for possible loan losses on disclosed claims under the Financial Reconstruction Law plus general loan-loss reserve.

Risk-Monitored Loans

In addition to disclosed claims under the Financial Reconstruction Law, the Bank also discloses risk-monitored loans under the Banking Law. As of March 31, 2004, risk-monitored loans (on a non-consolidated basis) amounted to ¥88.7 billion, compared with ¥199.7 billion at the end of the previous period.

Risk-Monitored Loans (After Partial and Direct Write-Offs)

<Non-Consolidated>

(Billions of Yen)

	2004	2003
Risk-monitored loans:		
Loans to bankrupt companies	11.4	9.2
Past due loans	65.9	99.0
Loans overdue for three months or more	—	1.3
Restructured loans	11.3	90.2
Total (A)	88.7	199.7
Year-end balance of total loans (B)	2,969.8	3,271.1
(A/B)	3.0%	6.1%

<Consolidated>

(Billions of Yen)

	2004	2003
Risk-monitored loans:		
Loans to bankrupt companies	11.5	9.2
Past due loans	66.0	99.0
Loans overdue for three months or more	—	1.3
Restructured loans	11.4	90.2
Total (A)	88.9	199.8
Year-end balance of total loans (B)	2,965.6	3,258.7
(A/B)	3.0%	6.1%

Self-Assessment, Disclosed Claims, Write-Offs, Reserves and Risk-Monitored Loans (After Partial and Direct Write-Offs, Non-Consolidated Basis)

(Billions of Yen)

Borrower categories for self-assessment	Disclosed claims pursuant to the Financial Reconstruction Law: Loans	Disclosed claims pursuant to the Financial Reconstruction Law: Other	Reserve and coverage for claims under the Financial Reconstruction Law	Reserve-to-unsecured-credit ratio	Reserve and coverage ratio	Risk-monitored loans
Bankrupt borrowers Substantially bankrupt borrowers	Bankrupt and similar credit 17.8		Collateral/Guarantee coverage 17.2 Reserve 0.6 (Partial, direct write-offs of loans 7.9)	(100.0%)	100.0%	Loans to bankrupt companies 11.4
Potentially bankrupt borrowers	Doubtful credit 59.0		Collateral/Guarantee coverage 29.6 Reserve 25.1 Estimated collections 4.2	85.6%	92.8%	Past due loans 65.9
Watch list borrowers	Substandard credit 11.9		Collateral/Guarantee coverage 7.2 Reserve 4.1 Estimated collections 0.6	87.4%	95.0%	Loans overdue for three months or more — Restructured loans 11.3
Normal borrowers	(Normal credit 2,907.4)					

Disclosed claims pursuant to the Financial Reconstruction Law 88.7	Collateral/Guarantee coverage 54.0 Reserve 29.9 Estimated collections 4.8	Reserve ratio for disclosed claims under the Financial Reconstruction Law 86.1%	Reserve and coverage ratio for disclosed claims under the Financial Reconstruction Law 94.6%	Risk-monitored loans 88.7
Total credit 2,996.1	Total reserve 162.3			

Reserve-to-unsecured-credit ratio = Reserve ÷ (Claims – Collateral, guarantees, etc.)
Reserve and coverage ratio = (Collateral, guarantees, etc. + Reserve) ÷ Claims

<Definitions of Borrower Categories>

Normal Business performance is strong and no special financial problems exist.

Watch list Borrowers that need to be monitored carefully because of weak business fundamentals, financial problems or problematic lending conditions.

Potentially bankrupt Borrowers that are not currently bankrupt but are highly likely to become bankrupt.

Substantially bankrupt Borrowers that are substantially bankrupt but are not legally or practically bankrupt yet.

Bankrupt Borrowers that are legally or practically bankrupt.

<Definitions of Asset Classifications>

Category I Assets that present no particular risk of collectability nor impairment of value.

Category II Assets, including credits, which bear above-average risk of collectability.

Category III Assets that bear substantial risk of final collectability or impairment of value, and are likely to incur losses.

Category IV Assets deemed to be uncollectable or valueless.

<Write-Off and Reserve Provision Rules>

Normal and watch list borrowers Based on historical bankruptcy rates, normal status borrowers, special attention borrowers and other watch list borrowers are classified and across-the-board provisions are made to the general loan-loss reserve.

Potentially bankrupt borrowers For each borrower, the expected recovery amount of category III assets (non-secured portion) is estimated and a provision is made to the specific loan-loss reserve for the amount of shortfall. The expected recovery amount is the discounted present value of the estimated cash flows from future recovery of the loan principal.

Substantially bankrupt and bankrupt borrowers In principle, the full amounts of category III and IV credits are written off directly.

<Definitions of Disclosed Claims Pursuant to the Financial Reconstruction Law>

Bankrupt and similar credit Bankrupt and de facto bankrupt refers to the credit of borrowers who are in a state of bankruptcy, corporate reorganization, composition, etc., and the equivalent thereof.

Doubtful credit Doubtful refers to credit with serious doubt concerning the recovery of principal and receiving of interest as contract provisions, because the borrower's financial condition and business results have worsened, although they have not reached the point of management collapse.

Substandard credit Special attention refers to loans in arrears for more than three months or with mitigated conditions.

Normal credit Normal credit refers to credit to borrowers whose financial condition and business results have no particular problem and which are not categorized in any of the above categories.

<Risk-Monitored Loans>

Loans to bankrupt companies Loans to bankrupt companies are loans for which interest in arrears has not been accrued because recovery or settlement of principal or interest is unlikely due to the prolonged delay in payment of principal or interest (which hereafter shall be called "non-accrual loans") and whose borrowers are legally bankrupt (defined below), excluding the amount of write-offs.

1. Borrowers that have applied for commencement of company or financial institution reorganization procedures pursuant to the provisions of the Corporate Reorganization Law.
2. Borrowers that have applied for reorganization pursuant to the provisions of the Civil Reorganization Law.
3. Borrowers that have applied for bankruptcy pursuant to the provisions of the Bankruptcy Law.
4. Borrowers that have applied to commence liquidation or special liquidation pursuant to the provisions of the Commercial Law.
5. Borrowers with reasons equivalent to 1. to 4. above as defined by Ministry of Finance ordinances.
6. Borrowers who have applied for commencement of legal liquidation procedures pursuant to overseas laws, corresponding to those listed above.

Past due loans Past due loans refer to non-accrual loans except those for which concessions on payment of interest were made in order to assist the reorganization of bankrupt companies and loans to them.

Loans overdue for three months or more Loans overdue for three months or more refers to those loans, excluding loans to bankrupt companies and past due loans for which principal or interest remains unpaid for at least three months.

Restructured loans Restructured loans refer to those loans, excluding loans to bankrupt companies, past due loans and loans overdue for three months or more for which agreement was made to provide reduction or a moratorium on interest payments, or concessions in the borrower's favor on interest or principal payments or to waive claims for the purpose of assisting the reconstruction of insolvent borrowers.

<Differences between Disclosed Claims Pursuant to the Financial Reconstruction Law and Risk-Monitored Loans>

- **Disclosed Claims**
  - Disclosure: Loans and other claims (securities loaned, foreign exchange, suspense payments, etc.)
  - Disclosed: By borrower (by loan for substandard credit)
- **Risk-Monitored Loans**
  - Disclosure: Loans only
  - Disclosed: By loan

Progress in Implementing the Business Revitalization Plan

Aozora Bank considers the implementation of the Business Revitalization Plan an integral part of its management strategy, and strives to meet the targets contained therein. The plan was formulated in accordance with the Financial Function Early Strengthening Law and implemented in September 2000 following approval by the Financial Reconstruction Commission. This allowed the Bank to issue ¥260 billion in preferred stocks to be paid for with public funds.

The Business Revitalization Plan is reviewed biennially. In August 2003, the Financial Services Agency announced the results of the latest review. In accordance with this review, and based on the Trinity Plan, we will aim to achieve the targets outlined in the Business Revitalization Plan by reinforcing our profit-earning capabilities. In particular, we will focus on: (1) finance for medium-sized companies, (2) revitalization business and (3) the structuring and securitization of financial products. To achieve its objectives, the Bank is implementing organizational reforms and developing its personnel systems, including staff transfers.

Business Performance

Since the implementation of the Business Revitalization Plan in 2000, Aozora Bank has regularly achieved the major business targets contained therein in terms of net income and other performance indicators.

In the fiscal year ended March 31, 2004, results were satisfactory as we recorded ¥31.9 billion in net income, an increase of ¥9.0 billion compared with the previous period. This result was due to (1) an increase in net non-interest income, (2) effective control of general and administrative expenses and (3) interest income earned as a result of favorable spreads and low interest rate funding.

Business Overview

The Bank will continue to successfully achieve its targets by (1) expanding its business with medium-sized companies and other corporate banking clients, (2) fostering its real estate finance business, (3) developing its revitalization business and (4) becoming proactively involved in the structuring and securitization of financial products. Going forward, the Bank will further strengthen its operations in these areas and enter such new businesses as foreign-currency investments.

Business Revitalization Plan

(Billions of Yen)

	2004		2005	2006	2007
Years ended/ending March 31,	Plan	Result	Plan	Plan	Plan
Net revenue	81.0	81.6	88.5	98.0	105.5
General and administrative expenses	41.0	39.2	41.5	42.0	42.5
Business profit before general loan-loss reserve	40.0	42.5	47.0	56.0	63.0
Net income	30.0	31.9	40.0	42.0	58.0

Note: The above targets were announced in August 2003.

Financial Information and Corporate Data

Consolidated Financial Highlights [Five-Year Summary]

Years Ended March 31

(Millions of Yen)

	2004	2003	2002	2001	2000
Operating income	113,788	109,748	106,700	275,730	223,909
Ordinary profit (loss)	7,606	8,920	14,355	99,116	(112,592)
Net income	30,530	23,376	18,703	98,331	112
Capital stock	419,781	419,781	419,781	419,781	353,114
Total stockholders' equity	526,848	497,514	477,046	460,876	1,229
Total assets	5,176,005	5,885,642	5,684,072	6,163,766	8,346,327
Debentures	1,054,973	1,470,126	1,468,193	2,479,408	3,709,377
Deposits	2,588,030	2,537,175	2,164,641	1,771,373	2,620,980
Loans and bills discounted	2,965,552	3,258,693	3,297,993	3,089,490	4,102,509
Securities	964,964	1,350,036	1,054,019	721,477	1,073,210
Total stockholders' equity per share (in yen)	85.63	75.29	68.07	62.36	0.39
Basic net income per share (in yen)	9.54	7.02	5.37	35.80	0.04
Diluted net income per share (in yen)	7.21	5.52	4.95	29.40	0.03
Consolidated capital adequacy ratio (domestic standard) (%)	15.66	13.30	14.05	15.13	—
Net cash provided by (used in) operating activities	(305,027)	105,182	923,515	(1,116,186)	453,607
Net cash provided by (used in) investing activities	360,100	(347,870)	(376,664)	459,986	(30,168)
Net cash provided by (used in) financing activities	(7,827)	(24,261)	(20,803)	235,036	(28,309)
Cash and cash equivalents, end of year	338,117	290,872	557,822	31,774	453,037

Notes: 1. Up to and including the fiscal year ended March 31, 2002, total stockholders' equity per share was calculated by dividing total stockholder's equity at the fiscal year-end, less the product of the number of preferred shares issued and outstanding at the fiscal year-end and the issue price, by the number of common shares issued and outstanding at the fiscal year-end, excluding treasury stock and parent company shares held by consolidated subsidiaries. However, since total stockholders' equity in the Bank was nil (¥0) for the fiscal year ended March 31, 2000, total stockholders' equity per share for that year is calculated by dividing total stockholders' equity at the fiscal year-end by the number of shares issued and outstanding at the fiscal year-end, excluding treasury stock and parent company shares held by consolidated subsidiaries.

2. Up to and including the fiscal year ended March 31, 2002, basic net income per share was calculated by dividing consolidated net income, less total dividends on preferred shares for the fiscal year ended March 31, 2002, by the average number of common shares issued and outstanding during the fiscal year ended March 31, 2002, excluding treasury stock and parent company shares and parent company shares held by consolidated subsidiaries.

3. From the fiscal year ended March 31, 2003, total stockholders' equity per share, basic net income per share and diluted net income per share are calculated by applying Financial Accounting Standard No. 2, "Accounting Standard for Earnings per Share" and Financial Accounting Standards Implementation Guidance No. 4, "Implementation Guidance for Accounting Standard for Earnings per Share."

Consolidated Financial Review

1. Consolidation and Equity-Method Companies

The consolidated financial statements as of March 31, 2004, include the accounts of the Bank and its nine consolidated subsidiaries. During the fiscal year under review, one consolidated subsidiary was newly included owing to the acquisition of its stock and one consolidated subsidiary was eliminated owing to its liquidation. No companies were accounted for using the equity method.

Consolidation and Equity-Method Companies

March 31

(Number of Companies)

	2004	2003	Change
Consolidated subsidiaries	9	9	0
Affiliated companies	0	0	0

2. Income Analysis

For the fiscal year ended March 31, 2004, in addition to recording healthy growth in net interest income, the net non-interest portion of consolidated net revenue (net fees and commissions, net trading revenues and net other operating income) grew 33.7%. General and administrative expenses remained tightly constrained and total credit-related expenses were limited to ¥7.3 billion. As a result, net income rose 30.6%, to ¥30.5 billion.

Income Analysis

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Consolidated net revenue (Note 1)	**86,797**	**76,828**	**9,969**
Net interest income	63,736	59,575	4,161
Net fees and commissions	8,732	7,388	1,343
Net trading revenues	2,865	3,446	(581)
Net other operating income	11,462	6,416	5,045
General and administrative expenses	**(45,201)**	**(42,565)**	**(2,636)**
Credit-related expenses	**(29,958)**	**(16,549)**	**(13,408)**
Gain and loss on stock transactions and loss on write-down of equity securities	**4**	**(1,079)**	**1,084**
Other income (loss)	**(4,035)**	**(7,712)**	**3,677**
Ordinary profit	**7,606**	**8,920**	**(1,314)**
Special income (loss) (Note 2)	**23,525**	**11,690**	**11,835**
Income before income taxes and minority interests	**31,131**	**20,610**	**10,520**
Current income taxes	**(495)**	**(891)**	**396**
Deferred income taxes	**80**	**3,592**	**(3,512)**
Minority interests in net income	**(186)**	**64**	**(251)**
Net income	**30,530**	**23,376**	**7,154**
Total credit-related expenses (Note 3)	**(7,285)**	**1,157**	**(8,443)**
Reversal of reserve for possible loan losses	22,672	17,344	5,327

Notes: 1. Consolidated net revenue = (Interest income – Interest expenses) + (Fees and commissions (income) – Fees and commissions (expenses)) + (Trading profits – Trading losses) + (Other operating income – Other operating expenses)

2. Reversal of reserve for possible loan losses exceeded provisions to this reserve, resulting in a surplus, which was recorded as a special income item.

3. Total credit-related expenses = Credit-related expenses (Net provision to general loan-loss reserve + Disposal of problem loans) + Reversal of reserve for possible loan losses posted as special income (Reversal of reserve for possible loan losses + Reversal of reserve for credit losses on off-balance-sheet instruments)

(1) Consolidated net revenue

Despite lower yields from loans and bills discounted and securities, net interest income increased ¥4.2 billion, to ¥63.7 billion. This rise was mainly attributable to improved efficiency in fund procurement, which resulted in lower interest expenses. Net fees and commissions, which were considerably bolstered by fees relating to the Bank's lending operations, climbed ¥1.3 billion, to ¥8.7 billion. Net trading revenues amounted to ¥2.9 billion. Net other operating income jumped ¥5.0 billion, to ¥11.5 billion, mainly owing to robust growth in income from derivatives and a strong result from the Bank's servicer subsidiary, AOZORA Loan Services. As a result, consolidated net revenue increased ¥10.0 billion, to ¥86.8 billion.

Consolidated Net Revenue

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net interest income	**63,736**	**59,575**	**4,161**
Interest income	80,651	84,172	(3,521)
Interest expenses	16,914	24,596	(7,682)
Net fees and commissions	**8,732**	**7,388**	**1,343**
Fees and commissions (income)	9,593	8,123	1,469
Fees and commissions (expenses)	860	734	126
Net trading revenues	**2,865**	**3,446**	**(581)**
Trading profits	2,865	3,446	(581)
Trading losses	—	—	—
Net other operating income	**11,462**	**6,416**	**5,045**
Other operating income	16,748	9,630	7,118
Other operating expenses	5,286	3,213	2,072
Consolidated net revenue	**86,797**	**76,828**	**9,969**

Note: For further details on net interest income, net fees and commissions, net trading revenues and net other operating income, please refer to page 61.

(2) General and administrative expenses

In the context of substantial growth in consolidated net revenue, tight cost control measures allowed us to limit the increase in general and administrative expenses, which rose ¥2.6 billion, to ¥45.2 billion.

(3) Total credit-related expenses

In addition to the steady disposal of problem loans, the Bank also carried out rigorous write-offs and reserve provisions, which resulted in total credit-related expenses of ¥7.3 billion. In accordance with the relevant accounting standards, the reversal of reserve for possible loan losses of ¥22.7 billion (the amount exceeding provisions to the reserve) was recorded within special income.

(4) Gain and loss on stock transactions and loss on write-down of equity securities

The Bank's holdings of equity securities are negligible. As a result, there was no significant impact on net income for the period under review.

(5) Ordinary profit

Ordinary profit amounted to ¥7.6 billion. Although this result represented a decline of ¥1.3 billion compared with the previous period, this was mainly attributable to the reversal of reserve for possible loan losses being posted as special income.

(6) Special income

Largely owing to the reversal of reserve for possible loan losses, special income amounted to ¥23.5 billion.

(7) Net income

Income before income taxes and minority interests increased ¥10.5 billion, to ¥31.1 billion. After adjustments for income taxes and other items, net income for the period under review amounted to ¥30.5 billion.

3. Balance Sheet Analysis

Assets and Liabilities

March 31

(Millions of Yen)

	2004	2003	Change
Assets	**5,176,005**	**5,885,642**	**(709,637)**
Loans and bills discounted	2,965,552	3,258,693	(293,140)
Securities	964,964	1,350,036	(385,071)
Trading account assets	488,449	532,291	(43,841)
Other assets	140,538	124,360	16,178
Deferred tax assets	12,323	13,777	(1,453)
Customers' liabilities for acceptances and guarantees	23,253	114,329	(91,075)
Reserve for possible loan losses	(162,247)	(199,045)	36,798
Liabilities	**4,648,453**	**5,387,447**	**(738,993)**
Debentures	1,054,973	1,470,126	(415,153)
Deposits (excluding negotiable certificates of deposit)	2,039,910	2,119,669	(79,758)
Negotiable certificates of deposit	548,120	417,506	130,614
Call money and bills sold	420,042	574,895	(154,852)
Other liabilities	182,811	298,798	(115,987)
Acceptances and guarantees	23,253	114,329	(91,075)
Minority interests	**703**	**681**	**22**
Total stockholders' equity	**526,848**	**497,514**	**29,334**

(1) Assets

Loans and bills discounted declined ¥293.1 billion, to ¥2,965.6 billion, mainly owing to ongoing efforts to dispose of non-performing assets. Securities decreased ¥385.1 billion, to ¥965.0 billion, which was largely attributable to the disposal of Japanese government bonds, as part of the appropriate management of the Bank's securities portfolio. Reserve for possible loan losses declined ¥36.8 billion, to ¥162.2 billion, owing to further progress in the disposal of problem loans. Consequently, assets decreased ¥709.6 billion, to ¥5,176.0 billion.

(2) Liabilities and minority interests

Within the context of the Bank's efforts to hold down procurement costs and bolster efficiency in fund procurement, debentures decreased ¥415.2 billion, to ¥1,055.0 billion. The combined balance of deposits and negotiable certificates of deposit rose ¥50.9 billion, to ¥2,588.0 billion, partly reflecting strong growth in time deposits held by retail clients. As a result, total liabilities fell ¥739.0 billion, to ¥4,648.5 billion. Minority interests increased slightly, to ¥703 million.

(3) Stockholders' equity

During the period under review, the payment of cash dividends on preferred stock and an increase in retained earnings resulted in a rise in total stockholders' equity of ¥29.3 billion, to ¥526.8 billion.

4. Consolidated Capital Adequacy Ratio (Domestic Standard)

March 31

(Millions of Yen)

		2004	2003
Tier I	Capital	419,781	419,781
	Non-cumulative perpetual preferred stock	272,036	272,036
	Newly issued stock	—	—
	Capital surplus	33,333	33,333
	Retained earnings	66,724	39,585
	Minority interest in consolidated subsidiaries	703	681
	Preferred stock issued overseas	—	—
	Net unrealized losses on available-for-sale securities	—	—
	Paid-in amount on treasury stock	—	—
	Treasury stock	0	0
	Foreign currency translation adjustments	—	—
	Goodwill	—	—
	Amount equal to consolidation adjustments	—	—
	Total (A)	**520,542**	**493,381**
	Step-up preferred stock	—	—
Tier II	Forty-five percent of the difference between fair value and book value in respect of land	—	—
	General reserve for possible loan losses	21,669	24,630
	Subordinated debt	1,080	6,598
	Total	**22,749**	**31,228**
	Tier II capital qualifying as capital (B)	**22,749**	**31,228**
Items deducted	**(C)**	**146**	**146**
Capital	**(A) + (B) – (C) (D)**	**543,145**	**524,464**
Risk-weighted assets	Balance-sheet exposure	3,266,608	3,811,435
	Off-balance-sheet exposure	200,542	129,502
	Total (E)	**3,467,150**	**3,940,938**
Capital adequacy ratio (domestic standard)	$\frac{(D)}{(E)} \times 100$	**15.66%**	**13.30%**
Tier I ratio (domestic standard)	$\frac{(A)}{(E)} \times 100$	**15.01%**	**12.51%**

Notes: 1. The capital adequacy ratio is calculated using the formula stipulated in a Ministry of Finance Notification based on Article 14-2 of the Banking Law, which follows the provisions of Article 17 of the Long-Term Credit Bank Law. The Bank uses the domestic standard.

2. Items deducted (C) is equivalent to the amount held at other financial institutions for their capital-raising purposes. This amount is not included in the consolidated financial statements.

Consolidated Balance Sheets

Aozora Bank, Ltd. and Consolidated Subsidiaries
March 31, 2004 and 2003

ASSETS	Millions of Yen 2004	Millions of Yen 2003	Thousands of U.S. Dollars (Note 1) 2004
Cash and cash equivalents (Note 3)	¥ 338,117	¥ 290,872	$ 3,200,358
Due from banks	46,546	80,220	440,570
Call loans and bills bought	25,431	27,744	240,715
Receivables under securities borrowing transactions	211,821	166,730	2,004,937
Commercial paper and other debt purchased	90,350	89,272	855,192
Trading account assets (Notes 4, 11 and 24)	488,449	532,291	4,623,284
Money held in trust	344		3,256
Securities (Notes 5 and 11)	964,964	1,350,036	9,133,597
Loans and bills discounted (Notes 6 and 11)	2,965,552	3,258,693	28,069,594
Foreign exchanges (Note 7)	1,355	2,956	12,834
Other assets (Note 15)	140,538	124,360	1,330,225
Premises and equipment (Note 8)	29,048	33,218	274,954
Deferred charges	153	184	1,449
Customers' liabilities for acceptances and guarantees (Note 9)	23,253	114,329	220,100
Deferred tax assets (Note 22)	12,323	13,777	116,649
Reserve for possible loan losses (Note 10)	(162,247)	(199,045)	(1,535,706)
TOTAL	¥5,176,005	¥5,885,642	$48,992,008

LIABILITIES AND STOCKHOLDERS' EQUITY	Millions of Yen 2004	Millions of Yen 2003	Thousands of U.S. Dollars (Note 1) 2004
LIABILITIES:			
Debentures (Note 12)	¥1,054,973	¥1,470,126	$ 9,985,548
Deposits (Notes 11 and 13)	2,588,030	2,537,175	24,496,269
Call money and bills sold (Note 11)	420,042	574,895	3,975,797
Payables under repurchase agreements (Note 11)	131,598	204,797	1,245,605
Payables under securities lending transactions (Note 11)	97,322		921,179
Commercial paper	5,000	3,000	47,326
Trading account liabilities (Note 4)	88,529	140,642	837,955
Borrowed money (Notes 11 and 14)	28,015	23,610	265,168
Foreign exchanges (Note 7)	2	2	26
Other liabilities (Note 15)	184,557	300,360	1,746,880
Liability for employees' retirement benefits (Note 16)	19,253	17,901	182,243
Reserve for credit losses on off-balance-sheet instruments	7,872	604	74,517
Other reserves			2
Acceptances and guarantees (Note 9)	23,253	114,329	220,100
Total liabilities	4,648,453	5,387,447	43,998,615
MINORITY INTERESTS	703	681	6,657
STOCKHOLDERS' EQUITY:			
Capital stock (Note 17):			
Common stock	147,745	147,745	1,398,439
Preferred stock	272,036	272,036	2,574,880
Capital surplus (Note 17)	33,333	33,333	315,508
Retained earnings (Notes 17 and 26)	70,335	43,293	665,739
Unrealized gain on available-for-sale securities	3,398	1,106	32,170
Total stockholders' equity	526,848	497,514	4,986,736
TOTAL	¥5,176,005	¥5,885,642	$48,992,008

See notes to consolidated financial statements.

Consolidated Statements of Income

Aozora Bank, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2004 and 2003

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2004	2003	2004
INCOME:			
Interest on:			
Loans and discounts	¥ 61,692	¥ 64,989	$ 583,935
Securities	5,789	8,040	54,799
Due from banks	390	514	3,700
Other	12,778	10,628	120,952
Fees and commissions	9,593	8,123	90,802
Trading account profits	2,865	3,446	27,125
Other operating income (Note 18)	16,748	9,630	158,530
Other income (Note 19)	27,637	23,512	261,592
Total income	137,496	128,885	1,301,435
EXPENSES:			
Interest on:			
Debentures	5,948	12,613	56,305
Deposits	9,092	8,700	86,067
Borrowings and rediscounts	715	1,081	6,773
Commercial paper			2
Other	1,157	2,200	10,957
Fees and commissions	860	734	8,148
Other operating expenses (Note 20)	5,286	3,213	50,035
General and administrative expenses	45,201	42,565	427,844
Other expenses (Note 21)	38,101	37,164	360,635
Total expenses	106,364	108,274	1,006,766
INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS	31,131	20,610	294,669
INCOME TAXES (Note 22):			
Current	495	891	4,686
Deferred	(80)	(3,592)	(761)
Total income taxes	414	(2,701)	3,925
MINORITY INTERESTS IN NET INCOME (LOSS)	186	(64)	1,762
NET INCOME	¥ 30,530	¥ 23,376	$ 288,982

	Yen		U.S. Dollars
	2004	2003	2004
PER SHARE OF COMMON STOCK (Notes 2.q and 25):			
Basic net income	¥9.54	¥7.02	$0.09
Diluted net income	7.21	5.52	0.07
Cash dividends of the fourth preferred stock	5.00	5.00	0.05
Cash dividends of the fifth preferred stock	3.72	3.72	0.04

See notes to consolidated financial statements.

CONSOLIDATED FINANCIAL INFORMATION

Consolidated Statements of Stockholders' Equity

Aozora Bank, Ltd. and Consolidated Subsidiaries

Years Ended March 31, 2004 and 2003

	Thousands		Millions of Yen					
	Issued Number of Shares							
	Common Stock	Preferred Stock	Common Stock	Preferred Stock	Capital Surplus	Retained Earnings	Unrealized Gain (Loss) on Available-for-sale Securities	Foreign Currency Translation Adjustments
BALANCE, APRIL 1, 2002	2,834,870	914,811	¥147,745	¥272,036	¥33,333	¥23,381	¥ (235)	¥ 785
Net income						23,376		
Cash dividends on preferred stock						(3,464)		
Net decrease in unrealized loss on available-for-sale securities							1,341	
Net decrease in foreign currency translation adjustments								(785)
BALANCE, MARCH 31, 2003	2,834,870	914,811	147,745	272,036	33,333	43,293	1,106	
Net income						30,530		
Exclusion of consolidated subsidiaries previously included in consolidated accounts						(24)		
Cash dividends on preferred stock						(3,464)		
Net increase in unrealized gain on available-for-sale securities							2,292	
BALANCE, MARCH 31, 2004	2,834,870	914,811	¥147,745	¥272,036	¥33,333	¥70,335	¥3,398	

	Thousands of U.S. Dollars (Note 1)					
	Common Stock	Preferred Stock	Capital Surplus	Retained Earnings	Unrealized Gain (Loss) on Available-for-sale Securities	Foreign Currency Translation Adjustments
BALANCE, MARCH 31, 2003	$1,398,439	$2,574,880	$315,508	$409,784	$10,469	
Net income				288,982		
Exclusion of consolidated subsidiaries previously included in consolidated accounts				(233)		
Cash dividends on preferred stock				(32,794)		
Net increase in unrealized gain on available-for-sale securities					21,701	
BALANCE, MARCH 31, 2004	$1,398,439	$2,574,880	$315,508	$665,739	$32,170	

See notes to consolidated financial statements.

CONSOLIDATED FINANCIAL INFORMATION

Consolidated Statements of Cash Flows

Aozora Bank, Ltd. and Consolidated Subsidiaries

Years Ended March 31, 2004 and 2003

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2004	2003	2004
OPERATING ACTIVITIES:			
Income before income taxes and minority interests	¥ 31,131	¥ 20,610	$ 294,669
Adjustments for:			
Depreciation and amortization	1,112	8,622	10,532
Amortization of goodwill	107		1,014
Decrease in reserve for possible loan losses	(36,798)	(94,092)	(348,304)
Increase in liability for employees' retirement benefits	1,352	1,930	12,804
Increase (decrease) in reserve for credit losses on off-balance-sheet instruments	7,268	(362)	68,798
Interest income	(80,651)	(84,172)	(763,386)
Interest expenses	16,914	24,596	160,103
Net losses (gains) on sales and maturities securities	1,702	(721)	16,111
Profit from money held in trust	(18)	(3)	(172)
Net exchange losses	10,239	7,652	96,917
Net losses on disposal of premises and equipment	157	303	1,490
Net decrease (increase) in trading account assets	43,841	(109,597)	414,971
Net decrease in trading account liabilities	(52,112)	(21,675)	(493,260)
Net decrease in loans and bills discounted	293,140	39,300	2,774,638
Net increase in deposits	50,864	372,534	481,439
Net increase (decrease) in debentures	(415,153)	1,933	(3,929,519)
Net increase in borrowed money (excluding subordinated)	8,500		80,454
Net decrease (increase) in due from banks	33,812	(32,741)	320,040
Net decrease in call loans and bills bought	1,234	2,847	11,681
Net increase in receivables under securities borrowing transactions	(45,091)	(79,539)	(426,797)
Net increase (decrease) in call money and bills sold	(228,052)	51,193	(2,158,562)
Net increase in commercial paper	2,000	3,000	18,930
Net increase in payables under securities lending transactions	97,322	(114,887)	921,178
Net decrease in foreign exchanges (asset)	1,600	6,483	15,154
Net increase (decrease) in foreign exchanges (liability)			6
Interest received in cash	83,146	92,493	787,002
Interest paid in cash	(19,090)	(27,220)	(180,696)
Other—net	(112,933)	37,494	(1,068,943)
Sub-total	(304,452)	105,982	(2,881,708)
Payments of income taxes	(575)	(799)	(5,445)
Net cash provided by operating activities	(305,027)	105,182	(2,887,153)
INVESTING ACTIVITIES:			
Purchases of securities	(5,093,878)	(3,311,015)	(48,214,656)
Proceeds from sale of securities	886,131	933,454	8,387,426
Proceeds from redemption of securities	4,583,043	2,072,748	43,379,493
Increase in money held in trust	(59,536)	(109,968)	(563,523)
Decrease in money held in trust	42,681	74,282	403,987
Purchases of premises and equipment	(2,319)	(7,676)	(21,950)
Proceeds from sale of premises and equipment	4,181	305	39,578
Net payment for acquisition of a subsidiary	(203)		(1,930)
Net cash used in investing activities	360,100	(347,870)	3,408,425
FINANCING ACTIVITIES:			
Repayment of subordinated debt	(4,095)	(20,700)	(38,760)
Dividends paid to preferred stock	(3,464)	(3,464)	(32,794)
Dividends paid to the minority stockholders	(243)	(97)	(2,300)
Other	(24)		(234)
Net cash used in financing activities	(7,827)	(24,261)	(74,088)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	47,244	(266,949)	447,184
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	290,872	557,822	2,753,174
CASH AND CASH EQUIVALENTS, END OF YEAR	¥ 338,117	¥ 290,872	$ 3,200,358

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Aozora Bank, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2004 and 2003

1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements of Aozora Bank, Ltd. (the "Bank" or the "Parent Company") and its consolidated subsidiaries 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 accounting principles generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications have been made in the 2003 financial statements to conform to the classifications used in 2004.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which the Bank is incorporated and operates. Japanese yen figures less than a million yen are rounded down to the nearest million yen, except for per share data. As a result, the totals do not necessarily agree with the sum of the individual amounts. The translation of Japanese yen amounts into U.S. dollar amounts is included solely for the convenience of readers outside Japan and has been made at the rate of ¥105.65 to $1, the approximate rate of exchange at March 31, 2004. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

2. Summary of Significant Accounting Policies

a. Consolidation—The consolidated financial statements as of March 31, 2004 include the accounts of the Bank and its consolidated subsidiaries, including Aozora Trust Bank, Ltd., Aozora Loan Services Co., Ltd., Aozora Card Co., Ltd. and 6 other subsidiaries in 2004 and 2003 (together, the "Group").

Under the control or influence concept, those companies in which the Bank, directly or indirectly, is able to exercise control over operations are fully consolidated, and those companies over which the Group has the ability to exercise significant influence are accounted for by the equity method.

The consolidated financial statements do not include the accounts of insignificant subsidiaries such as NCM Investments Corporation, because the combined total assets, total income, net income and earned surplus would not have had a material effect on the consolidated financial statements.

Investments in the unconsolidated subsidiaries and certain affiliated companies such as Vietnam International Leasing, Co., Ltd. are stated at cost. If the equity method of accounting had been applied to the investments in these companies, the effect on the accompanying consolidated financial statements would not be material.

The difference between the cost of an acquisition and the fair value of the net assets of the acquired subsidiaries at the date of acquisition is charged to income when incurred.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

b. Cash and Cash Equivalents—Cash and cash equivalents consist of cash on hand and due from the Bank of Japan.

c. Trading Account Assets/Liabilities—Transactions for trading purposes (the purpose of seeking to capture gains arising from short-term changes in interest rates, currency exchange rates or market prices of securities and other market-related indices or arbitrage opportunities) are included in "Trading account assets" and "Trading account liabilities" on a trade date basis. Trading account assets and liabilities are stated at fair value.

Profits and losses on transactions for trading purposes are shown as "Trading account profits" and "Trading account losses" on a trade date basis.

d. Securities—All securities are classified and accounted for, depending on management's intent, as follows: (1) trading securities which are held for the purpose of earning capital gains in the near term are stated at fair value, and the related unrealized gains and losses are included in income, (2) held-to-maturity debt securities which are expected to be held to maturity with the positive intent and ability to hold to maturity are stated at amortized cost and (3) available-for-sale securities are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of stockholders' equity.

Non-marketable available-for-sale securities are stated at cost determined by the moving-average method. For other than temporary declines in fair value, investment securities are reduced to net realizable value by a charge to income. Securities included in money held in trust on behalf of the Bank are stated at fair value, and the related unrealized gains and losses are included in income.

e. Derivatives and Hedging Activities—Derivatives for purposes other than trading are stated at fair value.

As regards hedging interest rate risk arising from financial assets and liabilities, the Bank used the deferral method of accounting, in accordance with the main rules of "Treatment for Accounting and Auditing of Application of Accounting Standard for Financial Instruments in Banking Industry" (the Japanese Institute of Certified Public Accountants ("JICPA") Industry Audit Committee Report No. 24) in the current fiscal year. In the previous year, in accordance with temporary measures prescribed by JICPA Industry Audit Committee Report No. 24, the Bank used so-called "macro hedging," a strategy to employ derivative transactions and control interest rate risks arising from financial assets and liabilities, such as loans, debentures and deposits, etc. within a set range, with aims to reduce risk as a whole. "Deferred losses and gains" in the balance sheet at March 31, 2004, related to "macro hedging" are being amortized as interest expense or interest income over 3 years, according to the remaining periods and notional amounts of the hedging instruments.

As regards hedging foreign exchange rate risk arising from financial assets and liabilities denominated in foreign currencies, the Bank also uses the deferral method of accounting. While the Bank had adopted the temporary measures prescribed by "Treatment of Accounting and Auditing Concerning Accounting for Foreign Currency Transactions in Banking Industry" (JICPA Industry Audit Committee Report No. 25) in the previous year, the Bank now applies hedge accounting, in accordance with the main rules of JICPA Industry Audit Committee Report No. 25, to currency swap transactions and foreign exchange swap transactions intended to convert funding currency (JPY) to investing currencies (foreign currencies). Also, in order to hedge the foreign exchange rate risk of "Available-for-sale securities" denominated in foreign currencies, except bonds, the Bank specifies the names of securities denominated in foreign currencies in advance, and applies fair value hedging to the specified securities, on the condition that foreign currency denominated liabilities, including forward contracts, exceed the acquisition costs of those securities.

Since the market for credit derivatives, including credit linked notes, in Japan was not well developed in the previous year, credit derivatives were booked as non-mark-to-market derivatives in a manner similar to the guarantee of liabilities. With the expansion of the credit-derivative market, valuation by the mark-to-market method is more readily determinable. Therefore, credit derivatives are stated at their market value. As a result, "Income before income taxes" increased by ¥3,510 million ($33,228 thousand), "Other assets" increased by ¥2,214 million ($20,962 thousand), "Other liabilities" increased by ¥198 million ($1,875 thousand), "Customers' liabilities for acceptances and guarantees" and "Acceptances and guarantees" decreased by ¥77,847 million ($736,843 thousand).

f. Premises and Equipment—Premises and equipment are stated at cost. Depreciation of premises and equipment of the Bank and its consolidated domestic subsidiaries is computed by the declining-balance method at rates based on the estimated useful lives of the assets, while the straight-line method is applied to buildings. The range of useful lives is principally 50 years for buildings and from 5 to 15 years for other premises and equipment.

g. Software—Costs of software developed or obtained for internal use are depreciated over the estimated useful lives of the software (principally 5 years).

h. Deferred Charges—Discounts on debentures are amortized by the straight-line method over the terms of the debentures. Debenture issuance expenses are amortized by the straight-line method over the shorter of the terms of the debentures or the 3-year period stipulated in Enforcement Regulations of the Japanese Commercial Code.

i. Write-off of Loans and Reserve for Possible Loan Losses—Loans to borrowers under legal proceedings, such as bankruptcy, and loans in similar conditions, are written off by the amount of loans exceeding the estimated realizable value of collateral and guarantees. The amount written off in the current fiscal year amounted to ¥8,489 million ($80,358 thousand) and ¥13,322 million for the years ended March 31, 2004 and 2003, respectively.

For loans to borrowers not yet bankrupt but likely to fall into bankruptcy, the necessary specific reserve amounts are provided for through an overall assessment of the borrowers' ability to pay, after subtracting from the loan balance the amount collectible on disposal of collateral or execution of guarantees. As to other loans, the Bank provides a general reserve by applying the historical loan-loss ratio determined over a certain period. An allowance for loans to specific foreign borrowers is provided based on the amount of expected losses due to the political and economic situation of their respective countries.

The Bank has also taken into account the precondition for exercise of the cancellation right in determining the necessary reserve amount. Under the clause of "Warranty of Loan Related Assets" described in the Share Purchase Agreement signed on June 30, 2000, between SOFTBANK CORP., ORIX Corporation, Tokio Marine and Fire Insurance Co., Ltd., and other financial institutions (the "Consortium"), Deposit Insurance Corporation of Japan and the Bank, a precondition of exercise of the cancellation right is the existence of a defect and a 20% deterioration in asset value.

All loans are subject to asset quality assessment conducted by the business-related divisions in accordance with the Self-Assessment Standards, and the results of the assessments are reviewed by the Asset Audit Division, which is independent from the business-related divisions, before the reserve amount is finally determined.

As to general loans, consolidated subsidiaries provide for a necessary reserve by applying the appropriate historical loan-loss ratio. For doubtful loans, consolidated subsidiaries provide a specific reserve based on the individual loan's assessment.

***j. Liability for Employees' Retirement Benefits*—**The Group accounts for the liability for employees' retirement benefits based on the projected benefit obligations and plan assets at the balance sheet date. Prior service cost is amortized using the straight-line method. Net actuarial gain (loss) is amortized using the straight-line method commencing from the next fiscal year after incurrence.

On December 19, 2003, the Bank received an approval from the Minister of Health, Labour and Welfare for the exemption from future retirement benefit obligations with respect to the substitutional portion of the Employees' Pension Fund, in accordance with the implementation of the Defined Benefit Enterprise Pension Plan Law. The amount of plan assets which will be transferred to the government in the subsequent year is calculated to be approximately ¥4,007 million ($37,936 thousand) as of March 31, 2004. The estimated profit would be ¥4,174 million ($39,516 thousand) on the condition that the equivalent amount of return were paid as of March 31, 2004, in accordance with Article 44-2 of "Practical Guidelines of Accounting for Retirement Benefits (Interim Report)" (JICPA Accounting Committee Report No. 13).

***k. Reserve for Credit Losses on Off-balance-sheet Instruments*—**Reserve for credit losses on off-balance-sheet instruments is provided for credit losses on commitments to extend loans and other off-balance-sheet financial instruments based on an estimated loss ratio or individually estimated loss amount determined by the same methodology which is used in determining the reserve for loan losses.

***l. Other Reserves*—**Other reserves include the reserve for securities transaction liabilities. The reserve for securities transaction liabilities is required to be provided under the Securities and Exchange Law of Japan.

***m. Lease Transactions*—**All leases of the Bank and its domestic consolidated subsidiaries are accounted for as operating leases. Under Japanese accounting standards for leases, finance leases that are deemed to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the consolidated financial statements.

***n. Income Taxes*—**Deferred income taxes are recorded to reflect the impact of temporary differences between assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes. These deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

***o. Foreign Currency Items*—**Assets and liabilities denominated in foreign currencies held by the Bank at the year end are translated into Japanese yen at exchange rates prevailing at the end of the fiscal year except for equity securities of affiliated companies which are translated at historical rates.

Foreign currency assets and liabilities of other consolidated subsidiaries are principally translated into yen equivalents at the exchange rates prevailing at the fiscal year end of each company.

In the fiscal year ended March 31, 2003, the Bank had adopted temporary measures prescribed by JICPA Industry Audit Committee Report No. 25.

In the fiscal year ended March 31, 2004, the Bank adopted the main rules of JICPA Industry Audit Committee Report No. 25 and applied hedge accounting prescribed by the Report to currency swap transactions and foreign exchange swap transactions which aim to convert funding currency (JPY) to investing currencies (foreign currencies). Consequently, this type of currency swap transactions and foreign exchange swap transactions, which were previously accrued, are marked-to-market from this fiscal year and the net credit or debt is recorded on the consolidated balance sheet. As a result, "Trading account assets" increased by ¥4,120 million ($39,000 thousand), "Other assets" decreased by ¥4,230 million ($40,046 thousand) and “Other liabilities” increased by ¥110 million ($1,046 thousand). This change did not affect profit or loss.

Translation differences related to forward exchange contracts, except as discussed above, which were previously stated on a net basis after offsetting, are stated on a gross basis from this fiscal year in accordance with JICPA Industry Audit Committee Report No. 25. As a result, Other assets and Other liabilities increased by ¥9,415 million ($89,120 thousand), respectively.

p. Dividends—Dividends are generally paid semiannually. Interim and year-end dividends are authorized subsequent to the end of the period to which they are related, and are reflected in the consolidated statements of stockholders’ equity when duly declared and authorized.

No dividend was proposed for stockholders of common stock for the years ended March 31, 2004 and 2003.

q. Per Share Information—Basic net income per share is computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding for the period, retroactively adjusted for stock splits.

Diluted net income per share reflects the potential dilution that could occur if securities were exercised or converted into common stock. Diluted net income per share of common stock assumes full conversion of the preferred stock at the beginning of the year with an applicable adjustment for related dividends to preferred stock.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years including dividends to be paid after the end of the year.

r. New Accounting Pronouncements—In August 2002, the Business Accounting Council issued a Statement of Opinion, “Accounting for Impairment of Fixed Assets,” and in October 2003 the Accounting Standards Board of Japan (ASB) issued ASB Guidance No. 6, “Guidance for Accounting Standard for Impairment of Fixed Assets.” These new pronouncements are effective for fiscal years beginning on or after April 1, 2005 with early adoption permitted for fiscal years ending on or after March 31, 2004.

The new accounting standard requires an entity to review its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

The Bank is currently in the process of assessing the effect of adoption of these pronouncements.

3. Cash and Cash Equivalents

Cash and cash equivalents as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Cash on hand	¥ 16,176	¥ 23,407	$ 153,111
Due from the Bank of Japan	321,941	267,465	3,047,247
Total	¥338,117	¥290,872	$3,200,358

4. Trading Account Assets and Liabilities

Trading account assets and liabilities as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Trading account assets:			
Trading securities	¥ 66,234	¥ 43,444	$ 626,926
Derivatives of trading securities		11	
Derivatives of securities held to hedge trading transactions	1	9	19
Derivatives of trading transactions	86,003	140,538	814,040
Other	336,209	348,287	3,182,299
Total	¥488,449	¥532,291	$4,623,284
Trading account liabilities:			
Trading securities sold short	¥ 6,848		$ 64,823
Derivatives of trading securities	3	¥ 57	31
Derivatives of securities held to hedge trading transactions	5		48
Derivatives of trading transactions	81,673	140,585	773,053
Total	¥ 88,529	¥140,642	$ 837,955

5. Securities

Securities as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Japanese national government bonds	¥728,623	¥ 965,526	$6,896,579
Japanese local government bonds	4,234	70,987	40,082
Japanese corporate bonds	65,476	78,067	619,747
Japanese stocks	1,636	1,877	15,488
Other	164,993	233,576	1,561,701
Total	¥964,964	¥1,350,036	$9,133,597

The carrying amounts and aggregate fair values of securities as of March 31, 2004 were as follows:

	Millions of Yen			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
Japanese national government bonds	¥728,860	¥ 42	¥290	¥728,612
Japanese local government bonds	3,700	58	34	3,724
Japanese corporate bonds	30,337	622	80	30,879
Japanese stocks	3	31		35
Other*	51,296	5,501	120	56,676
Held-to-maturity:				
Japanese national government bonds	10			10
Total	¥814,208	¥6,257	¥526	¥819,939

	Thousands of U.S. Dollars			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
Japanese national government bonds	$6,898,817	$ 406	$2,749	$6,896,475
Japanese local government bonds	35,025	558	328	35,256
Japanese corporate bonds	287,150	5,896	763	292,282
Japanese stocks	33	300		332
Other*	485,528	52,072	1,144	536,456
Held-to-maturity:				
Japanese national government bonds	104			104
Total	$7,706,657	$59,232	$4,984	$7,760,905

The carrying amounts and aggregate fair values of securities as of March 31, 2003 were as follows:

	Millions of Yen			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
Japanese national government bonds	¥ 964,492	¥1,066	¥ 42	¥ 965,515
Japanese local government bonds	70,321	187	65	70,443
Japanese corporate bonds	46,975	506	1,031	46,450
Japanese stocks	242	6	1	247
Other*	93,100	1,615	335	94,380
Held-to-maturity:				
Japanese national government bonds	10			10
Total	¥1,175,143	¥3,381	¥1,476	¥1,177,048

* Other includes investments in partnership and others which were reported at fair value.

Available-for-sale securities whose fair value was not readily determinable as of March 31, 2004 and 2003, were as follows:

	Carrying Amount		
	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Available-for-sale:			
Japanese local government bonds	¥ 509	¥ 544	$ 4,826
Japanese corporate bonds	34,596	31,617	327,465
Japanese stocks	1,559	1,570	14,766
Claims on loan trust	6,793		64,304
Other	108,503	140,336	1,027,009
Total	¥151,963	¥174,068	$1,438,370

Proceeds from sales of available-for-sale securities and the gross realized gains and losses on these sales for the years ended March 31, 2004 and 2003, were as follows:

	Carrying Amount		
	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Proceeds from sales	¥887,557	¥934,223	$8,400,923
Gross realized gains	2,897	3,376	27,427
Gross realized losses	4,589	964	43,439

The carrying values of debt securities by contractual maturities for securities classified as available-for-sale and held-to-maturity as of March 31, 2004, were as follows:

March 31, 2004	Millions of Yen		Thousands of U.S. Dollars	
	Available for Sale	Held to Maturity	Available for Sale	Held to Maturity
Due in one year or less	¥578,263	¥10	$5,473,391	$104
Due after one year through five years	302,873		2,866,761	
Due after five years through ten years	43,083		407,792	
Due after ten years	489		4,636	
Total	¥924,710	¥10	$8,752,580	$104

The carrying values and valuation gain recognized in the consolidated statements of income for trading securities as of March 31, 2004 and 2003, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Trading securities:			
Carrying value	¥402,444	¥391,732	$3,809,225
Valuation gain (loss) included in the income (loss) before income taxes	(500)	161	(4,740)

The above trading securities include negotiable certificates of deposits and commercial paper which were classified as trading assets.

6. Loans and Bills Discounted

Loans and bills discounted as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Bills discounted	¥ 6,310	¥ 5,524	$ 59,729
Loans on notes	416,967	635,342	3,946,688
Loans on deeds	2,359,561	2,440,107	22,333,758
Overdrafts	182,713	177,719	1,729,419
Total	¥2,965,552	¥3,258,693	$28,069,594

"Loans to bankrupt borrowers" are loans to borrowers who are legally bankrupt and amounted to ¥11,517 million ($109,019 thousand) and ¥9,237 million as of March 31, 2004 and 2003, respectively. "Past due loans" are non-accrual loans except for loans to bankrupt borrowers and loans to borrowers for which concessions on payments of interests were made in order to assist the reorganization of borrowers and amounted to ¥66,038 million ($625,066 thousand) and ¥98,988 million as of March 31, 2004 and 2003, respectively.

"Loans over due for three months or more" are those loans for which principal or interest remains unpaid for at least three months, excluding loans to bankrupt companies and past due loans and amounted to nil and ¥1,340 million as of March 31, 2004 and 2003, respectively.

"Restructured loans" are loans, excluding loans to bankrupt borrowers, past due and/or overdue for three months or more, for which concessions are made in the borrower's favor on interest or principal payment or to waive claims for the purpose of assisting in the reconstruction of insolvent borrowers and amounted to ¥11,374 million ($107,664 thousand) and ¥90,206 million as of March 31, 2004 and 2003, respectively.

The amounts referred to above are the amounts before bad debts are written off and specific reserves for possible loan losses are provided.

Overdraft contracts and contracts for loan commitments are those by which consolidated subsidiaries are bound to extend loans up to a prearranged amount, at the request of customers, unless the customer is in breach of contract conditions. The unutilized balance of these contracts amounted to ¥349,720 million ($3,310,184 thousand) and ¥246,846 million as of March 31, 2004 and 2003, respectively. ¥300,891 million ($2,847,998 thousand) and ¥214,885 million of these amounts relate to contracts with original contractual terms of a term of one year or less, or which are unconditionally cancelable at any time as of March 31, 2004 and 2003, respectively.

The amount of loans sold through senior certificates under a collateralized loan obligation (CLO) securitization totaled ¥100,000 million ($946,522 thousand) and ¥50,000 million for the years ended March 31, 2004 and 2003, respectively, with the subordinated certificates retained by the Bank totaling ¥34,400 million ($325,603 thousand) and ¥17,200 million as of March 31, 2004 and 2003, respectively, recorded as loans.

7. Foreign Exchanges

Foreign exchanges as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Assets:			
Due from foreign banks	¥1,355	¥2,956	$12,834
Total	¥1,355	¥2,956	$12,834
Liabilities:			
Due to foreign banks	¥ 2	¥ 2	$ 26
Total	¥ 2	¥ 2	$ 26

8. Premises and Equipment

Accumulated depreciation amounted to ¥22,370 million ($211,737 thousand) and ¥25,401 million as of March 31, 2004 and 2003, respectively.

9. Customers' Liabilities for Acceptances and Guarantees

All contingent liabilities arising from acceptances and guarantees are reflected in acceptances and guarantees. As a contra account, customers' liabilities for acceptances and guarantees are shown as assets representing the Bank's right of indemnity from customers.

10. Reserve for Possible Loan Losses

Reserve for possible loan losses as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
General reserve	¥127,623	¥167,265	$1,207,985
Specific reserve	33,960	30,436	321,439
Reserve for loans to restructuring countries	663	1,343	6,282
Total	¥162,247	¥199,045	$1,535,706

11. Collateral

The carrying amounts of assets pledged as collateral and the collateralized debt as of March 31, 2004 and 2003, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Assets:			
Securities	¥290,970	¥ 565,522	$2,754,102
Loans and bills discounted	334,885	225,043	3,169,767
Trading account assets	207,644	286,062	1,965,402
Total	¥833,501	¥1,076,628	$7,889,271
Debt:			
Deposits	¥ 30,000	¥ 50,000	$ 283,956
Borrowed money	100	100	947
Call money and bills sold	228,500	464,900	2,162,802
Payables under repurchase agreements	131,598	204,797	1,245,605
Payables under securities lending transactions	65,006		615,297
Total	¥455,204	¥ 719,797	$4,308,607

In addition, the following assets were pledged or deposited as margin money with respect to foreign exchange settlements and derivatives as of March 31, 2004 and 2003:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Securities	¥128,333	¥132,510	$1,214,705
Total	¥128,333	¥132,510	$1,214,705

12. Debentures

Debentures as of March 31, 2004 and 2003, consisted of the following:

March 31, 2004	Millions of Yen	Thousands of U.S. Dollars	Interest Rates
One-year discount debentures	¥ 51,241	$ 485,012	0.04%–0.08%
One-year coupon debentures	261,550	2,475,627	0.10%–0.90%
Two-year coupon debentures	410,300	3,883,578	0.15%–1.10%
Three-year coupon debentures	100,650	952,674	0.20%–1.25%
Five-year coupon debentures	231,231	2,188,657	0.10%–2.50%
Total	¥1,054,973	$9,985,548	

March 31, 2003	Millions of Yen		Interest Rates
One-year discount debentures	¥ 85,618		0.04%–0.16%
One-year coupon debentures	712,200		0.10%–0.90%
Two-year coupon debentures	440,900		0.40%–1.10%
Three-year coupon debentures	84,250		0.55%–1.25%
Five-year coupon debentures	147,158		0.10%–2.95%
Total	¥1,470,126		

13. Deposits

Deposits as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Current deposits	¥ 108,014	¥ 112,326	$ 1,022,382
Ordinary deposits	434,930	438,819	4,116,713
Deposits at notice	23,401	34,125	221,499
Time deposits	1,450,231	1,510,350	13,726,755
Negotiable certificates of deposit	548,120	417,506	5,188,074
Other	23,332	24,047	220,846
Total	¥2,588,030	¥2,537,175	$24,496,269

14. Borrowed Money

The weighted averaged annual interest rates applicable to borrowed money was 2.14% and 2.25% as of March 31, 2004 and 2003, respectively.

Borrowed money includes subordinated borrowings, which were ¥19,400 million ($183,625 thousand) and ¥23,495 million as of March 31, 2004 and 2003, respectively.

Annual maturities of borrowed money as of March 31, 2004, for the next five years and thereafter were as follows:

Year Ending March 31	Millions of Yen	Thousands of U.S. Dollars
2005	¥14,000	$132,513
2006	5,400	51,112
2007	500	4,733
2008	100	946
2009	15	142
2010 and thereafter	8,000	75,722
Total	¥28,015	$265,168

15. Other Assets and Liabilities

Other assets and liabilities as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Other assets:			
Accrued income	¥ 4,775	¥ 6,283	$ 45,202
Investments in partnership	39,245	40,562	371,464
Derivative financial instruments	35,467	27,461	335,704
Financial stabilization fund	32,628	32,628	308,831
Other	28,421	17,423	269,024
Total	¥140,538	¥124,360	$1,330,225
Other liabilities:			
Accrued expenses	¥ 11,018	¥ 15,262	$ 104,291
Borrowed bond trading	69,497	4,224	657,805
Derivatives other than for trading	14,083	223	133,308
Deferred gains on hedging instruments	15,980	27,265	151,262
Matured debentures	28,332	23,309	268,171
Other	45,645	230,076	432,043
Total	¥184,557	¥300,360	$1,746,880

16. Liability for Employees' Retirement Benefits

The Bank has employees' retirement benefits plans. Such retirement benefits are made in the form of a lump-sum severance payment from the Bank and annuity payments from trustees.

The liability for employees' retirement benefits plans as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Projected benefit obligation	¥ 40,859	¥ 40,100	$ 386,740
Fair value of plan assets	(18,839)	(15,770)	(178,321)
Unrecognized prior service cost	3,066	2,660	29,026
Unrecognized actuarial gain	(5,832)	(9,089)	(55,203)
Net liability	¥ 19,253	¥ 17,901	$ 182,242

The components of net periodic benefit costs of the employees' retirement benefits plans for the years ended March 31, 2004 and 2003, are as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Service cost	¥1,405	¥1,648	$13,306
Interest cost	933	947	8,832
Expected return on plan assets	(476)	(524)	(4,508)
Amortization of prior service cost	(297)	(88)	(2,811)
Recognized actuarial loss	2,240	1,619	21,210
Net periodic retirement benefit costs	¥3,806	¥3,602	$36,029

Assumptions used for the years ended March 31, 2004 and 2003, are set forth as follows:

	2004	2003
Discount rate	2.4%	2.4%
Expected rate of return on plan assets:		
Approved retirement annuities	0.5%	0.5%
Fund of welfare pension	3.5%	3.5%
Amortization period of prior service cost	9–12 years as average remaining service period	9–12 years as average remaining service period
Recognition period of actuarial gain/loss	5 years or average remaining service period if less than 5 years	5 years or average remaining service period if less than 5 years

17. Stockholders' Equity

(1) Capital Stock and Capital Surplus

The authorized number of shares as of March 31, 2004 were 5,189 million shares of common stock and 943 million shares of non-voting, non-cumulative preferred stock. The number of treasury stock as of March 31, 2004, were 705 shares.

Japanese companies are subject to the Japanese Commercial Code (the "Code") to which certain amendments have become effective since October 1, 2001.

The Code was revised whereby common stock par value was eliminated resulting in all shares being recorded with no par value and at least 50% of the issue price of new shares required to be recorded as common stock and the remaining net proceeds as additional paid-in capital, which is included in capital surplus. The Code permits Japanese companies, upon approval of the Board of Directors, to issue shares to existing stockholders without consideration as a stock split. Such issuance of shares generally does not give rise to changes within the stockholders' accounts.

The Code permits the transfer of additional paid-in capital and legal reserve to stated capital by resolution of the Board of Directors. The Code also permits the transfer of unappropriated retained earnings, available for dividends, to stated capital by resolution of the stockholders.

The revised Code eliminated restrictions on the repurchase and use of treasury stock allowing Japanese companies to repurchase treasury stock by a resolution of the stockholders at the general stockholders meeting and dispose of such treasury stock by resolution of the Board of Directors. The repurchased amount of treasury stock cannot exceed the amount available for future dividend plus the amount of common stock, additional paid-in capital or legal reserve to be reduced in the case where such reduction was resolved at the general stockholders meeting.

Preferred stock as of March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Preferred stock—authorized, 76,144 thousand shares; issued and outstanding, 48,144 thousand shares of fourth preferred stock	¥ 12,036	¥ 12,036	$ 113,923
Preferred stock—authorized, 867,000 thousand shares; issued and outstanding, 866,667 thousand shares of fifth preferred stock	260,000	260,000	2,460,957
Total	¥272,036	¥272,036	$2,574,880

(2) Retained Earnings

Under the Bank Law of Japan, an amount equivalent to at least 20% of cash dividends and certain other appropriations of retained earnings associated with cash outlays applicable to each period shall be appropriated as a legal reserve (a component of retained earnings) until such reserve and additional paid-in capital equals 100% of the Bank's stated capital. A legal reserve amount is not available for dividends but may be used to reduce a deficit by resolution of the stockholders or may be capitalized by resolution of the Board of Directors.

The amount of retained earnings available for dividends under the Code was ¥54,344 million ($514,379 thousand) as of March 31, 2004, based on the amount recorded in the Parent Company's general books of account. In addition to the provision that requires an appropriation for a legal reserve in connection with the cash payment, the Code imposes certain limitations on the amount of retained earnings available for dividends.

Dividends are approved by the stockholders at a meeting held subsequent to the fiscal year to which the dividends are applicable. Semiannual interim dividends may also be paid upon resolution of the Board of Directors, subject to certain limitations imposed by the Code.

18. Other Operating Income

Other operating income for the years ended March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Other operating income:			
Gain on sales of bonds	¥ 2,880	¥3,165	$ 27,261
Gains on foreign exchange transactions	2,347	853	22,216
Gain on derivatives	4,999		47,319
Other	6,522	5,611	61,734
Total	¥16,748	¥9,630	$158,530

19. Other Income

Other income for the years ended March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Gain on sales of stocks and other securities	¥ 17	¥ 211	$ 166
Reversal of reserve for possible loan losses	22,672	17,344	214,602
Other	4,946	5,956	46,824
Total	¥27,637	¥23,512	$261,592

20. Other Operating Expenses

Other operating expenses for the years ended March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Other operating expenses:			
Amortization of debenture issuance costs	¥ 225	¥ 279	$ 2,135
Loss on sales of bonds	4,586	1,085	43,413
Loss on redemption of bonds		280	
Loss on derivatives		1,182	
Other	474	384	4,487
Total	¥5,286	¥3,213	$50,035

21. Other Expenses

Other expenses for the years ended March 31, 2004 and 2003, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Provision for reserve for credit losses on off-balance-sheet instruments	¥ 7,268		$ 68,798
Write-off of claims	8,737	¥11,939	82,704
Loss on sales of stocks and other securities	2	648	25
Loss on write-down of stocks	10	643	99
Loss on disposal of premises and equipment	165	303	1,571
Accelerated depreciation		7,143	
Other	21,915	16,486	207,438
Total	¥38,101	¥37,164	$360,635

22. Income Taxes

The Bank and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in normal effective statutory tax rates of approximately 43.7% and 41.9% for the years ended March 31, 2004 and 2003, respectively.

The Group files a tax return under the consolidated corporate-tax system from the fiscal year ended March 31, 2004, which allows companies to base tax payments on the combined profits or losses of the parent company and its wholly owned domestic subsidiaries. Under the consolidated corporate-tax system, a surcharge tax of 2% of taxable income is levied in addition to the national corporate income tax rate for the fiscal year ended March 31, 2004.

The tax effects of significant temporary differences and loss carryforwards which resulted in deferred tax assets and liabilities as of March 31, 2004 and 2003, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Deferred tax assets:			
Tax loss carryforwards	¥ 269,103	¥ 231,706	$ 2,547,119
Loss on devaluation of securities	23	935	218
Reserve for possible loan losses	49,867	82,254	472,006
Other	26,832	53,067	253,975
Less valuation allowance	(331,169)	(353,386)	(3,134,592)
Total	14,656	14,577	138,726
Deferred tax liabilities:			
Unrealized gain on available-for-sale securities	(2,332)	(800)	(22,077)
Net deferred tax assets	¥ 12,323	¥ 13,777	$ 116,649

A reconciliation between the normal effective statutory tax rates and the actual effective tax rates reflected in the accompanying consolidated statements of income for the years ended March 31, 2004 and 2003, is as follows:

	2004	2003
Normal effective statutory tax rate	43.7%	41.9%
Expenses not deductible for income tax purposes	(0.1)	(0.2)
Valuation allowance	(44.7)	(53.1)
Other—net	2.4	(1.7)
Actual effective tax rate	1.3%	(13.1)%

As of March 31, 2004, the Bank and a consolidated subsidiary has tax loss carryforwards which are available to be offset against taxable income in future years. These tax loss carryforwards, if not utilized, will expire as follows:

Year Ending March 31	Millions of Yen	Thousands of U.S. Dollars
2005	¥431,251	$4,081,893
2009	60,069	568,567
2010	62,767	594,109
2011	107,358	1,016,171
Total	¥661,447	$6,260,740

With the enactment of the "Amendments to the Local Tax Law" (Legislation No. 9, 2003) on March 31, 2003, the tax basis of enterprise taxes, which was stipulated as "income and liquidation income" by Article 72, paragraph 12 of the Local Tax Law before the amendments, consists of "added value amount," "capital amount," and "income and liquidation income" from the fiscal year beginning April 1, 2004. The enterprise taxes based on the "added value amount" and "capital amount" are not pertinent to the enterprise taxes that have tax bases of income-related amounts. The "Amendments to the Local Tax Law" also stipulates that the metropolitan ordinance and the municipal ordinance are to be abolished from the fiscal year beginning April 1, 2004.

In connection with the "Amendments to the Local Tax Law," the effective statutory tax rates used in the calculation of deferred tax assets and liabilities from the fiscal years beginning April 1, 2004 was changed from 41.94% to 40.68%. As a result, there was a decrease in "Deferred tax assets" of ¥371 million ($3,520 thousand) and an increase in "Deferred income tax" of ¥443 million ($4,194 thousand) in the consolidated statements of operations for the fiscal year ended March 31, 2004.

There was also an increase in "Unrealized gain on available-for-sale securities" of ¥71 million ($674 thousand) for the fiscal year ended March 31, 2004.

23. Lease Transactions

The Bank and consolidated subsidiaries lease certain equipment and other assets.

Lease payments under finance leases were ¥1,055 million ($9,987 thousand) and ¥1,141 million for the years ended March 31, 2004 and 2003, respectively.

Pro forma information of leased property such as acquisition cost, accumulated depreciation, obligation under finance lease, depreciation expense and interest expense of finance leases that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the years ended March 31, 2004 and 2003, was as follows:

Year Ended March 31, 2004

	Millions of Yen			Thousands of U.S. Dollars		
	Equipment	Other	Total	Equipment	Other	Total
Acquisition cost	¥4,458	¥11	¥4,469	$42,197	$112	$42,309
Accumulated depreciation	2,511	10	2,521	23,774	95	23,869
Net leased property	¥1,946	¥ 1	¥1,948	$18,423	$ 17	$18,440

Year Ended March 31, 2003

	Millions of Yen		
	Equipment	Other	Total
Acquisition cost	¥5,638	¥401	¥6,039
Accumulated depreciation	3,241	111	3,353
Net leased property	¥2,396	¥290	¥2,686

Obligations under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Due within one year	¥ 808	¥1,012	$ 7,648
Due after one year	1,140	1,673	10,792
Total	¥1,948	¥2,686	$18,440

Depreciation expense under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Depreciation expense	¥1,055	¥1,141	$9,987

Depreciation expense is calculated using the straight-line method with zero residual value.

The amounts of acquisition cost, obligations and depreciation expense includes interest expense, due to its immateriality.

The minimum rental commitments under noncancelable operating leases as of March 31, 2004 and 2003, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Due within one year	¥7	¥8	$72
Due after one year			
Total	¥7	¥9	$72

24. Derivatives

a. Derivatives Transactions

Derivative financial instruments dealt

Derivatives involve interest rate-related transactions (such as interest rate futures, interest rate options and interest rate swaps), currency related transactions (such as currency swaps, foreign exchange forward contracts and currency options), stock and bond-related futures and options, and credit derivatives.

Policy and purpose to use derivatives

Derivative activities are significant to business operations. The Bank has been using derivatives actively, while controlling the various risks of derivatives, such as market and credit risks. The purpose of our use of derivatives is to offer customers products to hedge market risks such as interest rate risk and foreign exchange risk and to take proprietary trading positions by exploiting short-term fluctuations and differences among markets in interest rates, foreign exchange rates, securities prices and other factors. In order to stabilize and maximize earnings, the Bank also uses derivatives in ALM operations, helping to maintain interest rate risk and other risks of on-balance-sheet assets and liabilities at an appropriate level.

As regards hedging activities to control interest rate risk arising from financial assets and liabilities, the Bank uses deferral method of hedge accounting, in accordance with the main rules of JICPA Industry Audit Committee Report No. 24. The effectiveness of hedging for the purpose of offsetting market fluctuation is assessed as follows; the Bank specifies the items to be hedged such as deposits or lending and the hedging instruments to be used such as interest rate swaps and divides them into groups by remaining periods to maturity, and evaluates the hedging effectiveness within each of the groups.

Risk associated with derivatives

The two most significant derivatives-related risks are market and credit risks. Market risk can result in loss due to the volatility of factors such as interest rates and foreign exchange rates. Credit risk occurs when the counter-parties to a transaction fail to fulfill their obligations under a contract.

Risk control system for derivatives

The Bank strives to develop and maintain a proper risk control system to avert unexpected losses and to pursue reliable and sound business operations whereby the Bank takes risks commensurate with its financial strength to earn profits.

The Bank's basic philosophy of risk control is documented in "Master Policy for Risk Management." The Board of Directors establishes a basic framework of risk control, and within that framework responsible divisions control various risks, including market risk and credit risk. In addition, the Risk Management Division oversees the risk control system of the Bank as a whole, promotes the development of the system, measures and controls risks in a comprehensive manner. The Internal Audit Division audits the appropriateness and effectiveness of the risk control system. The Board of Directors is informed about the risks by the responsible divisions and uses this information for management decisions in order to maintain and improve the risk control system.

For market risk, the maximum estimated loss is calculated on a daily basis using the value-at-risk method and the result is monitored based on specified limits. If an actual loss exceeds a maximum estimate, causal analysis is conducted. During the 248 business days from April 2003 to March 2004 and the 246 business days from April 2002 to March 2003, the actual value-at-risk figure in trading operations at the head office were estimated as follows:

Value-at-risk

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Maximum	¥189	¥271	$1,793
Minimum	49	27	460
Average	113	142	1,070

As to credit risk, the exposure is calculated by the current exposure method, the sum of the replacement cost and the potential cost in connection with expected changes in market conditions, and is controlled together with credit risk related to on-balance-sheet transactions such as lending. These risks are managed in line with internal regulations. Credit risk equivalent amounts for capital adequacy ratio calculation purposes (based on a standard for domestic operations) as of March 31, 2004 and 2003, were estimated as follows:

Credit risk equivalent amount

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Currency related transactions	¥ 44,559	¥ 16,974	$ 421,766
Interest rate related transactions	122,407	187,014	1,158,610
Credit derivatives	19,339		183,048
Netting effect	(81,593)	(127,397)	(772,304)
Total	¥104,711	¥ 76,590	$ 991,120

Supplementation to market-value calculation

OTC derivatives in the trading account are valued in accordance with internal rules established in line with the Long-term Credit Bank Law Enforcement Regulations.

b. Fair Value of Derivatives Transactions

The Bank and consolidated subsidiaries had the following derivatives contracts, which were quoted on listed exchanges, outstanding as of March 31, 2004 and 2003:

	Millions of Yen		Thousands of U.S. Dollars	
March 31, 2004	Contract or Notional Amount	Fair Value	Contract or Notional Amount	Fair Value
Interest rate contracts:				
Futures written	¥275,601	¥(221)	$2,608,631	$(2,099)
Futures purchased	273,102	302	2,584,970	2,859
Bonds contracts:				
Futures written	2,914	(74)	27,588	(701)
Futures purchased	19,044	7	180,264	68
March 31, 2003				
Interest rate contracts:				
Futures written	¥ 66,968	¥(190)		
Futures purchased	39,529	89		
Options written	540,900	181		
Options purchased	540,900	421		
Bonds contracts:				
Futures written	22,998	(131)		
Futures purchased	8,355	3		
Futures options written	15,000	65		
Futures options purchased	5,000	9		
Equity contracts:				
Futures index written	238	2		
Futures index purchased	234	1		
Options index purchased	850			

The Bank and consolidated subsidiaries had the following derivatives contracts, which were not quoted on listed exchanges, outstanding as of March 31, 2004 and 2003:

	Millions of Yen		Thousands of U.S. Dollars	
March 31, 2004	**Contract or Notional Amount**	**Fair Value**	**Contract or Notional Amount**	**Fair Value**
Interest rate contracts:				
Interest rate swaps:				
Receive fixed and pay floating	¥9,422,587	¥115,752	$89,186,815	$1,095,626
Receive floating and pay fixed	9,266,196	(97,519)	87,706,550	(923,047)
Receive floating and pay floating	29,710	(45)	281,212	(427)
Other written	89,798	(102)	849,962	(967)
Other purchased	55,147	674	521,980	6,385
Foreign exchange:				
Currency swaps	308,713	199	2,922,043	1,890
Forward exchange contracts written	266,420	6,572	2,521,726	62,213
Forward exchange contracts purchased	441,850	(6,527)	4,182,215	(61,787)
Options written	142,191	4,387	1,345,875	41,525
Options purchased	154,747	6,869	1,464,722	65,018
Credit derivatives:				
Written	137,347	2,825	1,300,024	26,746
Purchased	81,395	(570)	770,426	(5,396)
March 31, 2003				
Interest rate contracts:				
Interest rate swaps:				
Receive fixed and pay floating	¥6,797,317	¥ 184,012		
Receive floating and pay fixed	6,771,600	(186,105)		
Receive floating and pay floating	4,200	(7)		
Other written	148,470	116		
Other purchased	155,895	757		
Foreign exchange:				
Currency swaps	195,090	(92)		

Derivatives which qualify for hedge accounting are not included in the above tables.

The contracts or notional amounts of derivatives which are shown in the above table do not represent the amounts exchanged by the parties and do not measure the exposure of the Bank and consolidated subsidiaries to credit or market risk.

Derivative transactions for trading purposes are stated at fair value in the accompanying consolidated financial statements.

25. Per Share of Common Stock

The reconciliation of the differences between basic and diluted net income per share ("EPS") for the years ended March 31, 2004 and 2003, is as follows:

	Millions of Yen	Thousands of Shares	Yen	U.S. Dollars
Year Ended March 31, 2004	Net Income	Weighted-average Shares	EPS	
Basic EPS—Net income available to common stockholders	¥27,066	2,834,870	¥9.54	$0.09
Effect of dilutive securities—Preferred stocks	3,464	1,396,276		
Diluted EPS—Net income for computation	¥30,530	4,231,146	¥7.21	$0.07
Year Ended March 31, 2003				
Basic EPS—Net income available to common stockholders	¥19,912	2,834,870	¥7.02	
Effect of dilutive securities—Preferred stocks	3,464	1,396,276		
Diluted EPS—Net income for computation	¥23,376	4,231,146	¥5.52	

26. Subsequent Events

1. Tohoku Bunka Gakuen University and Yuai Gakuen, our customers, filed for protection under the Civil Rehabilitation Law on June 21, 2004. We have a loan balance outstanding of ¥2,250 million ($21,297 thousand) with Tohoku Bunka Gakuen, with Yuai Gakuen as joint debtor, as of June 21, 2004 and may incur a loss on this loan in the future.

2. We obtained the agreement of the Deposit Insurance Corporation on June 17 and 23, 2004, with respect to certain credits for which the cancellation right was exercised pursuant to the clause of "Warranty of Loan Related Assets" described in the Share Purchase Agreement. As a result, we will reverse reserves amounting to ¥4,911 million ($46,491 thousand) in fiscal 2004.

3. Appropriation of Retained Earnings

The following appropriation of retained earnings as of March 31, 2004 was approved at the ordinary stockholders meeting held on June 29, 2004:

	Millions of Yen	Thousands of U.S. Dollars
Appropriations—Legal reserve	¥ 692	$ 6,559
Year-end dividends:		
The fourth preferred, ¥5 ($0.05) per share	240	2,278
The fifth preferred, ¥3.72 ($0.04) per share	3,224	30,516
Total	¥4,157	$39,353

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To the Board of Directors and Stockholders of
Aozora Bank, Ltd.:

We have audited the accompanying consolidated balance sheets of Aozora Bank, Ltd. and consolidated subsidiaries as of March 31, 2004 and 2003, and the related consolidated statements of income, stockholders' equity, and cash flows for the years then ended, all expressed in Japanese 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.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Aozora Bank, Ltd. and consolidated subsidiaries as of March 31, 2004 and 2003, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

As discussed in Note 2.e, the Company has changed its method of the accounting for credit derivatives in fiscal 2003.

As discussed in Note 26.1, Tohoku Bunka Gakuen University and Yuai Gakuen filed for protection under the Civil Rehabilitation Law on June 21, 2004. As of that date, the Company had a loan balance outstanding of ¥2,250 million ($21,297 thousand) with Tohoku Bunka Gakuen and Yuai Gakuen as joint debtor. The Company may incur a loss on this loan in the future.

As discussed in Note 26.2, the Company obtained the agreement of the Deposit Insurance Corporation on June 17 and 23, 2004, with respect to certain credits for which the cancellation right was exercised pursuant to the clause of "Warranty of Loan Related Assets" described in the Share Purchase Agreement. As a result, the Company will reverse reserves amounting to ¥4,911 million ($46,491 thousand) in fiscal 2004.

Our audits also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 1. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

Deloitte Touche Tohmatsu

June 29, 2004

Member of
Deloitte Touche Tohmatsu

Consolidated Financial Data

Income Analysis

Interest-Earning Assets and Interest-Bearing Liabilities

Years Ended March 31

(Millions of Yen, %)

	Average balance			Interest income/expense			Return/rates		
	2004	2003	Change	2004	2003	Change	2004	2003	Change
Balance of interest-earning assets	**4,817,059**	**4,937,007**	**(119,947)**	**80,651**	**84,172**	**(3,521)**	**1.67**	**1.70**	**(0.03)**
Loans and bills discounted	3,187,965	3,254,343	(66,378)	61,654	64,940	(3,285)	1.93	1.99	(0.06)
Securities	1,189,070	1,196,600	(7,529)	5,789	8,040	(2,251)	0.48	0.67	(0.18)
Call loans and bills bought	103,994	205,157	(101,163)	37	48	(10)	0.03	0.02	0.01
Receivables under resale agreements	240	180	59	0	0	0	0.01	0.00	0.00
Receivables under securities borrowing transactions	194,910	186,235	8,674	61	107	(46)	0.03	0.05	(0.02)
Cash and due from banks	33,911	30,646	3,264	390	514	(123)	1.15	1.67	(0.52)
Balance of interest-bearing liabilities	**4,553,795**	**4,880,686**	**(326,890)**	**16,914**	**24,596**	**(7,682)**	**0.37**	**0.50**	**(0.13)**
Debentures	1,155,711	1,635,804	(480,093)	5,948	12,613	(6,665)	0.51	0.77	(0.25)
Deposits	2,032,486	1,871,616	160,870	8,778	8,150	627	0.43	0.43	(0.00)
Negotiable certificates of deposit	593,344	418,451	174,893	314	549	(234)	0.05	0.13	(0.07)
Borrowed money	21,720	21,428	292	492	804	(312)	2.26	3.75	(1.48)
Commercial paper	218	90	128	0	0	0	0.07	0.07	(0.00)
Call money and bills sold	579,872	636,234	(56,361)	223	277	(53)	0.03	0.04	(0.00)
Payables under repurchase agreements	143,430	205,636	(62,205)	13	10	2	0.00	0.00	0.00
Payables under securities lending transactions	23,478	86,880	(63,402)	36	57	(21)	0.15	0.06	0.08

Fees and Commissions

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net fees and commissions	**8,732**	**7,388**	**1,343**
Fees and commissions received	**9,593**	**8,123**	**1,469**
Debentures, deposits and loan operations	5,961	3,525	2,435
Foreign exchange operations	178	180	(1)
Securities-related operations	720	460	260
Agency services	957	803	154
Safekeeping and safe deposit box services	10	20	(10)
Guarantee operations	188	1,573	(1,384)
Fees and commissions paid	**860**	**734**	**126**
Foreign exchange operations	108	96	11

Trading Revenues

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net trading revenues	**2,865**	**3,446**	**(581)**
Trading profits	**2,865**	**3,446**	**(581)**
Gains on trading securities	114	844	(729)
Gains on securities related to trading transactions	434	182	251
Gains on trading-related financial derivatives	1,921	1,816	104
Others	395	602	(207)
Trading losses	**—**	**—**	**—**

Other Operating Income

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net other operating income	**11,462**	**6,416**	**5,045**
Gains (losses) on foreign exchange transactions	2,347	853	1,493
Gains (losses) on bonds	(1,706)	1,799	(3,505)
Others	10,821	3,764	7,057

Non-Consolidated Business Results

Non-Consolidated Financial Highlights [Five-Year Summary]

Years Ended March 31

(Millions of Yen)

	2004	2003	2002	2001	2000
Operating income	105,335	101,633	100,984	270,720	219,956
Ordinary profit (loss)	7,309	7,437	13,706	98,971	(113,703)
Net income	31,854	22,875	18,563	99,690	—
Capital stock	419,781	419,781	419,781	419,781	353,114
Number of outstanding shares (in thousands)					
Common stock	2,834,870	2,834,870	2,834,870	2,834,870	2,501,536
The 2nd preferred stock				—	102,000
The 3rd preferred stock				—	386,398
The 4th preferred stock	48,144	48,144	48,144	48,144	120,000
The 5th preferred stock	866,667	866,667	866,667	866,667	
Total stockholders' equity	527,582	496,918	476,166	459,690	—
Total assets	5,188,071	5,895,314	5,687,366	6,174,922	8,500,368
Debentures	1,058,973	1,473,126	1,470,193	2,472,528	3,684,002
Deposits	2,607,081	2,555,905	2,177,240	1,778,939	2,635,411
Loans and bills discounted	2,969,770	3,271,087	3,304,379	3,092,049	4,104,221
Securities	971,763	1,356,754	1,060,690	727,758	1,135,653
Total stockholders' equity per share (in yen)	85.89	75.08	67.76	61.94	—
Dividends per share (in yen)					
Common stock	—	—	—	—	—
The 2nd preferred stock				—	—
The 3rd preferred stock				—	—
The 4th preferred stock	5.00	5.00	5.00	5.00	—
The 5th preferred stock	3.72	3.72	3.72	1.86	
(Interim dividends per share (in yen))					
(Common stock)	(—)	(—)	(—)	(—)	(—)
(The 2nd preferred stock)				(—)	(—)
(The 3rd preferred stock)				(—)	(—)
(The 4th preferred stock)	(—)	(—)	(—)	(—)	(—)
(The 5th preferred stock)	(—)	(—)	(—)	(—)	
Basic net income per share (in yen)	10.01	6.84	5.32	36.31	—
Diluted net income per share (in yen)	7.52	5.40	4.90	29.81	—
Dividend payout ratio (%)	—	—	—	—	—
Capital adequacy ratio (domestic standard) (%)	15.65	13.26	14.00	15.10	—
Number of employees	1,345	1,370	1,376	1,438	1,582

Notes: 1. Up to and including the fiscal year ended March 31, 2002, total stockholders' equity per share was calculated by dividing total stockholders' equity at the fiscal year-end, less the product of the number of preferred shares issued and outstanding at the fiscal year-end and the issue price, by the number of common shares issued and outstanding at the fiscal year-end (excluding treasury stock in the fiscal year ended March 31, 2002). However, since total stockholders' equity in the Bank was nil (¥0) for the fiscal year ended March 31, 2000, total stockholders' equity per share for that year is calculated by dividing total stockholders' equity at the fiscal year-end by the number of shares issued and outstanding at the fiscal year-end.

2. Up to and including the fiscal year ended March 31, 2002, basic net income per share was calculated by dividing net income, less total dividends on preferred shares for the fiscal year ended March 31, 2002, by the average number of common shares issued and outstanding during the fiscal year (excluding treasury stock in the fiscal year ended March 31, 2002).
3. For the fiscal year ended March 31, 2000, diluted net income per share is not given as no net income was recorded for that period.
4. From the fiscal year ended March 31, 2002, treasury stock is not included in capital stock. For this reason, total stockholders' equity per share, basic net income per share and diluted net income per share are calculated after deducting the number of shares of treasury stock from the outstanding number of shares.
5. From the fiscal year ended March 31, 2003, total stockholders' equity per share, basic net income per share and diluted net income per share are calculated by applying Financial Accounting Standard No. 2, "Accounting Standard for Earnings per Share" and Financial Accounting Standards Implementation Guidance No. 4, "Implementation Guidance for Accounting Standard for Earnings per Share."
6. Number of employees does not include executive officers, locally hired overseas staff or the Bank's employees seconded to other firms.

Non-Consolidated Financial Review

1. Income Analysis

In the fiscal year ended March 31, 2004, by achieving appropriate lending margins and keeping procurement costs in check, the Bank achieved steady growth in net interest income. The net non-interest portion of net revenue (net fees and commissions, net trading revenues and net other operating income) grew 48.4%. General and administrative expenses remained under tight control. As a result of these factors, business profit before general loan-loss reserve increased 26.8%, to ¥42.5 billion.

The Bank made steady disposals of problem loans and carried out rigorous write-offs and reserve provisions, which resulted in total credit-related expenses of ¥6.5 billion. Consequently, net income for the period climbed 39.3%, to ¥31.9 billion.

Income Analysis

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net revenue	**81,647**	**72,208**	**9,438**
Net interest income	62,790	59,500	3,289
Net fees and commissions	7,540	6,229	1,310
Net trading revenues	2,865	3,446	(581)
Net other operating income	8,451	3,031	5,419
General and administrative expenses	**(39,184)**	**(38,729)**	**(454)**
Business profit before general loan-loss reserve	**42,463**	**33,479**	**8,983**
Net provision to general loan-loss reserve (Note 1)	**(7,283)**	**—**	**(7,283)**
Business profit	**35,180**	**33,479**	**1,700**
Other income (loss)	**(27,870)**	**(26,042)**	**(1,828)**
Loss on disposal of problem loans	(22,283)	(16,536)	(5,746)
Gain and loss on stock transactions and loss on write-down of equity securities	11	(1,034)	1,045
Ordinary profit	**7,309**	**7,437**	**(127)**
Special income (Note 2)	**23,878**	**11,946**	**11,931**
Reversal of reserve for possible loan losses	23,033	17,610	5,423
Reversal of reserve for credit losses on off-balance-sheet instruments	—	349	(349)
Income before income taxes	**31,187**	**19,384**	**11,803**
Current income taxes	**189**	**(146)**	**336**
Deferred income taxes	**477**	**3,638**	**(3,161)**
Net income	**31,854**	**22,875**	**8,979**
Total credit-related expenses (Note 3)	**(6,532)**	**1,422**	**(7,955)**

Notes: 1. Net provision to general loan-loss reserve includes net provisions to reserve for credit losses on off-balance-sheet instruments.
2. Reversal of reserve for possible loan losses exceeded provisions to this reserve, resulting in a surplus, which was recorded as a special income item.
3. Total credit-related expenses = Net provision to general loan-loss reserve + Loss on disposal of problem loans + Reversal of reserve for possible loan losses + Reversal of reserve for credit losses on off-balance-sheet instruments.

(1) Net revenue

Net revenue rose 13.1%, to ¥81.6 billion, largely as a result of an increase in net non-interest income.

a. Net interest income

Although lower yields from loans and bills discounted and securities led to a reduction in interest income, improved efficiency in fund procurement resulted in significantly lower interest expenses. As a result, net interest income increased ¥3.3 billion, to ¥62.8 billion.

b. Net fees and commissions

Owing to a rise in fees derived from such operations as syndicated loans and committed lines of credit, net fees and commissions increased ¥1.3 billion, to ¥7.5 billion.

c. Net trading revenues

Owing to the impact of rising interest rates and other factors, net trading revenues declined ¥581 million, to ¥2.9 billion. The Bank maintains the highest standards of risk management in this area of its operations.

d. Net other operating income

Reflecting strong growth in income from such operations as derivatives and foreign exchange transactions, net other operating income jumped ¥5.4 billion, to ¥8.5 billion.

Net Revenue

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net interest income	**62,790**	**59,500**	**3,289**
Interest income	79,718	84,113	(4,395)
Interest expenses	16,928	24,612	(7,684)
Net fees and commissions	**7,540**	**6,229**	**1,310**
Fees and commissions (income)	8,528	7,079	1,449
Fees and commissions (expenses)	988	849	138
Net trading revenues	**2,865**	**3,446**	**(581)**
Trading profits	2,865	3,446	(581)
Trading losses	—	—	—
Net other operating income	**8,451**	**3,031**	**5,419**
Other operating income	13,628	6,195	7,433
Other operating expenses	5,177	3,163	2,014
Net revenue	**81,647**	**72,208**	**9,438**
Business profit	**35,180**	**33,479**	**1,700**

Notes: 1. Interest expenses excludes interest paid on money held in trust, which was nil (¥0) for the fiscal years ended March 31, 2004, and March 31, 2003. Fees and commissions (expenses) excludes bond redemption fees, which were ¥1 million in the fiscal year ended March 31, 2004, and ¥2 million in the fiscal year ended March 31, 2003.
2. Business profit is calculated by subtracting net provision to general loan-loss reserve and general and administrative expenses from net revenue.

(2) General and administrative expenses

Although the Bank reduced rental costs by relocating some branches, the recruitment of specialist staff, computer system-related expenditure and other factors led to a slight increase in general and administrative expenses, to ¥39.2 billion.

General and Administrative Expenses

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
General and administrative expenses	**39,184**	**38,729**	**454**
Personnel	16,019	15,909	110
Property and equipment	21,811	21,331	479
Taxes	1,353	1,487	(134)

(3) Business profit before general loan-loss reserve

Business profit before general loan-loss reserve grew ¥9.0 billion, to ¥42.5 billion. This result was primarily attributable to increases in net interest income, net fees and commissions and net other operating income as well as the successful restraint of general and administrative expenses.

(4) Other loss

a. Credit-related expenses

During the period under review, the Bank made a net provision to general loan-loss reserve (including net provisions to the reserve for credit losses on off-balance-sheet instruments) amounting to ¥7.3 billion. Loss on disposal of problem loans amounted to ¥22.3 billion, which included loan write-offs and losses on the sale of loans and other items.

However, owing to the reversal of reserve for possible loan losses of ¥23.0 billion (the amount exceeding provisions to the reserve), in accordance with the relevant accounting standards, the Bank recorded this amount as special income. As a result, total credit-related expenses amounted to ¥6.5 billion.

b. Gain and loss on stock transactions and loss on write-down of equity securities

The Bank's holdings of equity securities are negligible. As a result, there was no significant impact on net income for the period under review.

Credit-Related Expenses

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Net provision to general loan-loss reserve	**(7,283)**	**—**	**(7,283)**
Other loss:			
Loss on disposal of problem loans	(22,283)	(16,536)	(5,746)
Loan write-offs	(8,331)	(11,927)	3,595
Loss on sale of receivables and other items	(13,952)	(4,609)	(9,342)
Special income:			
Reversal of reserve for possible loan losses	23,033	17,610	5,423
Reversal of reserve for credit losses on off-balance-sheet instruments	—	349	(349)
Total credit-related expenses	**(6,532)**	**1,422**	**(7,955)**

Gain and Loss on Stock Transactions and Loss on Write-Down of Equity Securities

Years Ended March 31

(Millions of Yen)

	2004	2003	Change
Gain and loss on stock transactions and loss on write-down of equity securities	**11**	**(1,034)**	**1,045**
Gain on sale of equity securities	17	204	(187)
Loss on sale of equity securities	(0)	(615)	615
Write-down of equity securities	(6)	(623)	617

(5) Ordinary profit

Ordinary profit was almost unchanged, at ¥7.3 billion. As mentioned previously, a reversal of reserve for possible loan losses was recorded as special income.

(6) Special income

Owing to a reversal of reserve for possible loan losses, special income increased ¥11.9 billion, to ¥23.9 billion.

(7) Net income

Income before income taxes grew ¥11.8 billion, to ¥31.2 billion. After adjustments for income taxes, net income amounted to ¥31.9 billion.

2. Balance Sheet Analysis

Assets, Liabilities and Stockholders' Equity

March 31

(Millions of Yen)

	2004	2003	Change
Assets	**5,188,071**	**5,895,314**	**(707,243)**
Loans and bills discounted	2,969,770	3,271,087	(301,317)
Securities	971,763	1,356,754	(384,990)
Trading account assets	488,449	532,291	(43,841)
Call loans and bills bought	25,431	27,744	(2,312)
Deferred tax assets	12,227	13,270	(1,042)
Reserve for possible loan losses	(162,323)	(199,320)	36,997
Liabilities	**4,660,488**	**5,398,396**	**(737,907)**
Debentures	1,058,973	1,473,126	(414,153)
Deposits (excluding negotiable certificates of deposit)	2,058,961	2,138,399	(79,438)
Negotiable certificates of deposit	548,120	417,506	130,614
Call money and bills sold	420,042	574,895	(154,852)
Total stockholders' equity	**527,582**	**496,918**	**30,663**

(1) Assets

Loans and bills discounted declined ¥301.3 billion, to ¥2,969.8 billion, mainly owing to ongoing efforts to dispose of non-performing assets. Securities decreased ¥385.0 billion, to ¥971.8 billion, which was largely attributable to the disposal of Japanese government bonds, as part of the appropriate management of the Bank's securities portfolio. Reserve for possible loan losses declined ¥37.0 billion, to ¥162.3 billion, owing to further progress in the disposal of problem loans. Consequently, assets decreased ¥707.2 billion, to ¥5,188.1 billion.

(2) Liabilities

Within the context of the Bank's efforts to hold down procurement costs and bolster efficiency in fund procurement, debentures decreased ¥414.2 billion, to ¥1,059.0 billion. The combined balance of deposits and negotiable certificates of deposit rose ¥51.2 billion, to ¥2,607.1 billion, partly reflecting strong growth in time deposits held by retail clients. As a result, total liabilities fell ¥737.9 billion, to ¥4,660.5 billion.

(3) Stockholders' equity

During the period under review, the payment of cash dividends on preferred stock and an increase in retained earnings resulted in a rise in total stockholders' equity of ¥30.7 billion, to ¥527.6 billion.

3. Non-Consolidated Capital Adequacy Ratio (Domestic Standard)

March 31

(Millions of Yen)

			2004	2003
Tier I	Capital		419,781	419,781
	Non-cumulative perpetual preferred stock		272,036	272,036
	Newly issued stock		—	—
	Capital surplus		33,333	33,333
	Other capital surplus		—	—
	Legal reserve		2,449	1,756
	Voluntary reserve		—	—
	Profit carried forward to next term		65,173	37,501
	Others		—	—
	Net unrealized losses on available-for-sale securities		—	—
	Paid-in amount on treasury stock		—	—
	Treasury stock		0	0
	Goodwill		—	—
	Total	**(A)**	**520,737**	**492,372**
	Step-up preferred stock		—	—
Tier II	Forty-five percent of the difference between fair value and book value in respect of land		—	—
	General reserve for possible loan losses		21,702	24,667
	Subordinated debt		1,080	6,598
	Total		**22,782**	**31,265**
	Tier II capital qualifying as capital	**(B)**	**22,782**	**31,265**
Items deducted		**(C)**	**—**	**—**
Capital	**(A) + (B) – (C)**	**(D)**	**543,519**	**523,637**
Risk-weighted assets	Balance-sheet exposure		3,280,382	3,821,930
	Off-balance-sheet exposure		191,963	124,807
	Total	**(E)**	**3,472,346**	**3,946,738**
Capital adequacy ratio (domestic standard)	$\frac{(D)}{(E)}$ **x 100**		**15.65%**	**13.26%**
Tier I ratio (domestic standard)	$\frac{(A)}{(E)}$ **x 100**		**14.99%**	**12.47%**

Notes: 1. The capital adequacy ratio is calculated using the formula stipulated in a Ministry of Finance Notification based on Article 14-2 of the Banking Law, which follows the provisions of Article 17 of the Long-Term Credit Bank Law. The Bank uses the domestic standard.
2. Items deducted (C) is equivalent to the amount held at other financial institutions for their capital-raising purposes.

Non-Consolidated Financial Statements

Non-Consolidated Balance Sheets (Unaudited)

Aozora Bank, Ltd.
March 31, 2004 and 2003

ASSETS	Millions of Yen 2004	Millions of Yen 2003	Thousands of U.S. Dollars 2004
Cash and cash equivalents	¥ 337,977	¥ 290,732	$ 3,199,027
Due from banks	45,588	79,513	431,506
Call loans and bills bought	25,431	27,744	240,715
Receivables under securities borrowing transactions	211,821	166,730	2,004,937
Commercial paper and other debt purchased	67,290	73,867	636,923
Trading account assets	488,449	532,291	4,623,284
Money held in trust	344		3,256
Securities	971,763	1,356,754	9,197,952
Loans and bills discounted	2,969,770	3,271,087	28,109,513
Foreign exchanges	1,355	2,956	12,834
Other assets	167,251	133,179	1,583,068
Premises and equipment	27,923	32,098	264,298
Deferred charges	153	184	1,448
Customers' liabilities for acceptances and guarantees	23,046	114,222	218,138
Deferred tax assets	12,227	13,270	115,739
Reserve for possible loan losses	(162,323)	(199,320)	(1,536,428)
TOTAL	¥5,188,071	¥5,895,314	$49,106,210

LIABILITIES AND STOCKHOLDERS' EQUITY	Millions of Yen 2004	Millions of Yen 2003	Thousands of U.S. Dollars 2004
LIABILITIES:			
Debentures	¥1,058,973	¥1,473,126	$10,023,409
Deposits	2,607,081	2,555,905	24,676,585
Call money and bills sold	420,042	574,895	3,975,797
Payables under repurchase agreements	131,598	204,797	1,245,605
Payables under securities lending transactions	97,322		921,178
Commercial paper	5,000	3,000	47,326
Trading account liabilities	88,529	140,642	837,955
Borrowed money	27,900	23,495	264,080
Foreign exchanges	2	127	25
Other liabilities	174,237	289,987	1,649,195
Liability for employees' retirement benefits	18,846	17,571	178,383
Reserve for credit losses on off-balance-sheet instruments	7,908	625	74,851
Other reserves			2
Acceptances and guarantees	23,046	114,222	218,138
Total liabilities	4,660,488	5,398,396	44,112,529
STOCKHOLDERS' EQUITY:			
Common stock	147,745	147,745	1,398,439
Preferred stock	272,036	272,036	2,574,880
Capital surplus	33,333	33,333	315,508
Retained earnings	71,087	42,697	672,858
Unrealized gain on available-for-sale securities	3,380	1,106	31,996
Total stockholders' equity	527,582	496,918	4,993,681
TOTAL	¥5,188,071	¥5,895,314	$49,106,210

Non-Consolidated Statements of Income (Unaudited)

Aozora Bank, Ltd.

Years Ended March 31, 2004 and 2003

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
INCOME:			
Interest on:			
Loans and discounts	¥ 60,230	¥ 64,609	$ 570,099
Securities	6,318	8,365	59,803
Due from banks	390	514	3,696
Other	12,778	10,624	120,952
Fees and commissions	8,528	7,079	80,728
Trading account profits	2,865	3,446	27,125
Other operating income	13,628	6,195	129,001
Other income	24,609	20,187	232,933
Total income	129,351	121,022	1,224,337
EXPENSES:			
Interest on:			
Debentures	5,965	12,629	56,466
Deposits	9,093	8,702	86,069
Borrowings and rediscounts	714	1,080	6,762
Commercial paper			2
Other	1,154	2,200	10,931
Fees and commissions	989	852	9,369
Other operating expenses	5,174	3,160	48,981
General and administrative expenses	41,174	40,288	389,728
Other expenses	33,895	32,724	320,829
Total expenses	98,163	101,638	929,137
INCOME BEFORE INCOME TAXES	31,187	19,384	295,200
INCOME TAXES			
Current	(189)	146	(1,798)
Deferred	(477)	(3,638)	(4,515)
Total income taxes	(666)	(3,491)	(6,313)
NET INCOME	¥ 31,854	¥ 22,875	$ 301,513

	Yen		U.S. Dollars
	2004	2003	2004
PER SHARE OF COMMON STOCK:			
Basic net income	¥10.01	¥6.84	$0.09
Diluted net income	7.52	5.40	0.07
Cash dividends of the fourth preferred stock	5.00	5.00	0.05
Cash dividends of the fifth preferred stock	3.72	3.72	0.04

Non-Consolidated Statements of Earned Surplus (Unaudited)

Aozora Bank, Ltd.

Years Ended March 31, 2004 and 2003

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Balance at beginning of year	¥41,633	¥22,915	$394,073
Appropriation:			
Cash dividends	(3,464)	(3,464)	(32,794)
Transfer to legal reserve	(692)	(692)	(6,559)
Net income	31,854	22,875	301,513
Balance at end of year	¥69,331	¥41,633	$656,233

Debenture Operations

Outstanding Balance and Average Balance of Debentures

Years Ended March 31

(Millions of Yen)

	2004		2003	
	Term-end balance	Average balance	Term-end balance	Average balance
Aozora debentures	1,007,731	1,092,647	1,387,508	1,517,558
Discounted Aozora debentures . . .	51,241	66,397	85,618	121,246
Total	**1,058,973**	**1,159,044**	**1,473,126**	**1,638,804**

Note: Debentures do not include debenture subscriptions.

Balance by Residual Period

March 31

(Millions of Yen)

	2004			2003		
	Total	Aozora Discounted	Discounted Aozora debentures	Total	Aozora Discounted	Discounted Aozora debentures
Less than 1 year	562,415	511,439	50,976	1,120,036	1,034,713	85,322
1 – 3 years	346,005	345,740	264	286,137	285,842	295
3 – 5 years	150,536	150,536		66,930	66,930	
5 – 7 years	16	16		23	23	
Over 7 years	—	—		—	—	
Total	**1,058,973**	**1,007,731**	**51,241**	**1,473,126**	**1,387,508**	**85,618**

Deposit Operations

Balance by Deposit Account

Years Ended March 31

(Millions of Yen)

			2004			2003		
			Total	Domestic operations	International operations	Total	Domestic operations	International operations
Deposits								
	Liquid deposits	Average balance	481,985	481,985	—	513,763	513,763	—
		(%)	(23.50)	(23.58)	—	(27.18)	(27.65)	—
		Term-end balance	585,182	585,182	—	603,836	603,836	—
		(%)	(28.42)	(28.59)	—	(28.24)	(28.33)	—
	Interest-bearing deposits	Average balance	423,534	423,534	—	465,728	465,728	—
		(%)	(20.65)	(20.72)	—	(24.64)	(25.07)	—
		Term-end balance	477,115	477,115	—	491,509	491,509	—
		(%)	(23.17)	(23.31)	—	(22.98)	(23.06)	—
	Time deposits (in general)	Average balance	1,559,401	1,559,401	—	1,367,800	1,342,225	25,574
		(%)	(76.01)	(76.31)	—	(72.36)	(72.24)	(78.84)
		Term-end balance	1,450,446	1,450,446	—	1,510,515	1,510,515	—
		(%)	(70.45)	(70.86)	—	(70.64)	(70.86)	—
	Deregulated interest rate time deposits (fixed)	Average balance	1,335,812	1,335,812		1,176,656	1,176,656	
		(%)	(65.12)	(65.37)		(62.25)	(63.33)	
		Term-end balance	1,273,686	1,273,686		1,309,365	1,309,365	
		(%)	(61.86)	(62.22)		(61.23)	(61.43)	
	Deregulated interest rate time deposits (floating)	Average balance	223,588	223,588		165,569	165,569	
		(%)	(10.90)	(10.94)		(8.76)	(8.91)	
		Term-end balance	176,760	176,760		201,150	201,150	
		(%)	(8.58)	(8.64)		(9.41)	(9.44)	
	Others	Average balance	10,069	2,210	7,858	8,781	1,919	6,862
		(%)	(0.49)	(0.11)	(100.00)	(0.46)	(0.10)	(21.16)
		Term-end balance	23,332	11,354	11,977	24,047	17,235	6,811
		(%)	(1.13)	(0.55)	(100.00)	(1.12)	(0.81)	(100.00)
	Total	Average balance	2,051,457	2,043,598	7,858	1,890,345	1,857,908	32,437
		(%)	(100.00)	(100.00)	(100.00)	(100.00)	(100.00)	(100.00)
		Term-end balance	2,058,961	2,046,983	11,977	2,138,399	2,131,587	6,811
		(%)	(100.00)	(100.00)	(100.00)	(100.00)	(100.00)	(100.00)
Negotiable certificates of deposit		Average balance	593,344	593,344	—	418,451	415,451	—
		Term-end balance	548,120	548,120	—	417,506	417,506	—
Total		Average balance	2,644,801	2,636,942	7,858	2,308,797	2,276,360	32,437
		Term-end balance	2,607,081	2,595,103	11,977	2,555,905	2,549,093	6,811

Notes: 1. Time deposits (in general) = Time deposits
Deregulated interest rate time deposits (fixed) = Deregulated interest rate time deposits for which the interest up to the due date is determined when the deposits are made.
Deregulated interest rate time deposits (floating) = Deregulated interest rate time deposits for which the interest varies according to changes in market interest rates during the period of deposit.
2. Liquid deposits = Deposits at notice + Ordinary deposits + Current deposits
3. Average balance of domestic offices' foreign-currency denominated transactions in the international operations sector has been computed by the daily current method.

Balance of Time Deposits by Residual Period

March 31

(Millions of Yen)

	2004			2003		
	Total	Deregulated interest rate (fixed)	Deregulated interest rate (floating)	Total	Deregulated interest rate (fixed)	Deregulated interest rate (floating)
Less than 3 months	251,971	228,916	23,055	353,418	296,592	56,825
3 – 6 months	114,082	84,372	29,710	136,091	92,161	43,930
6 months – 1 year	148,565	119,101	29,464	375,610	316,110	59,500
1 – 2 years	144,753	104,473	40,280	163,015	129,370	33,644
2 – 3 years	347,738	310,938	36,800	105,204	101,404	3,800
More than 3 years	443,335	425,885	17,450	377,174	373,724	3,450
Total	**1,450,446**	**1,273,686**	**176,760**	**1,510,515**	**1,309,365**	**201,150**

Outstanding Balance by Depositor

March 31

(Millions of Yen, %)

	2004		2003	
	Balance	Share	Balance	Share
Corporations	612,145	29.82	591,270	27.67
Individuals	1,100,750	53.61	1,004,972	47.04
Public sector	20,616	1.00	92,244	4.32
Financial institutions	319,612	15.57	448,103	20.97
Total	**2,053,123**	**100.00**	**2,136,591**	**100.00**

Note: The above balance does not include negotiable certificates of deposit and deposits in Japan Offshore Market accounts.

Loan Operations

Outstanding Balance of Loans

Years Ended March 31

(Millions of Yen)

		2004			2003		
		Total	Domestic operations	International operations	Total	Domestic operations	International operations
Loans on deeds	Average balance	2,477,061	2,423,986	53,075	2,263,930	2,213,448	50,482
	Term-end balance	2,359,847	2,309,168	50,679	2,440,493	2,388,298	52,194
Loans on notes	Average balance	543,559	542,919	639	841,021	840,533	487
	Term-end balance	440,667	439,716	950	658,342	657,861	480
Overdrafts	Average balance	169,352	169,352	—	162,060	162,060	—
	Term-end balance	162,944	162,944	—	166,727	166,727	—
Bills discounted	Average balance	4,792	4,792	—	5,553	5,553	—
	Term-end balance	6,310	6,310	—	5,524	5,524	—
Total	**Average balance**	**3,194,765**	**3,141,050**	**53,714**	**3,272,565**	**3,221,595**	**50,970**
	Term-end balance	**2,969,770**	**2,918,139**	**51,630**	**3,271,087**	**3,218,412**	**52,675**

Notes: 1. Average balance of domestic offices' foreign-currency denominated transactions in the international operations sector has been computed by the daily current method.

2. The Bank carries out partial and direct write-off of loans. This also applies to the table shown below.

Balance by Residual Period

March 31

(Millions of Yen)

	2004			2003		
	Total	Fixed interest	Floating interest	Total	Fixed interest	Floating interest
Less than 1 year	1,045,331			1,187,608		
1 – 3 years	677,733	383,670	294,063	723,871	501,948	221,923
3 – 5 years	770,410	501,211	269,199	809,208	549,988	259,219
5 – 7 years	212,790	93,919	118,871	245,298	157,093	88,204
Over 7 years	262,906	159,824	103,081	304,363	191,520	112,842
Indefinite period	596	—	596	736	—	736
Total	**2,969,770**			**3,271,087**		

Note: No distinction has been made between fixed interest and floating interest for loans with a residual period of less than 1 year.

Breakdown of Loans and Bills Discounted by Industry

March 31

(Number of Borrowers, Millions of Yen, %)

	2004			2003		
	Number of borrowers	Balance of loans	Share	Number of borrowers	Balance of loans	Share
Loans by domestic offices (excluding Japan Offshore Market accounts)	**5,505**	**2,932,246**	**100.00**	**5,891**	**3,238,635**	**100.00**
Manufacturing	548	439,428	14.99	529	478,405	14.77
Agriculture, forestry and fisheries	9	7,752	0.26	8	7,883	0.24
Mining	8	2,310	0.08	13	11,688	0.36
Construction	100	129,947	4.43	108	153,839	4.75
Utilities	33	20,701	0.71	33	17,648	0.55
Information and communications	156	71,279	2.43	147	70,109	2.16
Transport	170	244,762	8.35	169	312,489	9.65
Wholesale and retail	496	302,888	10.33	469	340,694	10.52
Financial and insurance	104	423,543	14.44	103	464,015	14.33
Real estate	405	574,253	19.58	392	732,163	22.61
Various services	688	487,851	16.64	713	599,553	18.51
Local government	3	5,550	0.19	1	1,200	0.04
Others	2,785	221,977	7.57	3,206	48,943	1.51
Loans by overseas offices (including Japan Offshore Market accounts)	**28**	**37,523**	**100.00**	**24**	**32,452**	**100.00**
Governments and official institutions	—	—	—	—	—	—
Financial institutions	—	—	—	—	—	—
Commercial and industrial	28	37,523	100.00	24	32,452	100.00
Others	—	—	—	—	—	—
Total	**5,533**	**2,969,770**		**5,915**	**3,271,087**	

Breakdown of Loans and Bills Discounted by Collateral

March 31

(Millions of Yen)

	2004	2003
Securities	31,429	37,108
Claims	564,472	617,301
Merchandise	10	10
Land and buildings	643,004	853,542
Factories	1,233	766
Foundations	200,002	275,360
Vessels	27,516	21,128
Others	782,205	897,046
Total	**2,249,874**	**2,702,263**
Guarantees	173,363	177,893
Credits	546,532	390,930
Total	**2,969,770**	**3,271,087**

Note: Includes collateral in which the Bank has a third-party perfected security interest

Write-Off of Loans

March 31

(Millions of Yen)

	2004	2003
Write-off of loans	**8,331**	**11,927**

Reserves for Possible Loan Losses

Years Ended March 31

(Millions of Yen)

	2004					2003				
			Reduction during year					Reduction during year		
	Balance at beginning of year	Provision	Used for specific purpose	Other	Balance at end of year	Balance at beginning of year	Provision	Used for specific purpose	Other	Balance at end of year
General reserve for possible loan losses	167,564	127,890	—	167,564	127,890	175,688	167,564	—	175,688	167,564
Specific reserve for possible loan losses	30,412	33,769	13,963	16,449	33,769	116,882	30,412	76,292	40,589	30,412
Possible loan losses related to non-residents	—	—	—	—	—	—	—	—	—	—
Provision for country risk reserve	1,343	663	—	1,343	663	653	1,343	—	653	1,343

Country Risk Reserve

March 31

(Millions of Yen)

	2004	2003
Indonesia	7,780	8,725
Total	**7,780**	**8,725**
(Percentage of total assets)	**(0.14%)**	**(0.14%)**

Note: Receivables associated with specific overseas countries consist of loans and bills discounted, and are provided for as reserves for possible loan losses (country risk reserve).

Securities

Outstanding Balance and Average Balance of Securities Held

Years Ended March 31

(Millions of Yen)

		2004			2003		
		Total	Domestic operations	International operations	Total	Domestic operations	International operations
Total	**Average balance**	**1,195,745**	**1,033,848**	**161,897**	**1,204,002**	**981,562**	**222,440**
	(%)	**(100.00)**	**(100.00)**	**(100.00)**	**(100.00)**	**(100.00)**	**(100.00)**
	Term-end balance	**971,763**	**838,862**	**132,900**	**1,356,754**	**1,140,692**	**216,061**
	(%)	**(100.00)**	**(100.00)**	**(100.00)**	**(100.00)**	**(100.00)**	**(100.00)**
National government bonds	Average balance	909,623	909,623	—	836,904	836,904	—
	(%)	(76.07)	(87.98)	—	(69.51)	(85.26)	—
	Term-end balance	728,612	728,612	—	965,515	965,515	—
	(%)	(74.98)	(86.86)	—	(71.16)	(84.64)	—
Local government bonds	Average balance	21,723	21,723	—	36,039	36,039	—
	(%)	(1.82)	(2.10)	—	(2.99)	(3.67)	—
	Term-end balance	4,234	4,234	—	70,987	70,987	—
	(%)	(0.44)	(0.50)	—	(5.23)	(6.22)	—
Short-term corporate bonds	Average balance	—	—	—	—	—	—
	(%)	—	—	—	—	—	—
	Term-end balance	—	—	—	—	—	—
	(%)	—	—	—	—	—	—
Corporate bonds	Average balance	74,869	74,869	—	77,146	77,146	—
	(%)	(6.26)	(7.24)	—	(6.41)	(7.86)	—
	Term-end balance	65,351	65,351	—	77,943	77,943	—
	(%)	(6.72)	(7.79)	—	(5.74)	(6.83)	—
Stocks	Average balance	8,561	8,561	—	9,268	9,268	—
	(%)	(0.72)	(0.83)	—	(0.77)	(0.94)	—
	Term-end balance	8,570	8,570	—	8,631	8,631	—
	(%)	(0.88)	(1.02)	—	(0.64)	(0.76)	—
Others	Average balance	180,967	19,070	161,897	244,643	22,203	222,440
	(%)	(15.13)	(1.85)	(100.00)	(20.32)	(2.27)	(100.00)
	Term-end balance	164,993	32,093	132,900	233,676	17,614	216,061
	(%)	(16.98)	(3.83)	(100.00)	(17.23)	(1.55)	(100.00)

Notes: 1. Total for Others is the sum of Domestic operations and International operations.
2. Average balance of domestic offices' foreign-currency denominated transactions in international operations is computed by the daily current method.

Balance of Securities by Residual Period

March 31

(Millions of Yen)

	2004						2003					
	National government bonds	Local government bonds	Short-term corporate bonds	Corporate bonds	Stocks	Others	National government bonds	Local government bonds	Short-term corporate bonds	Corporate bonds	Stocks	Others
Less than 1 year	551,144	1	—	14,705		12,401	569,751	64,700	—	7,163		22,339
1 – 3 years	76,503	123	—	24,868		83,863	158,578	480	—	34,031		69,721
3 – 5 years	80,598	598	—	20,576		15,626	206,552	1,920	—	21,729		82,106
5 – 7 years	—	417	—	2,214		442	25,182	741	—	11,233		6,500
7 – 10 years	20,365	2,604	—	2,987		7,258	5,451	2,629	—	3,785		1,202
Over 10 years	—	489	—	—		—	—	515	—	—		30,738
Indefinite period	—	—	—	—	8,570	45,400	—	—	—	—	8,631	21,069
Total	**728,612**	**4,234**	**—**	**65,351**	**8,570**	**164,993**	**965,515**	**70,987**	**—**	**77,943**	**8,631**	**233,676**

Derivative Transactions

Hedge accounting for interest rate risk

- In the fiscal year ended March 31, 2003, the Bank applied the “risk adjustment approach” specified by the JICPA as a hedge accounting method (macro hedge), to control the interest rate risk arising from the Bank’s extensive portfolio of financial assets and liabilities.
- In the fiscal year ended March 31, 2004, the Bank applied hedge accounting in accordance with the rules stipulated in JICPA Industry Audit Committee Report No. 24.

Hedge accounting for exchange rate risk

- In the fiscal year ended March 31, 2004, the Bank applied hedge accounting in accordance with the rules stipulated in JICPA Industry Audit Committee Report No. 25.

Notes: 1. Unrealized gains or losses on hedging instruments that qualify for hedge accounting are shown below.
2. Valuation gains (losses) from interest rate swaps are posted to the income statement. These included accrued interest income on interest rate swap transactions of ¥160 million for the fiscal year ended March 31, 2004, and ¥1,349 million for the fiscal year ended March 31, 2003.
3. Valuation gains (losses) from currency swaps are posted to the income statement. These included accrued interest expenses on currency swap transactions of ¥86 million for the fiscal year ended March 31, 2004.

Interest Rate Swaps

Years Ended March 31

(Millions of Yen)

	2004				2003			
	Contract amount	Over one year	Fair value	Valuation gains (losses)	Contract amount	Over one year	Fair value	Valuation gains (losses)
Total	**412,400**	**412,400**	**(1,658)**	**(1,658)**	**4,000,712**	**3,350,712**	**28,614**	**28,614**
Receivable fixed rate/ Payable floating rate	412,400	412,400	(1,658)	(1,658)	2,449,000	1,874,000	74,303	74,303
Receivable floating rate/ Payable fixed rate	—	—	—	—	1,551,712	1,476,712	(45,688)	(45,688)
Receivable floating rate/ Payable floating rate	—	—	—	—	—	—	—	—

Currency Swaps

Years Ended March 31

(Millions of Yen)

	2004				2003			
	Contract amount	Over one year	Fair value	Valuation gains (losses)	Contract amount	Over one year	Fair value	Valuation gains (losses)
Total	**63,390**	**31,695**	**(110)**	**(110)**				

Capitalization

History of Capitalization

(Millions of Yen)

Month/Year	Capital increases	Capital thereafter	Remarks
Mar. 1988	2,694	96,364	Conversion of convertible bonds (Nov. 2, 1987–Mar. 31, 1988)
Oct. 1988	2,321	98,686	Conversion of convertible bonds (Apr. 1, 1988–Oct. 31, 1988)
Nov. 1988	27,985	126,671	Compensatory public subscription, 5,000 thousand shares; Issue price ¥11,194; Transfer to capital ¥5,597
Mar. 1989	1,415	128,086	Conversion of convertible bonds (Nov. 1, 1988–March 31, 1989)
Mar. 1990	20,290	148,377	Conversion of convertible bonds (Apr. 1, 1989–March 31, 1990)
Mar. 1991	3,814	152,191	Conversion of convertible bonds (Apr. 1, 1990–March 31, 1991)
Mar. 1992	28	152,220	Conversion of convertible bonds (Apr. 1, 1991–March 31, 1992)
Mar. 1995	71	152,292	Conversion of convertible bonds (Apr. 1, 1994–March 31, 1995)
Oct. 1996	25,500	177,792	Compensatory private placement (the 2nd preferred stock, 102,000 thousand shares); Issue price ¥500; Transfer to capital ¥250
Jul. 1997	83,498	261,290	Compensatory private placement (common stock, 766,039 thousand shares); Issue price ¥218; Transfer to capital ¥109
Jul. 1997	61,823	323,114	Compensatory private placement (the 3rd preferred stock, 386,398 thousand shares); Issue price ¥320; Transfer to capital ¥160
Mar. 1998	30,000	353,114	Compensatory private placement (the 4th preferred stock, 120,000 thousand shares); Issue price ¥500; Transfer to capital ¥250
Sep. 2000	66,666	419,781	Compensatory private placement (common stock, 333,334 thousand shares); Issue price ¥300; Transfer to capital ¥200
Oct. 2000	(260,000)	159,781	Non-compensatory reduction of capital • Capital reduction of ¥105,287 million by redemption of the 2nd preferred stock, 102,000 thousand shares; the 3rd preferred stock, 386,398 thousand shares; and the 4th preferred stock, 71,856 thousand shares • Capital reduction of ¥154,712 million exceeding face amount of common stock and transferred to capital
Oct. 2000	260,000	419,781	Compensatory private placement (the 5th preferred stock, 866,667 thousand shares); Issue price ¥300; Transfer to capital ¥300

Major Shareholders

(As of March 31, 2004)

a. Common Stock

	Number of shares held	Percentage of total outstanding shares
Cerberus NCB Acquisition, L.P. General Partner Cerberus Aozora GP LLC	1,753,328 thousand	61.84%
ORIX Corporation	425,041	14.99
The Tokio Marine and Fire Insurance Co., Ltd.	425,041	14.99
Shinkin Central Bank	5,680	0.20
The Shinkumi Federation Bank	5,680	0.20
The Rokinren Bank	5,680	0.20
THE MICHINOKU BANK, LTD.	5,680	0.20
The Hachijuni Bank, Ltd.	5,680	0.20
THE SURUGA BANK, LTD.	5,680	0.20
The Bank of Kyoto, Ltd.	5,680	0.20
The Chugoku Bank, Limited	5,680	0.20
The Hiroshima Bank, Ltd.	5,680	0.20
The Yamaguchi Bank, Ltd.	5,680	0.20
THE BANK OF FUKUOKA, LTD.	5,680	0.20
THE SHINWA BANK, LTD.	5,680	0.20
THE NISHI-NIPPON BANK, LTD.	5,680	0.20
The Fukuoka City Bank, Ltd.	5,680	0.20

b. The 4th Preferred Stock

	Number of shares held	Percentage of total outstanding shares
Deposit Insurance Corporation	48,144 thousand	100.00%
Total	48,144 thousand	100.00%

c. The 5th Preferred Stock

	Number of shares held	Percentage of total outstanding shares
Resolution and Collection Corporation	866,667 thousand	100.00%
Total	866,667 thousand	100.00%

Corporate Data

Corporate History

April	1957	Established as The Nippon Fudosan Bank, Limited (Capital: ¥1 billion) in accordance with the Long-Term Credit Bank Law
November		Started issuance of debentures
September	1958	Started issuance of discount debentures
July	1964	Started foreign exchange business as an authorized foreign exchange bank
September		Listed stock on the Tokyo Stock Exchange
February	1970	Listed stock on the Osaka Securities Exchange
October	1977	Changed name to The Nippon Credit Bank, Ltd.
May	1991	Established NCB Private Equity Co., Ltd. (currently Aozora Investment Co., Ltd.)
February	1994	Established The Nippon Credit Trust Bank, Ltd. (currently Aozora Trust Bank, Ltd.), the first domestic subsidiary classified as other type of business
December	1998	Started special public management in accordance with the Financial Reconstruction Law and terminated listing of stock on the Tokyo Stock Exchange and the Osaka Securities Exchange
June	1999	Established NCB Servicer Co., Ltd. (currently AOZORA Loan Services Co., Ltd.), and commenced servicer operations in September 1999
June	2000	Share Purchase Agreement regarding the transfer of the Bank's shares is signed between Deposit Insurance Corporation and SOFTBANK CORP., ORIX Corporation, The Tokio Marine and Fire Insurance Co., Ltd., and other financial institutions.
September		Ended special public management
November		Commenced telephone banking services
January	2001	Changed name to Aozora Bank, Ltd.
April		Launched Aozora Direct Time Deposit as a product exclusively available through telephone banking
December		Aozora Card Co., Ltd., was jointly established by ORIX Corporation and ORIX Credit Corporation
January	2002	Adopted AOZORA, a blue elephant, as the Bank's mascot
October		Commenced over-the-counter sales of personal pension life insurance policies
January	2003	Began issuing collateralized loan obligations (CLOs)
March		Moved headquarters
April		Announced the Trinity Plan management strategy
September		Through a common stock tender offer conducted in accordance with the Securities Exchange Law, all common stock of the Bank held by SOFTBANK CORP. was transferred to the ownership of Cerberus NCB Acquisition, L.P. General Partner Cerberus Aozora GP LLC.

Business Activities

- **Debentures**

  Issuance of debentures and discounted debentures

- **Deposits**

  Deposits

  Checking accounts, savings accounts, time deposits, deposits-at-notice, tax-savings deposits, non-residents deposits in yen and deposits in foreign currencies

  Certificates of deposit

  Limited to national and local public entities, bond management firms and other specified customers

- **Lending and guarantee of liabilities**

  Loans, discounts on promissory notes, guarantee of liabilities for equipment funds and long-term operating fund services

  Loans for long-term funds (term exceeding six months), other than equipment funds and long-term operating funds

  Loans for short-term funds (term of less than six months), limited to the total amount of deposits or corresponding funds

  Discounts on promissory notes, guarantee of liabilities and acceptance of promissory notes

- **Securities**

  Securities investment business

  Underwriting of public bonds

  Over-the-counter sales of public bonds, including national government bonds, and securities investment trusts

  Sales and purchase of securities products

  Receipt of payment for stocks or corporate bonds, and payment of dividends

  Registration of public bonds as a registered institution under the Corporate Bonds Registration Law

  Consignment business for soliciting or managing public bonds

  Trust business for secured corporate bonds

- **Domestic exchange**

  Such services as money orders between branches of the Bank and those of other banks, collection of payments, etc.

- **Foreign exchange**

  Remittance to foreign countries and other foreign currency-related businesses

- **Other services**

  Revenue agency for Bank of Japan and agency business for national bonds

  Receipt of public funds of local public entities, including Tokyo

  Agency business for: Japan Finance Corporation for Small and Medium Enterprise; Organization for Workers' Retirement Allowance Mutual Aid; Government Pension Investment Fund; Japan National Oil Corporation; and Welfare and Medical Service Agency

  Custody services

  Rental of safe-deposit boxes

  Lending of securities

  Commercial paper

  Interest rate, currency and other derivative transactions

  Over-the-counter sales of insurance products

Office Directory
(As of July 20, 2004)

Overseas Network

Representative Offices

Singapore Representative Office

Head of South East Asia
Masanao Kobayashi

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#23-02 Suntec Tower 4,
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Senior Representative
Masayuki Ohga

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Jakarta Representative Office

Chief Representative
Hiroshi Matsumoto

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Domestic Network

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Tel: 03-3835-7511

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Tel: 087-821-5521

Fukuoka
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Fukuoka 810-0001
Tel: 092-751-9627

Web site http://www.aozorabank.co.jp/

Business Network

(As of March 31, 2004)

*All companies listed below are consolidated subsidiaries.

Aozora Bank, Ltd.

Operation		Company	Business
Banking operations	Head Office and branches		
	Main affiliate	Aozora Trust Bank, Ltd.	
Securities services	Head Office and branches		
Trust services	Main affiliate	Aozora Trust Bank, Ltd.	*Trust services, banking operations*
Other operations	Main affiliates	AOZORA Loan Services Co., Ltd.	*Distressed loan servicing*
		Aozora Card Co., Ltd.	*Card loan services*
		Aozora Investment Co., Ltd.	*Venture capital investment*
		Aozora Business Service Co., Ltd.	*Administrative temporary staff services*
		Aozora Information Systems Co., Ltd.	*Systems development*
		Blue Planet Corporation	*Management consulting services*

Subsidiaries at a Glance

(As of June 29, 2004)

(Millions of Yen, %)

Company Name	Location	Business Activities	Established	Capital	Aozora Bank's Share-holding	Group Share-holding
Aozora Trust Bank, Ltd.	3-1, Kudan-minami 1-chome, Chiyoda-ku, Tokyo	Trust services, banking operations	February 28, 1994	5,000	100.00	—
AOZORA Loan Services Co., Ltd.	13-5, Kudan-kita 1-chome, Chiyoda-ku, Tokyo	Distressed loan servicing	June 18, 1996	500	67.60	—
Aozora Card Co., Ltd.	3-4, Nibancho, Chiyoda-ku, Tokyo	Card loan services	December 6, 2001	1,000	60.00	—
Aozora Investment Co., Ltd.	3-1, Kudan-minami 1-chome, Chiyoda-ku, Tokyo	Venture capital investment	May 17, 1991	20	100.00	—
Aozora Business Service Co., Ltd.	3-1, Kudan-minami 1-chome, Chiyoda-ku, Tokyo	Administrative temporary staff services	September 21, 1987	10	100.00	—
Aozora Information Systems Co., Ltd.	8-15, Hyakunincho 2-chome, Shinjuku-ku, Tokyo	Systems development	April 1, 1967	150	100.00	—
AOZORA SOFTWARE CORPORATION	8-15, Hyakunincho 2-chome, Shinjuku-ku, Tokyo	Systems development	May 9, 1973	12	—	100.00
Aozora Computer Co., Ltd.	21, Nikkocho 1-chome, Fuchu-shi, Tokyo	Computer operation	April 1, 1991	20	5.00	95.00
Blue Planet Corporation	14-12, Kudan-kita 1-chome, Chiyoda-ku, Tokyo	Management consulting services	April 20, 2001	370	55.10	—

Note: From late August 2004, Aozora Information Systems Co., Ltd., and AOZORA SOFTWARE CORPORATION will be relocated to: 17-11, Kanda-Nishikicho 3-chome, Chiyoda-ku, Tokyo.

Directors and Auditors, Executive Officers

(As of June 29, 2004)

DIRECTORS AND AUDITORS

Chairman
Edward G. Harshfield*

President
Hirokazu Mizukami*

Director
Yoshihiko Miyauchi

Director
James Danforth Quayle

Director
Frank W. Bruno

Director
Jake Garn

Director
Yoichiro Iwama

Director
Pieter Korteweg

Director
Lawrence B. Lindsey

Director
Michael E. Rossi

Director
John L. Steffens

Director
John C. Stomber

Director
Kiyoshi Tsugawa

* Concurrently serving as Executive Officer

Standing Auditor
Ken Shigihara

Auditor
Alan S. Waldenberg

Auditor
Mitch R. Fulscher

Auditor
Akira Tachimoto

EXECUTIVE OFFICERS

Senior Managing Executive Officer
Yuji Inagaki

Senior Managing Executive Officer
Izumi Ogura

Senior Managing Executive Officer
David Hackett

Senior Managing Executive Officer
William Chute

Senior Managing Executive Officer
Lee Millstein

Senior Managing Executive Officer
Yoshiyuki Kurihara

Senior Managing Executive Officer
Takeyoshi Morikawa

Managing Executive Officer
Tomoaki Ishii

Managing Executive Officer
Norimichi Kurakake

Managing Executive Officer
Hirokazu Takino

Executive Officer
Ryoichi Kawai

Executive Officer
Tadaaki Satoyoshi

Executive Officer
Yukimichi Nakatani

Executive Officer
Katsutoshi Ishida

Executive Officer
Akira Takami

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Forward-Looking Statements
This annual report contains forward-looking statements regarding the Bank's financial condition and results of operations. These forward-looking statements, which include the Bank's views and assumptions with respect to future events, involve certain risks and uncertainties. Actual results may differ from forecasts due to changes in economic conditions.

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Investors Relations Department,
Financial Management Division,
Aozora Bank, Ltd.

AOZORA BANK, LTD.

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