

Higo Bank

Annual Report 2005



Profile

The Higo Bank is a regional bank whose main business base is Kumamoto Prefecture in central Kyushu. Possessing a varied sweep of natural beauty, including the volcano Mt. Aso, which boasts the world's largest caldera, and the scenic Amakusa area with its 200 islands of widely varying sizes, the prefecture is home to thriving agricultural, forestry, and fisheries industries.

In recent years, Kumamoto Prefecture has become a center for leading-edge industries, notably semiconductors, for which it has been called "Japan's Silicon Valley." The number of high-tech companies setting up shop in Kumamoto is still on the increase, and is expected to contribute greatly to the area's development in the near future.

The center of Kumamoto city has also been seeing the successive start-ups of a number of redevelopment projects, and accelerating progress is being made in bolstering the city's transport infrastructure. Roughly half of the extension of the Shinkansen Line from Fukuoka down the west coast of Kyushu to Kagoshima has been completed, and the construction of a modern road traffic network, principally to feed the Kyushu Expressway is making progress.

These conditions offer many opportunities to vitalize the region by cultivating small and medium-sized



mainstay businesses and promoting new businesses to support these new industries. Kumamoto is home to many new industries, and we have a support organization in which the public and private sectors work together, called the Kumamoto Prefecture Business Promotion Support Center. The center was established with funds from the Kumamoto prefectural government and the Higo Bank.

In addition to our main work of banking operations, we also put our energy into creating a better living environment for the prefecture's citizens by supporting organizations such as The Distribution Economics Institute of Kumamoto Area and the Kumamoto Development Research Center. Higin Venture Capital Co., Ltd., established in 1996, also cooperates with these organizations to provide comprehensive support to match the growth stage of the venture companies.

The Bank has continued to be active in supporting cultural events such as concerts and art exhibits as well as in promoting environmental conservation efforts, with the establishment of the Higo Water Resources Protection Foundation. Believing that it will become all the more important for us to make broad social contributions, we set up a Regional Culture Department in our Head Office in 1995 to act as a organization specializing in social contributions.

Contents

<i>Profile</i>	1
<i>Message from the President</i>	2
<i>Management Policy</i>	3
<i>Results (Non-Consolidated)</i>	4
<i>Excellent Financial Indicators</i>	5
<i>ISO 14001 certification</i>	8
<i>Corporate Data</i>	9
<i>Service Network</i>	10
<i>Financial Section</i>	11

Message from the President



Higo Bank marked the 80th anniversary of its foundation on July 25, 2005, a milestone reached thanks to the strong backing of all stakeholders. I would like to take this opportunity to convey my sincere appreciation to our customers, shareholders and other stakeholders for the consistent support they have shown the Bank.

During the term under review, the Japanese financial industry made progress in dealing with the bad-debt problems at major financial institutions, and the focus of financial revitalization is shifting from the megabanks to regional banks. With customers looking at financial institutions with an increasingly cautious eye, following the complete abolition of the deposit insurance system in April 2005, it is becoming increasingly important for regional banks to step up efforts to finance small and medium-sized enterprises (SMEs) and corporate revitalization.

Other key tasks are to bolster management capability and improve convenience for local users as measures to strengthen the function of community-based financing services, as an enhanced function of relationship banking.

In this environment, all employees and officers of the Bank are as one in their commitment to realize our vision of forging a robust corporate structure based on the strong support provided by our customers. This vision represents our basic goal under the second three-year medium term management plan for the new century, which went into effect in fiscal 2003. It also reflects our long-standing corporate missions of putting the customer first, contributing to the prosperity of the region we serve while maintaining a high level of corporate ethics, and fostering a free and creative corporate culture.

As we pursue these initiatives, we continue to ask for the understanding and support of all of our stakeholders.

A handwritten signature in black ink that reads "H. Oguri". The signature is written in a cursive, flowing style.

July 2005

Hiroo Oguri, *President*

Management Policy

The “Second Medium-Term Management Plan for the New Century”

Higo Bank’s new medium-term management plan, the second of the new century, covers the three years from April 1, 2003 to March 31, 2006. Our basic goal is to forge a robust corporate structure based on the strong support of the customer, and we aim to bolster our earnings power and financial soundness by engaging in further dialogue with customers, understanding them better and supplying them with high-quality tailored financial services that meet their needs appropriately.

For fiscal 2005, as the final year of the plan, we will work to further strengthen earnings power by simultaneously increasing gross business profit and operational efficiency, while maintaining current high level of financial soundness.

SLOGAN

***“Prospering with the customer, and winning the customer’s full support
(with every employee dedicated to his or her role)”***

The basic concept of the new management plan is ensuring that every employee performs his or her duties, to realize our goal of “Putting the customer first.” To this end, we have chosen as our slogan, “Prospering with the customer, and winning the customer’s full support (with every employee dedicated to his or her role).”

PERIOD OF PLAN

April 1, 2003 to March 31, 2006 (3 years)

BASIC GOAL

Forging a robust corporate structure based on the strong support of the customer

- ▶ **The strong support of the customer:** We will earn this by understanding customer needs, putting ourselves in the customer’s position and providing high-quality tailored financial services.
- ▶ **Forging a robust corporate structure:** We will achieve this by bolstering earning power and enhancing risk management by strengthening our marketing and maximizing our efficiency.

INDICATOR	TARGET
1. ROE (Return on Equity)	5% or more
2. Adjusted OHR (Ratio of expenses to core gross business profit)	Less than 65%
3. Capital ratio (domestic standards)	10% or more
4. Core net business profit per employee	¥10 million or more

CONDUCT CHARTER

1. Taking the customer’s viewpoint, we will conduct our business in a spirit of gratitude.
2. By prioritizing dialogue with customers, we will increase our understanding of customer needs.
3. By fully understanding our customer’s problems, we will solve them quickly and decisively.
4. By observing laws, regulations and in-house standards we will fully meet our social responsibilities and conduct ourselves within the bounds of common sense.

Results (Non-Consolidated)

Deposits and loans

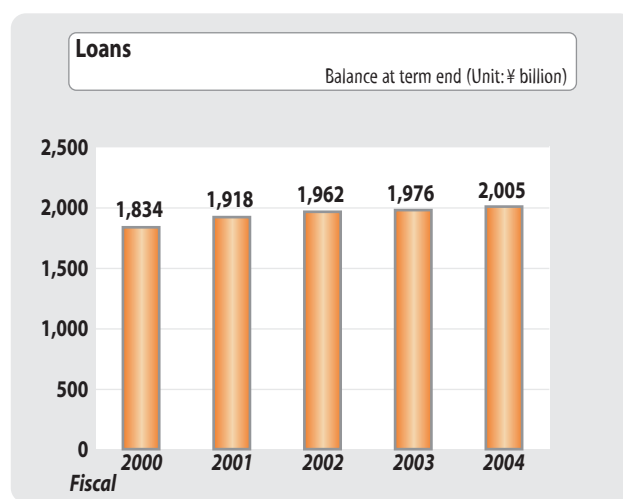
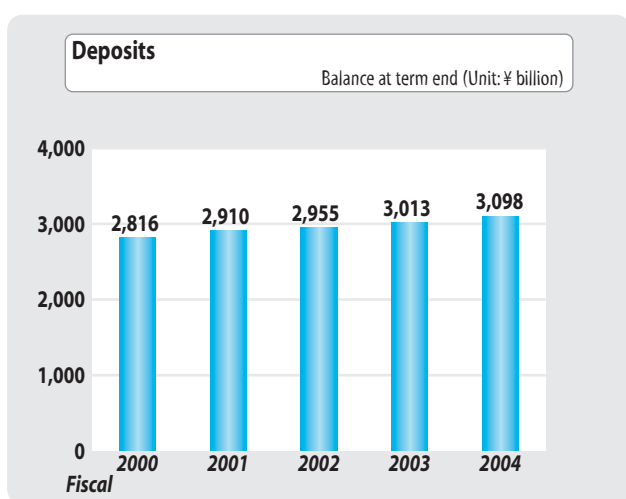
Deposits

As a result of closely tailoring its marketing initiatives to customer and regional needs, the Higo Bank increased total deposits by ¥85,119 million, or 2.8%, to ¥3,098,654 million. The average balance of deposits also increased ¥74,537 million, or 2.5%, to ¥3,038,955 million.

The term-end balance of negotiable certificate of deposits stood at ¥63,528 million. The balance of customer assets — excluding yen denominated deposits — rose 28.4%, or ¥61,100 million, to ¥276,200 million.

Loans

By actively responding to the needs of local SMEs, public bodies and retail banking customers (individuals), the Bank raised its term-end balance of loans outstanding by ¥29,402 million, or 1.5% compared with the previous term-end, to ¥2,005,973 million. The average balance of loans outstanding rose ¥18,117 million, or 1.0%, to ¥1,895,636 million.



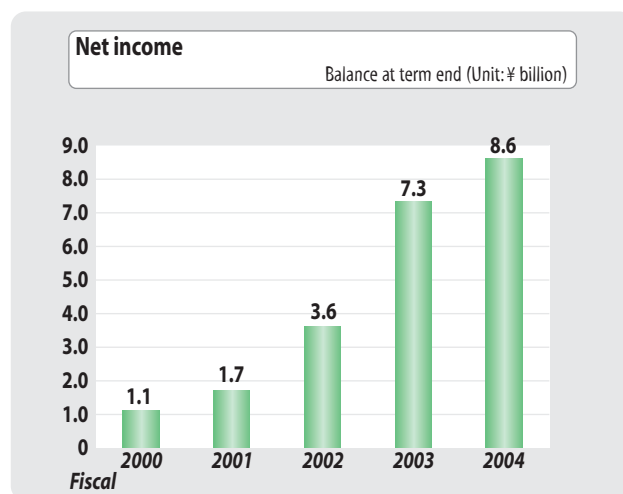
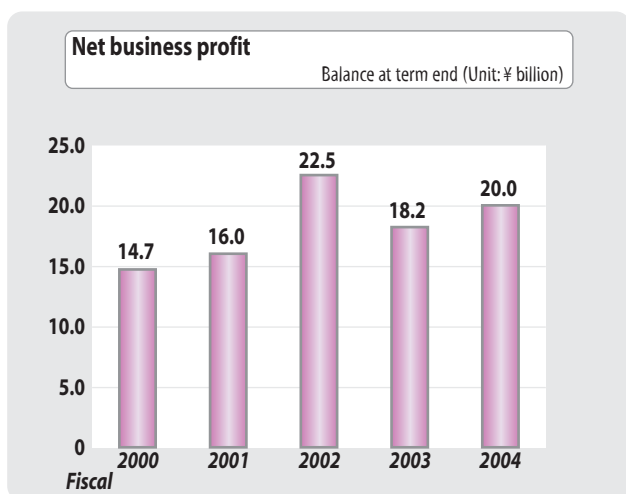
Revenues

Net business profit

With a reduction in expenses and a decline in the provision for reserve for possible loan losses, net business profit increased ¥1,782 million, to ¥20,060 million.

Net income

Net income was up ¥1,311 million, at ¥8,650 million.



Excellent Financial Indicators

High Evaluations from the Ratings Institutions

Ratings are a concise, symbolic representation of credit risk, indicating a company's credibility and the reliability of its performance with respect to liabilities. The ratings institution, as a disinterested third party, publishes its overall evaluation of a company's financial position and earnings capability. Higo Bank has received official ratings from three ratings institutions in Japan and abroad, and we received high evaluations, ranking A, for each of the long-term ratings.

(Long-term credit rating: as of March 31, 2005)

- ❖ **Moody's Investors Service** **A2**
- ❖ **Standard & Poor's** **A**
- ❖ **Rating and Investment Information, Inc.** **A+**

*A top-class regional bank in Kyushu, with high standards among the domestic banks.

Moody's Credit Rating



S&P Credit Rating



Unrealized Gain on Securities

The Bank recorded a ¥52,400 million gain on valuation of securities.



Period ended March 31, 2005

(billions of yen)

	Unrealized gain
Held-to-maturity	0.5
Available-for-sale securities	51.8
Shares	38.8
Bonds, etc.	13.0
Total	52.4

Higo Bank has an Excellent Reputation as a Financially Sound Bank Carrying Few Non-Performing Loans

Disclosure of Claims under the Financial Reconstruction Law (non-consolidated)

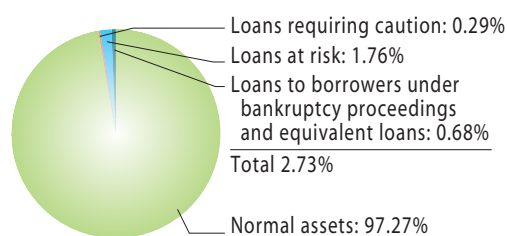
As of March 31, 2005 (billions of yen)

	Loan balance	Coverage by collateral and guarantees	Reserve for possible loan losses	Coverage ratio
Loans to borrowers under bankruptcy proceedings and equivalent loans	13.7	8.2	5.4	100.0%
Loans at risk	35.7	21.3	12.7	95.4%
Loans requiring caution	5.9	2.8	1.1	68.3%
Subtotal	55.4	32.4	19.4	93.6%
Normal loans	1,978.9			
Total	2,034.4			

Note: Figures have been rounded down to the nearest ¥100 million. Fractions in the coverage ratios up to 0.04 have been rounded down, and from 0.05 upward have been rounded up.

Higo Bank's non-performing loans under the disclosure standards mandated by the Financial Reconstruction Law stood at ¥55,493 million as of the end of March 2005, representing 2.73% of the total loan balance. This is an extremely low level compared with Japan's other regional banks.

Of these non-performing loans, 93.6% are covered by collateral, guarantees, and the reserve for possible loan losses, providing a sufficient buffer for the Bank.



Explanation of terms

Loans to borrowers under bankruptcy proceedings and equivalent loans

This category indicates loans to borrowers undergoing bankruptcy proceedings or corporate rehabilitation, or loans to borrowers in a state of virtual bankruptcy.

Loans at risk

This category indicates loans to borrowers who, while not yet in a state of bankruptcy, are suffering from a severe deterioration in financial conditions and are very likely unable to repay outstanding loans.

Loans requiring caution

This category indicates loans for which no repayments, including payments of interest, have been made for 3 months or more, or whose repayment conditions have been eased.



Note: Non-performing loans held by the entire Higo Bank Group on a consolidated basis, including subsidiaries and affiliates, in accordance with the disclosure standards under the Financial Reconstruction Law, totaled ¥57,811 million, accounting for 2.82% of the group's total loan balance.

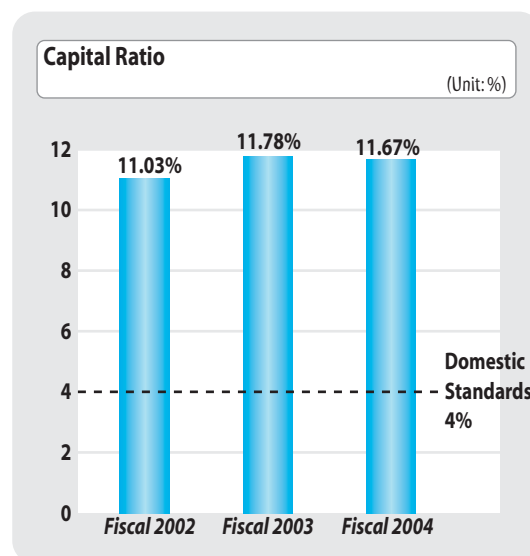
One of the Highest Capital Ratios Among Japan's Regional Banks

The capital ratio is the ratio of a bank's total equity (capital stock, retained earnings and other items) to total risk-weighted assets, including loans, marketable securities and others. This figure is growing in importance for banks as an indicator of their financial soundness and overall safety as the deregulation of Japan's financial services industry progresses.

As of March 31, 2005, Higo Bank's capital ratio was 11.67% based on domestic standards. This is one of the highest ratios of any regional bank in Japan, and is far above the 4% standard for capital adequacy set in the Prompt Corrective Action by the government.

Using only Tier I capital, which includes common stock and certain other elements of equity, the capital ratio stands at 10.90%. When applying the BIS common minimum standard, Higo Bank's capital ratio remains at a high 12.83%.

*Risk-weighted assets are calculated by multiplying assets and the credit equivalents of off-balance-sheet transactions by a risk factor that varies depending on the credit quality of each asset.



Acquisition of Bank's Own Shares and Retirement of Treasury Stock

To bolster investor value, in December 2001 Higo Bank began purchasing its own shares as part of its capital policy. Based on a resolution made at the annual shareholders' meeting in June 2004, we instituted a policy of acquiring our own shares, up to the closing of the 2005 annual shareholders' meeting, with a maximum limit of 5,000,000 shares of treasury stock and an outlay of up to ¥4,000 million. From June 2004 to March 2005, we acquired 3,669,000 shares, with a total purchase price of ¥2,609 million. We then retired these shares at the end of March 2005.

Since December 2001, we have purchased a cumulative total of 12,954,000 shares at a value of ¥7,198 million. We had retired all of these shares by the end of March 2005.

By retiring treasury stock and reducing the number of shares issued, we are increasing per-share stock value and improving capital efficiency. In continuing our policy of acquiring our own stock whenever possible and focusing on increasing profitability, we believe that we can raise investment efficiency and meet the expectations of all shareholders and investors.

ISO14001 certification

Higo Bank is actively addressing environmental issues, as demonstrated by our efforts to protect water resources over many years. To take these activities to a new level systematically and continuously, we drew up environmental policies in April 2004.

In October 2004, we acquired the ISO14001 certification, the international standard for environmental management systems.

Environmental policies of Higo Bank

We believe that the basis of our social contribution is to serve the local community based on our corporate mission of contributing to the prosperity of the region we serve while maintaining a high level of corporate ethics.

Higo Bank's main business base is Kumamoto Prefecture in central Kyushu. Possessing a varied sweep of natural beauty, Kumamoto Prefecture is home to the volcano Mt. Aso, which boasts the world's largest caldera, plains that extend from the foot of the mountain, and woodlands that occupy 70% of the prefectural land area. The prefecture enjoys access to clean and pure groundwater that supplies drinking water to 900,000 residents in the urban area of Kumamoto, and the scenic Amakusa area fosters a rich ecological system.

All Higo Bank employees and officers are aware of their responsibility to preserve the natural environment of Kumamoto for future generations. With this recognition, we are committed to achieving the following objectives:

1. To reduce the environmental burden generated by the corporate activities of the Bank.
2. To assist our customers in their activities to protect the environment through the operations of the Bank.
3. To make an active contribution to local communities addressing environmental issues.

To achieve these objectives, the Bank will take the following steps:

1. Build and operate an environmental management system that meets ISO14001 standards, and continue to improve the system.
2. Comply with laws and regulations related to the environment and other provisions recognized by the Bank.
3. Take measures to prevent pollution.
4. Ensure that the Bank's employees are aware of these environmental policies and disclose the policies to the general public.

April 1, 2004

The Higo Bank

Hiroo Oguri, President

Acquisition of ISO14001 Certification

On October 22, 2004, Higo Bank acquired the ISO14001 certification of the international standard for environmental management. The certification is for the divisions in our main building and the annex of the head office as well as affiliates of the Bank.

We are the first financial institution in Kyushu to acquire the ISO14001 certification. In the certification review, the examination authority gave high marks to our environmental efforts, particularly in the following areas:

- Cooperative activities with the Higo Water Resources Protection Foundation
- Credit analysis system that pays attention to the environment

We have received strong praise for our cooperative activities with the Higo Water Resources Protection Foundation, reflecting our long-standing commitment to grass-roots activities in local communities. In our credit analysis system, our efforts to make use of banking operations were highly valued.

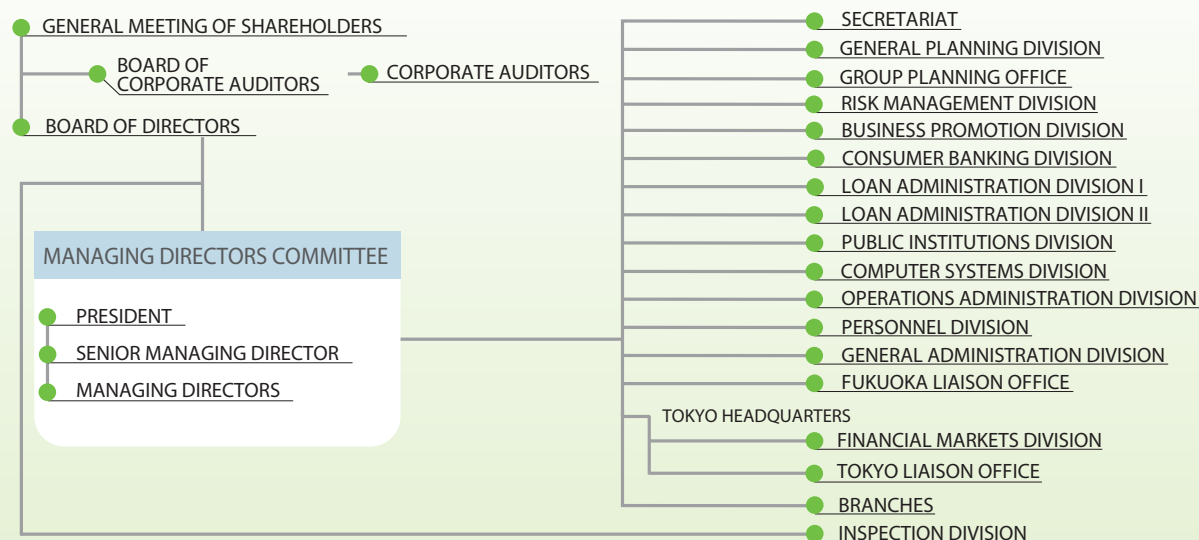
Corporate Data As of July 1, 2005

Established: July 25, 1925
 Total Assets: ¥3,453.1 billion
 Deposits: ¥3,098.6 billion
 Loans and Bills Discounted: ¥2,005.9 billion
 Capital Stock: ¥18.1 billion

Capital Ratio: 11.67% (domestic standards)
 Number of Employees: 2,099
 Number of Offices: 130
 (Head Office and 114 domestic branches, 12 sub-branches, 3 agencies and 1 overseas representative office)

(As of March 31, 2005)

Organization



Board of Directors and Corporate Auditors

President and Representative Director	Hiroo Oguri		
Senior Managing Director and Representative Director	Masaomi Mori		
Managing Directors	Ken Inomata	Moriaki Yamada	Hiroo Nagata
	Takahiro Kai	Kenichi Hida	
Directors	Tetsuo Uemura	Hisaya Kakihara	
	Shunichi Toyoda	Hidenobu Takagi	
Corporate Auditors	Toshiyuki Sumita (standing)	Toshiro Maruoka (standing)	
	Naosuke Tokuyama	Jiro Yamada	Tadasu Yonawa

Principal Shareholders As of March 31, 2005

Name	Number of shares		Equity stake (%)
	(thousand)		
Meiji Yasuda Life Insurance Co.	11,621		4.78
Higo Bank Employees' Shareholding Association	11,177		4.60
Mizuho Corporate Bank, Ltd.	10,291		4.23
Takara Kogyo Co., Ltd.	7,682		3.16
Japan Trustee Services Bank, Ltd. (trust account)	7,033		2.89
Sompo Japan Insurance Inc.	6,854		2.82
The Bank of Fukuoka, Ltd.	5,864		2.41
Tokio Marine & Nichido Fire Insurance Co., Ltd.	5,319		2.19
The Master Trust Bank of Japan, Ltd. (trust account)	4,824		1.98
The Dai-ichi Mutual Life Insurance Company	4,041		1.66
Total	74,709		30.76

Service Network

Head Office

1, Renpeicho, Kumamoto 860-8615
Phone: (096) 325-2111

Financial Markets Division

Tokyo Main Office

10-2, Kyobashi 2-chome,
Chuo-ku, Tokyo 104-0031
Phone: (03) 3535-2431
Facsimile: (03) 3535-6129

Kumamoto Office

1, Renpeicho, Kumamoto 860-8615
Phone: (096) 326-8646
Facsimile: (096) 326-8027

Foreign Exchange Offices

Head Office

1, Renpeicho, Kumamoto 860-8615
Phone: (096) 326-8642

Tokyo Branch

10-2, Kyobashi 2-chome,
Chuo-ku, Tokyo 104-0031
Phone: (03) 3561-3121

Osaka Branch

NM Plaza Midosuji 6F,
6-3, Awaji-cho 3-chome,
Chuo-ku, Osaka 541-0047
Phone: (06) 6208-6551

Fukuoka Branch

8-1, Daimyo 2-chome,
Chuo-ku, Fukuoka 810-0041
Phone: (092) 741-7935

Yatsushiro Branch

3-25, Honmachi 2-chome,
Yatsushiro 866-0861
Phone: (0965) 32-3171

Tamana Branch

548, Takase, Tamana 865-0025
Phone: (0968) 73-2151

Suidocho Branch

3-31, Kamitoricho,
Kumamoto 860-0845
Phone: (096) 352-3111

Kagoshima Branch

1-3, Yamanokuchicho,
Kagoshima 892-0844
Phone: (099) 223-7221

Amakusa Branch

1-1, Suwamachi, Hondo 863-0037
Phone: (0969) 22-2151

Ozu Branch

182-1, Muro, Ozumachi 869-1235
Phone: (096) 293-3131

Matsubase Branch

920-1, Matsubase, Matsubasemachi
869-0502
Phone: (0964) 32-1121

TOPICS

Opening of Shanghai Representative Office

On December 1, 2004 Higo Bank established a Shanghai Representative Office in Raffles City, which faces the People's Park in central Shanghai. The office will respond to customer needs for operating businesses in China. The address of the Shanghai Representative Office is as follows:
Unit 4007, Office Tower of Raffles City Shanghai,
No. 268 Xi Zang Middle Road, Shanghai, 200001,
People's Republic of China



THE HIGO BANK, LTD.
CONSOLIDATED BALANCE SHEETS
March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
ASSETS:			
Cash and due from banks	¥ 62,174	¥ 78,650	\$ 578,955
Call loans and bills bought	44,204	15,505	411,621
Monetary claims purchased	7,848	4,138	73,079
Trading assets	782	2,834	7,281
Money held in trust	5,000	5,000	46,559
Securities	1,259,223	1,162,591	11,725,700
Loans	2,006,186	1,976,639	18,681,311
Foreign exchange	2,860	1,659	26,631
Other assets	20,981	27,441	195,372
Premises and equipment	44,951	45,134	418,577
Deferred tax assets	371	1,100	3,454
Customers' liabilities for acceptances and guarantees	24,637	31,207	229,416
Reserve for possible loan losses	(24,703)	(25,235)	(230,030)
Total assets	<u>¥ 3,454,518</u>	<u>¥ 3,326,668</u>	<u>\$ 32,167,967</u>
LIABILITIES AND SHAREHOLDERS' EQUITY:			
Liabilities:			
Deposits	¥ 3,160,747	¥ 3,040,562	\$ 29,432,414
Call money and bills sold	5,369	6,182	49,995
Collateral received under securities lending transactions	6,321	3,120	58,860
Borrowed money	-	3	-
Foreign exchange	6	10	55
Other liabilities	17,655	16,157	164,400
Reserve for retirement benefits	17,687	18,107	164,698
Deferred tax liabilities	1,904	0	17,729
Deferred tax liabilities related to land revaluation	6,182	6,190	57,565
Acceptances and guarantees	24,637	31,207	229,416
Total liabilities	<u>3,240,512</u>	<u>3,121,544</u>	<u>30,175,174</u>
Minority interests:			
Minority interests	1,346	1,222	12,533
Total minority interests	<u>1,346</u>	<u>1,222</u>	<u>12,533</u>
Shareholders' equity:			
Common stock	18,128	18,128	168,805
Capital surplus	8,133	8,133	75,733
Retained earnings	145,114	141,193	1,351,280
Excess of land revaluation	9,120	9,132	84,924
Unrealized gain on securities, net of tax	32,271	27,354	300,502
Less: Treasury stock	109	42	1,014
Total shareholders' equity	<u>212,660</u>	<u>203,901</u>	<u>1,980,258</u>
Total liabilities, minority interests and shareholders' equity	<u>¥ 3,454,518</u>	<u>¥ 3,326,668</u>	<u>\$ 32,167,967</u>

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

THE HIGO BANK, LTD.
CONSOLIDATED STATEMENTS OF INCOME
For the years ended March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Income:			
Interest on loans	¥ 38,266	¥ 39,198	\$ 356,327
Interest on and dividends from securities	15,518	15,844	144,501
Other interest	392	226	3,650
Fees and commissions	9,854	9,272	91,759
Trading revenue	140	137	1,303
Other operating income	1,054	2,159	9,814
Other income	1,475	2,057	13,734
Total income	<u>66,701</u>	<u>68,896</u>	<u>621,109</u>
Expenses:			
Interest on deposits	916	1,227	8,529
Interest on borrowings and call money	115	160	1,070
Interest on securities lending transactions	81	74	754
Other interest	1,964	1,970	18,288
Fees and commissions	3,146	2,886	29,295
Other operating expenses	1,685	2,208	15,690
General and administrative expenses	40,737	40,836	379,336
Other expenses	3,580	6,405	33,336
Total expenses	<u>52,226</u>	<u>55,771</u>	<u>486,320</u>
Income before income taxes	14,474	13,125	134,779
Income taxes			
- Current	4,104	4,963	38,215
- Deferred	1,558	632	14,507
Minority interests	123	134	1,145
Net income	<u>¥ 8,686</u>	<u>¥ 7,394</u>	<u>\$ 80,882</u>
Per share amounts			
Primary net income	¥ 35.11	¥ 29.47	\$ 0.32

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

THE HIGO BANK, LTD.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
For the years ended March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Common stock:			
Balance at beginning of year	¥ 18,128	¥ 18,128	\$ 168,805
Balance at end of year	18,128	18,128	168,805
Capital surplus:			
Balance at beginning of year	8,133	8,133	75,733
Balance at end of year	8,133	8,133	75,733
Retained earnings:			
Balance at beginning of year	141,193	136,934	1,314,768
Reversal of excess of land revaluation	11	46	102
Net income	8,686	7,394	80,882
Dividends paid	(1,476)	(1,495)	(13,744)
Bonuses to directors and corporate auditors	(47)	(41)	(437)
Retirement of treasury stock	(3,254)	(1,643)	(30,300)
Balance at end of year	145,114	141,193	1,351,280
Excess of land revaluation:			
Balance at beginning of year	9,132	9,178	85,035
Reversal of excess of land revaluation	(11)	(46)	(102)
Balance at end of year	9,120	9,132	84,924
Unrealized gain on securities:			
Balance at beginning of year	27,354	21,743	254,716
Unrealized gain on securities	4,917	5,611	45,786
Balance at end of year	32,271	27,354	300,502
Treasury stock:			
Balance at beginning of year	(42)	(3)	(391)
Net change during the year	(67)	(39)	(623)
Balance at end of year	(109)	(42)	(1,014)
Total shareholders' equity	¥ 212,660	¥ 203,901	\$ 1,980,258

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

THE HIGO BANK, LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the year ended March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Cash flows from operating activities:			
Income before income taxes	¥ 14,474	¥ 13,125	\$ 134,779
Depreciation and amortization	2,880	2,787	26,818
(Decrease) increase in allowance for possible loan losses	(532)	1,150	(4,953)
Decrease in reserve for retirement benefits	(420)	(1,343)	(3,910)
Interest and dividend income	(54,176)	(55,268)	(504,479)
Interest expenses	3,076	3,434	28,643
Investment securities losses	996	585	9,274
Gains on money held in trust	(92)	(174)	(856)
Increase in loans	(30,048)	(15,310)	(279,802)
Increase in deposits	85,967	56,923	800,512
Increase (decrease) in negotiable certificates of deposit	34,217	(15,690)	318,623
Decrease (increase) in due from banks	7,495	(5,885)	69,792
Increase in call loans	(32,410)	(5,130)	(301,797)
Decrease in call money	(813)	(30,044)	(7,570)
Increase (Decrease) in collateral received under securities lending transactions	3,200	(7,588)	29,797
Interest income (cash basis)	54,902	56,389	511,239
Interest expense (cash basis)	(3,123)	(3,984)	(29,080)
Other	1,365	7,000	12,710
Total	86,958	977	809,740
Payments for income taxes	(2,771)	(4,192)	(25,803)
Net cash provided by (used in) operating activities	84,186	(3,215)	783,927
Cash flows from investing activities:			
Payments for purchases of securities	(258,514)	(242,411)	(2,407,244)
Proceeds from sales of securities	2,542	36,988	23,670
Proceeds from redemption of securities	168,823	203,528	1,572,055
Payments for increase in money held in trust	-	(310)	-
Proceeds from decrease in money held in trust	82	462	763
Payments for purchases of premises and equipment	(1,373)	(1,427)	(12,785)
Proceeds from sales of premises and equipment	51	506	474
Net cash used in investing activities	(88,388)	(2,663)	(823,056)
Cash flows from financing activities:			
Cash dividends paid	(1,476)	(1,495)	(13,744)
Payment for purchase of treasury stock	(3,331)	(1,690)	(31,017)
Proceeds from sales of treasury stock	9	8	83
Net cash used in financing activities	(4,798)	(3,178)	(44,678)
Effect of exchange rate changes on cash and cash equivalents	18	8	167
Net decrease in cash and cash equivalents	(8,981)	(9,049)	(83,629)
Cash and cash equivalents at beginning of year	66,616	75,665	620,318
Cash and cash equivalents at end of year	¥ 57,634	¥ 66,616	\$ 536,679

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

THE HIGO BANK, LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The consolidated financial statements have been prepared from the accounts maintained by The Higo Bank, Ltd. (the “Bank”) and its consolidated subsidiaries (together referred to as the “Group”) in accordance with the provisions set forth in the Japanese Commercial Code and in conformity with accounting principles and practices generally accepted in Japan, the Banking Law of Japan, the Financial Statements Regulation (ordinances promulgated by the Ministry of Finance), and the Uniform Accounting Standards for Banks in Japan, which are different from International Accounting Standards in certain respects as to application and disclosure requirements.

Certain items presented in the consolidated financial statements filed with the Ministry of Finance in Japan have been reclassified for the convenience of readers outside Japan.

The consolidated financial statements are not intended to present the consolidated financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries and jurisdictions outside Japan.

Amounts of less than ¥ 1 million have been omitted. As a result, the yen totals shown in the financial statements and notes thereto do not necessarily agree with the sum of the individual account balances.

2. Summary of Significant Accounting Policies

(1) Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Bank and its subsidiaries, after the elimination of all material intercompany transactions, balances, and unrealised gains and losses.

The number of subsidiaries and affiliates as of March 31, 2005 and 2004 was as follows:

	2005	2004
Consolidated subsidiaries	7	7
Affiliates (accounted for under the equity method)	1	1

(2) Fiscal year-ends of consolidated subsidiaries

Fiscal year-ends for the consolidated subsidiaries are as follows:

March 31 7 consolidated subsidiaries

(3) Summary of significant accounting policies

(a) Cash and cash equivalents

Cash and cash equivalents in the consolidated statements of cash flows are composed of cash on hand and due from the Bank of Japan.

(b) Foreign currency translation

The Bank maintains its accounting records in yen. Foreign currency assets and liabilities are translated into yen at the exchange rates prevailing on the balance-sheet dates. There were no assets/liabilities denominated in foreign currency held by consolidated subsidiaries.

(c) Trading assets and Trading liabilities

Securities, monetary receivables, money trusts, etc. included in “Trading assets” or “Trading liabilities” are stated at market value. Trading-related derivative financial instruments are valued based on the assumption that they are settled at the end of the fiscal year.

Profits and losses from trading assets and trading liabilities are recorded in “Trading revenue/expenses” on a trade date basis. In the case of securities, monetary receivables, etc., held for trading purposes, “Trading revenue/expenses” include interest received/paid during the fiscal year and the difference between the valuation profits and losses at the end of the current fiscal year and those at the end of the previous fiscal year. In the case of trading-related derivative financial instruments, “Trading revenue/expenses” include interest received/paid during the fiscal year and the difference in profits and losses at the end of the fiscal year and at the end of the previous fiscal year based on the assumption that transactions were settled.

Consolidated subsidiaries of the Bank have no transaction for trading assets and trading liabilities, and similar transaction.

(d) Financial Instruments

i) Securities

Held-to-maturity debt securities are stated at amortized cost as determined by the moving average method. Other securities with market quotations are stated at the market prices prevailing at the balance sheet date. Cost of sales of such securities is determined by the moving average method. Net unrealized gains or losses on these securities, net of tax, are reported as a separate item in the shareholders' equity. Other securities without market quotations are stated at cost or amortized cost as determined by the moving average method. Investments in securities included in money trusts managed separately, the primary objective of which is to invest in securities, are stated at market prices. Other investments in money trusts are accounted for in a manner consistent with those discussed above. In the previous years, equity interests in limited liability partnerships (LLPs), and those in voluntary partnership under the Civil Code and silent partnership under the Commercial Code characteristics of which are similar to those of LLPs had been included in “Other assets”. However, from this fiscal year, these are included in “Others” of “Securities” as they are defined as securities under the Securities and Exchange Law by the “The Law for Partial Amendments to Securities and Exchange Law” (Law No.97 dated June 9, 2004).

ii) Derivatives

Derivatives other than those designated as “ Trading assets and Trading Liabilities ” (see (c) Trading assets and Trading liabilities above) are stated at fair value, with changes in fair value included in net profit or loss for the period in which they arise, except for derivatives that are designated as “hedging instruments” (see iii) Hedge Accounting below).

iii) Hedge Accounting

a) Hedge of interest rate risks

The Bank has adopted the deferral method of hedge accounting and, for specific interest rate swaps, the accrual method of hedge accounting.

In the previous year, the Bank utilized a macro hedge methodology using derivatives to manage overall interest rate risk arising in various financial assets and liabilities held, including loans and deposits, pursuant to “Temporary Treatment for Accounting and Auditing of Application of Accounting Standard for Financial Instruments in Banking Industry” (JICPA Industry Audit Committee Report No.15).

The gain and loss deferred under the previous macro hedge methodology are amortized as interest expense over 2 years from the previous year corresponding to the remaining period to maturity and to the notional principal of the hedging instruments. Deferred hedge profits and losses are nil and nil at March 31, 2005, respectively and nil and ¥13 million at March 31, 2004, respectively.

b) Hedging foreign currency exchange risks

The Bank has adopted the deferral method of hedge accounting for hedges of the risks arising from financial assets and liabilities due to the fluctuation of foreign exchange rates which is described in “Treatment for Accounting and Auditing of Application of Accounting Standard for Foreign Currency Transactions in Banking Industry” (JICPA Industry Audit Committee Report No.25). Hedge effectiveness is assessed by checking that the foreign currency amounts of hedging instruments corresponds to the amount of hedged items, financial monetary assets and liabilities denominated in foreign currencies, using currency swaps or foreign exchange swaps transactions entered into to mitigate the foreign exchange rate risk arising on hedged items.

Net unrealized gain or losses on hedging instruments are included in “Other assets”. Gross unrealized losses at March 31, 2005 and 2004 are ¥847 million (\$7,887 thousand) and ¥588 million, respectively. Gross unrealized gains at March 31, 2005 and 2004 are ¥14 million (\$130 thousand) and ¥49 million, respectively.

(e) Premises and equipment

i) Depreciation of premises and equipment is computed as follows.

Premises: Depreciation is computed using the declining balance method over the estimated useful lives of the respective assets.

However, depreciation on buildings acquired after April 1, 1998 (excluding annex facilities of buildings) is computed by the straight-line method.

Equipment: Depreciation is computed by the declining balance method over the estimated useful lives of the respective assets.

The useful lives of premises and equipment are generally as follows:

Building 20 ~ 50 years

Equipment 5 ~ 20 years

- ii) Based on the Law Concerning the Revaluation of Land (Law 34 promulgated on March 31, 1998), land for commercial-use was revalued on March 31, 1999.

In accordance with Article 3, Paragraph 3 of Law 34, revaluations were made based on the prices that form the basis for calculating land value taxes as set out in Article 2, Subparagraph 3 of the Ordinance Implementing the Law Concerning Revaluation of Land (Government Ordinance No.119 dated March 31, 1998), with appropriate adjustments.

The unrealized gain (net of tax effect) is recorded as "Excess of land revaluation" in shareholders' equity and the tax effect is recorded as "Deferred tax liabilities" related to land revaluation. The difference between the book value of the land revalued in accordance with Article 10 of the Law Concerning the Revaluation of Land and the market value was ¥11,313 million (\$105,345 thousand) and ¥10,034 million at March 31, 2005 and 2004, respectively.

- (f) Costs of computer software developed or obtained for internal use

Costs of computer software developed or obtained for internal use are deferred and amortized using the straight-line method over the estimated useful lives of 5 years.

- (g) Reserve for loan losses

The reserve for loan losses is provided as follows:

- 1) The reserve for claims on debtors who are legally or substantially bankrupt is provided based on the amount remaining after deducting the amount expected to be collected through the disposal of collateral or through the execution of guarantees.
- 2) The reserve for claims on debtors who are not currently legally bankrupt but are likely to become bankrupt is provided at the amount considered necessary after due consideration of the results of a solvency assessment. The solvency assessment identifies the amounts expected to remain after deducting the amounts expected to be collected through the disposal of collateral or through the execution of guarantees.
- 3) The reserve for claims on debtors other than the above is provided based on default rates calculated using actual defaults during a certain period in the past.

All claims are assessed by the branches and credit supervision divisions based on the internal rules for the self-assessment of assets. The Asset Examination Division,

which is independent from the branches and credit supervision divisions, audits these self-assessments, and the reserve is provided based on the audit results.

With respect to the claims with collateral or guarantees on debtors who are legally or substantially bankrupt, estimated uncollectible amounts have been directly charged off against claims. The charge off amounted to ¥11,238 million (\$104,646 thousand) and ¥13,113 million for the years ended March 31, 2005 and 2004, respectively.

(h) Reserve for retirement benefits

The reserve for retirement benefits, which is provided for the payment of employees' retirement benefits, represents the estimated present value of projected benefit obligations in excess of the fair value of the plan assets, taking in to account adjustments for unrecognized prior year service costs and unrecognized actuarial differences. Unrecognized prior service costs and unrecognized actuarial differences are amortized on a straight-line basis over a period of 10 years from the year following the year in which they arise.

The Bank obtained an approval for an exemption from the benefits related to future employee service by the Ministry of Health, Labor and Welfare on November 14, 2003 in connection with the substitutional portion of the Employee Pension Fund.

The substitutional portion, which will be transferred to the government in a subsequent year (minimum liability reserve) measured at the end of this fiscal year is approximately ¥10,720 million (\$99,823 thousand). The Bank has estimated a gain on exemption of ¥6,019 million (\$56,048 thousand) calculated applying the Article 44-2 of the "Practical Guideline for Accounting Standard for Employees' Retirement Benefits" assuming that the transfer took place at March 31, 2005.

(i) Leases

Finance leases (other than those that are deemed to transfer ownership of the leased assets to the lessees) are accounted for as operating leases.

(j) Valuation of assets and liabilities in consolidated subsidiaries

Assets and liabilities in consolidated subsidiaries are revalued to fair market value when a majority interest in the subsidiaries is purchased.

(k) Per share information

Net income per share is computed based on the weighted average number of shares of common stock outstanding during the year.

Per share information is as follows:

	Yen		U.S. dollars
	2005	2004	2005
Net assets per share	¥ 876.17	¥ 823.90	\$ 8.15
Net income per share	35.11	29.47	0.32

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Net income	¥ 8,686	¥ 7,394	\$ 80,882
Deducting bonuses to directors	(44)	(47)	(409)
Net income attributable to common stock	8,642	7,347	80,473

	Thousand	
	2005	2004
The average number of shares outstanding during the year	246,121	249,244

(l) Treasury stock

The number of common stock held by consolidated subsidiaries and affiliates accounted for by the equity method was 158 thousand and 68 thousand at March 31, 2005 and 2004, respectively.

(m) Accounting standard for impairment of fixed assets

On August 9, 2002, the Business Accounting Council in Japan issued “Accounting Standard for Impairment of Fixed Assets”. The standard requires that fixed assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss shall be recognized in the income statement by reducing the carrying amount of impaired assets or a group of assets to the recoverable amount to be measured as the higher of net selling price and value in use.

The standard shall be effective for the Bank for the fiscal years beginning on April 1, 2005. An earlier adoption is permitted for the fiscal years beginning on April 1, 2004. In addition, an earlier adoption is permitted for annual financial statements for the fiscal year ending on March 31, 2004.

The Bank is currently in the process of assessing the potential impact that this standard will have on the Group’s financial position.

3. U.S. Dollar Amounts

The Group maintains its accounting records in yen. The U.S. dollar amounts included in the consolidated financial statements and notes thereto represent the arithmetic results of translating yen to dollars on the basis of ¥107.39 to US\$1, the approximate rate of exchange prevailing on March 31, 2005. The inclusion of such dollar amounts is solely for convenience and is not intended to imply that assets and liabilities originated in yen have been or could be readily converted, realized, or settled in dollars at the given rate or at any other rate.

4. Supplemental Information

With the promulgation of “The Law for Partial Amendments to Local Tax Law” (Law No.9) on March 31, 2003, a portion of taxation basis of enterprise taxes was changed (pro forma standard taxation basis introduced), and “added value component” and “capital component” were newly added to the taxation basis from the fiscal years beginning on April 1, 2004. As a result, the Bank included the portion of enterprise tax amounts calculated based on “added value component” and “capital component” in “General and administrative expenses” on the consolidated statements of income from this fiscal year pursuant to “Practical Treatment for Presentation of Pro Forma Standard Taxation Portion of Enterprise Tax on Corporation in the Statement of Income” (Accounting Standards Board of Japan, Practice Report No.12)

5. Cash and Cash Equivalents

Reconciliation of the cash and cash equivalent balances on the consolidated statements of cash flows and the account balances on the consolidated balance sheets are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Cash and due from banks	¥ 62,174	¥ 78,650	\$ 578,955
Foreign currency deposits	(3,221)	(10,398)	(29,993)
Other deposits	(1,317)	(1,636)	(12,263)
Cash and cash equivalent	¥ 57,634	¥ 66,616	\$ 536,679

6. Securities

The following disclosure includes certificates of deposits included in “Cash and due from banks”, commercial paper included in “Monetary claims purchased” as well as “Securities” on the balance sheet.

“Securities” on the balance sheet included stocks of affiliates amounting to ¥193 million (\$1,797 thousand) and ¥170 million at March 31, 2005 and 2004, respectively.

(1) Carrying value and market value of securities

(a) Trading securities

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Carrying value	¥ 782	¥ 2,834	\$ 7,281
Unrealized gain (loss) charged to income	2	(0)	18

(b) Held-to-maturity debt securities with market value.

Municipal government bonds	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Carrying value	¥ 15,655	¥ 22,859	\$ 145,777
Market value	16,130	23,650	150,200
Net unrealized gain	474	791	4,413
Gains	474	791	4,413
Losses	-	-	-

Corporate bonds	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Carrying value	¥ 3,724	¥ 3,764	\$ 34,677
Market value	3,821	3,842	35,580
Net unrealized gain	97	78	903
Gains	101	92	940
Losses	3	13	27

Note: Market values are mainly based on their market prices at the balance sheet date.

(c) Other securities with market value

	Millions of yen				
	2005				
	Acquisition cost	Carrying value	Net Unre- alized gain	Gains	Losses
Stocks	¥ 37,451	¥ 76,254	¥ 38,802	¥ 39,407	¥ 604
Bonds					
Japanese					
Government Bonds	535,236	542,129	6,893	7,008	
Municipal					
Government Bonds	182,193	186,016	3,822	4,215	
Corporate Bonds	244,465	246,610	2,145	2,236	
	961,895	974,756	12,861	13,461	
Others	183,651	183,860	208	2,321	2,1
Total	¥ 1,182,998	¥ 1,234,871	¥ 51,872	¥ 55,189	¥ 3,317

		Millions of yen				
		2004				
		Acquisition cost	Carrying value	Net Unre- alized gain	Gains	Losses
Stocks		¥ 35,008	¥ 69,413	¥ 34,405	¥ 35,485	¥ 1,080
Bonds						
	Japanese					
	Government Bonds	456,761	461,258	4,496	5,992	1,495
	Municipal					
	Government Bonds	172,289	175,179	2,890	3,673	783
	Corporate Bonds	263,033	264,475	1,442	1,949	506
		892,084	900,913	8,829	11,614	2,785
Others		157,781	160,443	2,661	3,300	638
	Total	¥1,084,874	¥1,130,771	¥ 45,896	¥ 50,401	¥ 4,504

		Thousands of U.S. dollars				
		2005				
		Acquisition cost	Carrying value	Net Unre- alized gain	Gains	Losses
Stocks		\$ 348,738	\$ 710,066	\$ 361,318	\$ 366,952	\$ 5,624
Bonds						
	Japanese					
	Government Bonds	4,984,039	5,048,226	64,186	65,257	1,070
	Municipal					
	Government Bonds	1,696,554	1,732,153	35,589	39,249	3,650
	Corporate Bonds	2,276,422	2,296,396	19,973	20,821	847
		8,957,025	9,076,785	119,759	125,346	5,577
Others		1,710,131	1,712,077	1,936	21,612	19,666
	Total	\$11,015,904	\$11,498,938	\$ 483,024	\$ 513,911	\$ 30,887

Note: Carrying values on the Consolidated Balance Sheet are stated mainly based on their market prices at the balance sheet date.

In the fiscal year ended March 31, 2005 and 2004, losses on impairment of ¥243 million (\$2,262 thousand) and ¥449 million were recorded for stocks with market value, respectively.

Losses on impairment were recorded for all securities with market value whose market values at the balance sheet dates were less than 50% of the cost of these securities. In addition, losses on impairment are recorded for certain securities with market value whose market values at the balance sheet dates fell 30% or more but less than 50% after assessment of price trends and credit risks of issuers.

- (2) Held-to-maturity debt securities sold during the fiscal years ended March 31, 2005 and 2004.

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Corporate Bonds			
Cost	¥ -	¥ 49	\$ -
Sold at	-	51	-
Gains (Losses)	-	1	-

The reason of sold : Early redemption of Bonds

- (3) Other securities sold during fiscal years ended March 31, 2005 and 2004.

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Amounts sold	¥ 3,099	¥ 36,398	\$ 28,857
Gross gains	70	1,060	651
Gross losses	694	682	6,462

- (4) Carrying value of securities without market value

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Held-to-maturity Debt Securities	¥ 3,050	¥ 3,250	\$ 28,401
Other Securities	1,713	1,769	15,951

- (5) Reclassified securities

The Bank and its consolidated subsidiaries had no reclassified securities.

(6) Maturities of held-to-maturity debt securities and other securities held.

		Millions of yen			
		2005			
		Within one year	Over one year but within 5 years	Over 5 years but within 10 years	Over 10 years
Bonds					
Japanese Government Bonds	¥	64,071	¥ 317,347	¥ 49,225	¥ 111,484
Municipal Government Bonds		27,711	116,592	57,367	-
Corporate Bonds		46,934	174,327	30,419	1,702
	¥	<u>138,718</u>	¥ <u>608,267</u>	¥ <u>137,012</u>	¥ <u>113,187</u>
Others					
		14,054	98,426	59,626	-
	¥	<u>152,772</u>	¥ <u>706,694</u>	¥ <u>196,639</u>	¥ <u>113,187</u>

		Millions of yen			
		2004			
		Within one year	Over one year but within 5 years	Over 5 years but within 10 years	Over 10 years
Bonds					
Japanese Government Bonds	¥	24,111	¥ 336,577	¥ 50,482	¥ 50,087
Municipal Government Bonds		23,150	123,291	51,597	-
Corporate Bonds		73,257	179,205	19,027	-
	¥	<u>120,518</u>	¥ <u>639,074</u>	¥ <u>121,107</u>	¥ <u>50,087</u>
Others					
		27,040	72,056	55,016	-
	¥	<u>147,558</u>	¥ <u>711,130</u>	¥ <u>176,124</u>	¥ <u>50,087</u>

		Thousands of U.S. dollars			
		2005			
		Within one year	Over one year but within 5 years	Over 5 years but within 10 years	Over 10 years
Bonds					
Japanese Government Bonds	\$	596,619	\$ 2,955,088	\$ 458,376	\$1,038,122
Municipal Government Bonds		258,040	1,085,687	534,193	-
Corporate Bonds		437,042	1,623,307	283,257	15,848
	\$	<u>1,291,721</u>	\$ <u>5,664,093</u>	\$ <u>1,275,835</u>	\$ <u>1,053,980</u>
Others					
		130,868	916,528	555,228	-
	\$	<u>1,422,590</u>	\$ <u>6,580,631</u>	\$ <u>1,831,073</u>	\$ <u>1,053,980</u>

(7) Details of unrealized gain on other securities

The unrealized gain on other securities on the balance sheet consists of the following:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Gross unrealized gain on Other securities	¥ 51,872	¥ 45,896	\$ 483,024
Less: deferred tax liabilities	19,608	18,542	182,586
Net unrealized gain on other securities	32,264	27,354	300,437
Less: Minority interest	0	0	0
Unrealized gain on Other securities of Affiliates attributable to the parent company	8	1	74
Unrealized gain on Other securities on the balance sheet	¥ 32,271	¥ 27,354	\$ 300,502

7. Money Held in Trust

The carrying and market values of money held in trust, as of March 31, 2005 and 2004, were as follows:

(1) Money Held in Trust Held for Investment

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Carrying value	¥ 5,000	¥ 5,000	\$ 46,559
Unrealized gain charged to income	591	810	

(2) Money Held in Trust Held to Maturity

None.

(3) Other Money Held in Trust (Money Held in Trust other than Held for Investment or Held to Maturity)

None.

8. Loans

Loans at March 31, 2005 and 2004 include the following:

	Millions of yen		Thousands of US dollars
	2005	2004	2005
Bankruptcy loans (1)	¥ 5,935	¥ 4,141	\$ 55,265
Non-accrual loans (2)	40,612	39,765	378,173
Accruing loans past due 3 months or more	328	1,070	3,054
Restructured loans (3)	5,647	15,783	52,584
Total	¥ 52,523	¥ 60,761	\$ 489,086

- (1) Bankruptcy loans represent non-accrual loans to borrowers who are legally bankrupt as defined in Article 96-1-3 and 4 of the Japanese Tax Law Enforcement Regulation (Article 97 of 1965 Cabinet Order).
- (2) Non-accrual loans represent non-accrual loans other than (i) bankruptcy loans and (ii) loans for which payments of interest are deferred in order to assist or facilitate the restructuring of borrowers in financial difficulties.
- (3) Restructured Loans represent loans on which contracts were amended in favor of borrowers (e.g., reduction of or exemption from stated interest, deferral of interest payments, extension of maturity dates, renunciation of claims) in order to assist or facilitate the restructuring of borrowers in financial difficulties.

Loans include bills discounted amounting to ¥28,918 million (\$269,280 thousand) and ¥33,482 million at March 31, 2005 and 2004, respectively. The Bank is entitled, without limitation, to dispose these bills discounted.

“Other expenses” in the statements of income includes loans written off amounting to nil and ¥1,328 million for the fiscal year ended March 31, 2005 and 2004, respectively.

9. Assets Pledged

Assets pledged as collateral are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Securities	¥ 33,845	¥ 30,836	\$ 315,159

Liabilities related to the above pledged assets are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Deposits	¥ 10,683	¥ 7,023	\$ 99,478
Collateral received under securities lending transactions	¥ 6,321	¥ 3,120	\$ 58,860

In addition, securities totalling ¥111,161 million (\$1,035,115 thousand) and ¥65,231 million are pledged as collateral for settlement of exchange, short-term funding, derivatives or as variation margin, etc. at March 31, 2005 and 2004, respectively.

10. Commitment Line Agreements Related to Overdrafts and Loans

Commitment line agreements relating to overdrafts and loans represent agreements to allow customers to extend overdrafts or loans up to agreed amounts at the customers' request as long as no violation against the conditions of the agreements exists.

Unused commitment lines under such agreements are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Original maturity within one year or cancelable by the Bank at any time without any penalty	¥ 559,917	¥ 552,642	\$ 5,213,865
Others	10,880	1,170	101,312
Total	¥ 570,797	¥ 553,812	\$ 5,315,178

The amount of unexercised commitment lines does not necessarily affect the future cash flows of the Bank and consolidated subsidiaries because many such agreements are terminated without being exercised. Many of these agreements have provisions, which stipulate the Bank and consolidated subsidiaries may deny extending loans or decrease the commitment line when there are certain changes in financial markets, certain issues in securing loans and other reasons. The Bank requests collateral in the form of premises or securities as deemed necessary upon providing such commitments. In addition, the Bank monitors the financial condition of customers in accordance with its internal rules on a regular basis (semi-annually) and takes necessary measures including revisiting the terms of commitments and other means to prevent credit losses.

11. Reserve for retirement benefits

The Bank operates defined benefit retirement plans covering substantially all employees. Pension plans have been operating since April 1, 1970 (plan under the Japanese Welfare Pension Insurance Law) and since April 1, 1995 (tax qualified pension plan) in addition to the lump-sum retirement benefit plan. The Bank obtained an approval for an exemption from the benefits related to future employee service by the Ministry of Health, Labor and Welfare on November 14, 2003 in connection with the substitutional portion of the Employee Pension Fund.

The reserve for retirement benefits as of March 31, 2005 and 2004 is analyzed as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Projected benefit obligations	¥ (64,506)	¥ (62,510)	\$ (600,670)
Plan assets	33,390	30,324	310,922
	(31,116)	(32,186)	(289,747)
Unrecognized transition amount	-	-	-
Unrecognized actuarial differences	16,862	17,706	157,016
Unrecognized prior service cost	(3,227)	(3,628)	(30,049)
	(17,481)	(18,107)	(162,780)
Prepaid pension cost	205	-	1,908
Reserve for retirement benefits	¥ (17,687)	¥ (18,107)	\$ (164,698)

Notes: 1. The above table includes amounts related to the portion subject to the Japanese Welfare Pension Insurance Law.

2. The substitutional portion, which will be transferred to the government in a subsequent year (minimum liability reserve) measured at the end of this fiscal year is approximately ¥10,720 million (\$99,823 thousand). The Bank has estimated a gain on exemption of ¥6,019 million (\$56,048 thousand) calculated applying the Article 44-2 of the "Practical Guideline for Accounting Standard for Employees' Retirement Benefits" assuming that the transfer took place at March 31, 2005.
3. Discretionary additional payments are not included.
4. Consolidated subsidiaries have adopted simplified methods to calculate projected benefit obligations.

Net pension expense related to the retirement benefits for the year ended March 31, 2005 and 2004 was as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Service cost	¥ 1,270	¥ 1,336	\$ 11,826
Interest cost	1,246	1,345	11,602
Expected return on plan assets	(990)	(909)	(9,218)
Amortization of prior service cost	(400)	(276)	(3,724)
Amortization of actuarial differences	2,077	1,469	19,340
Amortization of transition amount	-	-	-
Other	14	24	130
Net pension expense	¥ 3,217	¥ 2,991	\$ 29,956

Note: Net pension expense of certain consolidated subsidiaries adopting simplified methods is included in the service cost.

Assumptions used in the calculation of the above information were as follows:

	<u>2005</u>	<u>2004</u>
Discount rate	2.0%	2.0%
Expected rate of return on plan assets		
Japanese Welfare Pension Insurance Law	3.5%	4.0%
Tax qualified pension plan	2.5%	3.0%
Method of attributing the projected benefits to periods of services	Straight-line basis	Same as on the left
Amortization of prior service cost	10 years from the year differences arise	Same as on the left
Amortization of unrecognized actuarial differences	10 years from the year following the year differences arise	Same as on the left

12. Income taxes

At March 31, 2005 and 2004, significant components of deferred tax assets and liabilities were as follows:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2004</u>	<u>2005</u>
Deferred tax assets:			
Reserve for possible loan losses	¥ 8,993	¥ 10,433	\$ 83,741
Reserve for retirement benefit	6,977	6,989	64,968
Depreciation	1,823	1,908	16,975
Loss on impairment of securities	2,592	2,488	24,136
Other	517	467	4,814
Total	<u>20,903</u>	<u>22,288</u>	<u>194,645</u>
Valuation allowance	<u>(2,628)</u>	<u>(2,528)</u>	<u>(24,471)</u>
Deferred tax assets	<u>18,275</u>	<u>19,759</u>	<u>170,174</u>
Deferred tax liabilities:			
Unrealized gain on Other securities	(19,607)	(18,541)	(182,577)
Excess of land revaluation real estate	(117)	(117)	(1,089)
Other	(83)	(0)	(772)
Total	<u>(19,808)</u>	<u>(18,659)</u>	<u>(184,449)</u>
Net deferred tax assets (liabilities)	<u>¥ (1,532)</u>	<u>¥ 1,100</u>	<u>\$ (14,265)</u>

The reconciliation of the statutory tax rate to the effective income tax rate for the years ended March 31, 2005 and 2004 is not provided, as the difference in rates is less than 5% of the statutory tax rate.

13. Leases

(1) Information on finance lease contracts without an ownership transfer for the years ended March 31, 2005 and 2004 was as follows:

(a) Acquisition cost, accumulated depreciation, net book value, Lease expenses, depreciation expenses, and interest expense on the leased assets (assuming capitalization of finance leases) were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Acquisition cost	¥ 6,020	¥ 6,525	\$ 56,057
Accumulated depreciation	(3,155)	(2,940)	(29,378)
Net book value	<u>¥ 2,864</u>	<u>¥ 3,585</u>	<u>\$ 26,669</u>
Lease expenses	<u>¥ 1,444</u>	<u>¥ 1,325</u>	<u>\$ 13,446</u>
Depreciation expenses	<u>¥ 1,279</u>	<u>¥ 1,174</u>	<u>\$ 11,909</u>
Interest expenses	<u>¥ 173</u>	<u>¥ 164</u>	<u>\$ 1,610</u>

Depreciation is based on the straight-line method over the lease term of the leased assets. Interest expenses are determined by the allocation of the portion of the total lease payment that exceeds the acquisition cost of leased assets, using the interest method.

(b) The amount of future lease payments at March 31, 2005 and 2004, which excludes the interest portion, were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Future lease payments:			
Due within one year	¥ 1,120	¥ 1,204	\$ 10,429
Due in over one year	1,874	2,504	17,450
Total	<u>¥ 2,994</u>	<u>¥ 3,709</u>	<u>\$ 27,879</u>

(2) The amount of future lease payments at March 31, 2005 and 2004 were on operating lease contracts as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Future lease payments:			
Due within one year	¥ 0	¥ 0	\$ 0
Due in over one year	0	0	0
Total	<u>¥ 0</u>	<u>¥ 1</u>	<u>\$ 0</u>

14. Derivative Financial Instruments

(1) Derivative financial instruments used by the Bank

The Bank enters into futures and options on interest rates, currencies, stocks and bonds, and interest rate swaps and currency swaps.

The Bank enters into these derivative transactions in order to manage and hedge the risks associated with interest rate fluctuations and exposure to changes in the market value of assets and liabilities held by the Bank. In addition, the Bank enters into derivative transactions for trading purposes, within the position and loss limits set up by the Bank.

Other companies in the Group do not enter into derivative transactions.

(2) Risks on derivative transactions

The major risks associated with derivative transactions, which have the potential to materially impact the Bank's financial condition, are market risk and credit risk.

Market risk is related to the increase and decrease in the market value of the positions held by the Bank due to changes in the market price and interest rates of the underlying assets. Market risk is also subject to changes in liquidity and the volatility of the markets. Credit risk refers to possible losses on the positions held by the Bank, which result from a counterparty's failure to perform according to the terms and conditions of the contract.

The Bank mainly applies a quantitative measurement method in order to capture market risk. The Bank monitors the outstanding balance and profit and loss for each type of transaction on a daily basis. In addition, the Bank applies a "Value-at-Risk" measurement method to transactions for which it is considered necessary to apply a more sophisticated method. The Bank manages credit risk by establishing credit limits for counterparties. Reviews of the adequacy of established credit lines are made on a regular basis and as deemed necessary.

The credit risk amounts calculated based on the capital adequacy rules as of March 31, 2005 and 2004 was ¥6,427 million (\$59,847 thousand) and ¥11,577 million, respectively.

(3) Risk management system of the Bank

The Bank exercises and controls the derivative transactions using limits including position limits, credit limits for each counterparty and stop loss limits in accordance with the Bank's policy on derivative transactions. Risks quantified are reported to the department and the director responsible for monitoring the transactions and the board of directors.

The front office function and the back office function are segregated. The middle office is responsible for risk management and monitors front and back offices' compliance with regulations and internal rules.

Contract amounts or notional principal amounts of derivative financial instruments disclosed represent nominal contract amounts or the notional principal amounts set up for the calculation of the settlement amounts. Generally, they do not represent the amounts for which the actual assets are exchanged. These amounts do not represent, by themselves, the volume of market risk and credit risk related to the underlying derivative financial instruments.

(4) Market value of derivative financial instruments

(a) Interest Rate Related Transactions

		Millions of yen			
		2005			
		Contractual value or notional principal amount	Including Over one year	Market value	Unrealized Profit/(Loss)
Over-the-counter					
Interest rate swaps					
	Receipts fixed-payments floating	¥ 2,000	¥ -	¥ 26	¥ 26
	Receipts floating-payments fixed	2,000	-	(22)	(22)
Total				¥ 3	¥ 3

		Millions of yen			
		2004			
		Contractual value or notional principal amount	Including Over one year	Market value	Unrealized Profit/(Loss)
Over-the-counter					
Interest rate swaps					
	Receipts fixed-payments floating	¥ 2,000	¥ 2,000	¥ 57	¥ 57
	Receipts floating-payments fixed	2,697	2,000	(62)	(62)
Total				¥ (5)	¥ (5)

		Thousands of U.S. dollars			
		2005			
		Contractual value or notional principal amount	Including Over one year	Market value	Unrealized Profit/(Loss)
Over-the-counter					
Interest rate swaps					
	Receipts fixed-payments floating	\$ 18,623	\$ -	\$ 242	\$ 242
	Receipts floating-payments fixed	18,623	-	(204)	(204)
Total				\$ 27	\$ 27

Notes: 1. Market values of exchange-traded instruments are based on closing prices of the Tokyo International Financial Futures Exchange and others.

Market values of over-the-counter transactions are based on the discounted present values or the option pricing calculation model, etc.

2. The balances as of March 31, 2005 and 2004 disclosed above exclude derivatives accounted for as hedges. The derivatives disclosed are valued at market value on the balance sheet with resulting gains and losses taken to the statement of income.

(b) Foreign exchange related transactions

Balance as of March 31, 2005 and 2004

	Millions of yen			
	2005			
	Notional Principal Amount	Including Over one year	Market value	Unrealized Profit/(Loss)
Over-the-counter currency swaps	¥ 84,898	¥ 39,158	¥ (8)	¥ (8)
Over-the-counter Foreign exchange forward contracts				
Sales	2,206	-	(30)	(30)
Purchase	831	-	34	34
Total			¥ (5)	¥ (5)

	Millions of yen			
	2004			
	Notional Principal Amount	Including Over one year	Market value	Unrealized Profit/(Loss)
Over-the-counter currency swaps	¥ 80,459	¥ 46,859	¥ (56)	¥ (56)
Over-the-counter Foreign exchange forward contracts				
Sales	2,219	-	127	127
Purchase	1,257	-	(15)	(15)
Total			¥ 55	¥ 55

	Thousands of U.S. dollars			
	2005			
	Notional Principal amount	Including Over one year	Market Value	Unrealized Profit/(Loss)
Over-the-counter currency swaps	\$ 790,557	\$ 364,633	\$ (74)	\$ (74)
Over-the-counter Foreign exchange forward contracts				
Sales	20,541	-	(279)	(279)
Purchase	7,738	-	316	316
Total			\$ (46)	\$ (46)

Notes: 1. Market values are based on the discounted present values and market prices prevailing as of the year-end date.

2. Balances as of March 31, 2005 and 2004 are valued at market value on the balance sheet with resulting gains and losses taken to the statement of income. The balance disclosed above exclude derivatives accounted for as hedges.

15. Appropriation of retained earnings

The annual shareholders' meeting, which was held on June 28, 2005, approved the following appropriations of retained earnings for the year ended March 31, 2005:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Cash dividends (¥3.00 per share)	¥ 728	¥ 742	\$ 6,779
Bonuses to directors and corporate Auditors	44	47	409
Transfer to voluntary reserve	4,000	2,010	37,247

16. Segment information

(1) Segment information by Type of Business

In addition to the banking business, the Group is also engaged in the credit card business, credit guarantee business and other businesses. Such segment information has not been provided, as the percentage of those activities is insignificant to the Group.

(2) Segment information by Geographic Area

All of the Group's entities or branches are in Japan.

(3) Recurring income from international operations

	Millions of yen
	2004
Recurring income from international operations	¥ 6,958
Total operating income	68,214
International Operations' Ratio	10.2%

Recurring income from internal operations for the year ended March 31, 2005 is not provided, as it is less than 10% of total operating income.

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors of
The Higo Bank, Ltd.

We have audited the accompanying consolidated balance sheets of The Higo Bank, Ltd. and its consolidated subsidiaries (the “Group”) as of March 31, 2005 and 2004, and the related consolidated statements of income, shareholders’ equity and cash flows for the years then ended, all expressed in Japanese Yen. These consolidated financial statements are the responsibility of the Bank’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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated 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 the Group as of March 31, 2005 and 2004, 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.

The amounts expressed in U.S. dollars, provided solely for the convenience of the reader, have been translated on the basis set forth in Note 3 to the accompanying consolidated financial statements.



ChuoAoyama PricewaterhouseCoopers
Tokyo, Japan
June 28, 2005



1, Renpeicho, Kumamoto 860-8615, Japan

Phone: (096) 325-2111

<http://www.higobank.co.jp/>