FINANCIAL REVIEW

1. SALES AND EARNINGS

General Conditions

During the year ended March 31, 2005, although the Japanese economy initially maintained an upward trend, the tempo of economic growth slackened after the summer, reflecting slower growth of exports and higher prices of oil and raw materials. Overseas, while the U.S. economy expanded smoothly supported by active housing investment and private capital expenditures, the EU economy decelerated gradually, affected by the stronger Euro.

While the domestic market for Internal Combustion Engine and Machinery was sluggish, overseas markets, especially the small-sized tractors market in the United States, were brisk due to active private consumption and the high level of housing starts. As for the public works related markets, the total amount of orders remained stagnant as ever due to the continuously declining public works spending. The domestic demand for ductile iron pipe, which is one of the mainstays in the public works related products, had no signs of an increase although the pace of decrease declined. Environmental Engineering also faced a difficult operating environment in terms of receiving orders from public agencies.

Sales

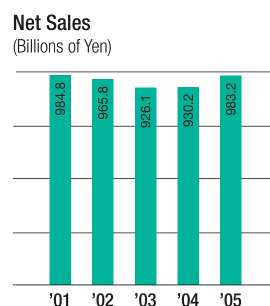
Under such conditions, net sales of the Company during the year under review were ¥983.2 billion ($9,189 million), a 5.7% increase from the prior year, and domestic sales were ¥637.9 billion ($5,962 million), a 0.8% decrease from the prior year. Although the negative impact from the business transfer of building materials operations carried out in December 2003 (a decrease of ¥28.5 billion) was largely offset by a favorable increase of sales in other segments, the compensation was not sufficient and domestic sales slightly declined from the prior year. Overseas sales were ¥345.3 billion ($3,227 million), a 20.4% increase from the prior year. This increase was mainly due to the continuing growth in sales of tractors in North America where a very promising new product was introduced, and brisk sales of construction machinery and engines principally in the United States and European markets. As a result, overseas sales accounted for 35.1% of net sales, 4.3 percentage points higher than in the prior year.

Sales in Internal Combustion Engine and Machinery were ¥582.7 billion ($5,445 million), 16.2% higher than in the prior year, comprising 59.3% of consolidated net sales. Sales in Pipes, Valves, and Industrial Castings were ¥170.6 billion ($1,595 million), 2.6% lower than in the prior year, comprising 17.3% of consolidated net sales. Sales in Environmental Engineering were ¥117.6 billion ($1,099 million), 1.7% higher than in the prior year, comprising 12.0% of consolidated net sales. Other sales were ¥112.3 billion ($1,050 million), 18.5% lower than in the prior year, comprising 11.4% of consolidated net sales.

Operating Income

Operating income increased 322.4% from the prior year, to ¥92.3 billion ($863 million). In spite of the appreciation of the yen and higher prices of raw materials, a significant decrease in pension costs (a decrease of ¥44.9 billion), increased sales centering on the Internal Combustion Engine and Machinery segment, and the reduction of costs and spending control in public works related business contributed to an increase in operating income. In the prior year, the Company recognized a large amount of unrecognized actuarial loss that resulted from unfavorable stock market conditions in Japan in the past few years before the prior year and a reduction of the discount rate used in pension plans in the year before the prior year. The Company also had expenses related to reorganization of the building materials business in the prior year (¥4.8 billion). In contrast, the Company had non-recurring operating income in connection with the business transfer of two subsidiaries in the year under review. As a result of these factors, operating income for the year under review expanded significantly.

Operating income or loss in each industry segment (before elimination of intersegment profits and corporate expenses) was as follows: Internal Combustion Engine and Machinery, operating income of ¥79.2 billion ($740 million), a 46.5% increase; Pipes, Valves, and Industrial Castings, operating income of ¥11.5 billion ($107 million), as compared to an operating loss of ¥5.7 billion in the prior year; Environmental Engineering, operating income of ¥5.7 billion ($53 million), a 4,262.6% increase; and Other, operating income of ¥9.4 billion ($88 million), as compared to an operating loss of ¥7.8 billion in the prior year.



References to "the Company" mentioned on pages 12 to 23 refer to Kubota Corporation and subsidiaries.

Profitability in Internal Combustion Engine and Machinery benefited from the brisk sales of lawn mowers as well as compact and utility tractors in the U.S. market, due to steady private consumption and strong housing construction, which was similar with that of the prior year. In addition to the above factors, the decrease in pension costs contributed to an increase in operating income in this segment. Profitability in Pipes, Valves, and Industrial Castings benefited from rigorous cost controls and the increased efficiency of the manufacturing process as well as the decrease in pension costs. In Environmental Engineering, profitability improved due to the decrease in pension costs.

Cost of Sales

The cost of sales increased 1.7% from the prior year, to ¥713.3 billion ($6,666 million). The cost of sales as a percentage of net sales decreased 2.9 percentage points, to 72.5%. The decrease in the ratio was attributable to the substantial decrease in pension costs.

SG&A Expenses

Selling, general, and administrative (SG&A) expenses decreased 9.0% from the prior year, to ¥181.7 billion ($1,698 million). The ratio of SG&A expenses to net sales decreased 3.0 percentage points, to 18.5%. The decrease in pension costs as well as the Company's efforts for spending control in all aspects of business operations contributed to the decrease in the ratio.

Loss (Gain) from Disposal and Impairment of Businesses and Fixed Assets

Gain from disposal and impairment of business and fixed assets was ¥4.1 billion ($38 million), as compared to a loss of ¥6.9 billion in the prior year. The gains in connection with the business transfer of two subsidiaries in the year under review contributed to this improvement. The Company recognized a gain of ¥5.6 billion in connection with the sale of a subsidiary that operated a golf course. Also, the Company had a gain as a result of the sale of Firstserver, Inc., one of the Company's subsidiaries that operated a rental computer server business.

Other Income (Expenses)

Other income (expenses), net, was income of ¥69.3 billion ($647 million), an increase of ¥64.0 billion from the prior year. The increase is largely due to ¥58.6 billion from a government subsidy, which is the difference in the substitutional portion of accumulated benefit obligation settled and related plan assets transferred to the Japanese government. In addition, the foreign exchange gain improved ¥5.1 billion ($48 million) and interest and dividend income increased by ¥2.2 billion ($21 million).

Income before Income Taxes, Minority Interests in Earnings of Subsidiaries, and Equity in Net Income of Affiliated Companies

Due to the factors described above, income before income taxes, minority interests in earnings of subsidiaries, and equity in net income of affiliated companies increased 496.2%, to ¥161.6 billion ($1,510 million).

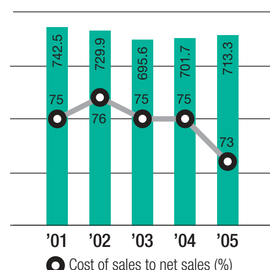
Income Taxes

Income taxes increased 210.5% from the prior year, to ¥42.5 billion ($398 million). The effective tax rate decreased 24.3 percentage points, to 26.3%. The primary reason for the decrease in the effective tax rate was due to the deductibility of the historical impairment losses and net operating losses related to the sale and dissolution of the subsidiaries. Related deferred tax assets were fully reserved prior to the sale and dissolution of the subsidiaries. Income tax—current was ¥28.9 billion ($270 million), a decrease of ¥0.3 billion ($3 million), and income tax—deferred (expense) was ¥13.6 billion ($127 million) as compared to income tax—deferred (benefit) of ¥15.6 billion in the prior year.

Minority Interests in Earnings of Subsidiaries and Equity in Net Income of Affiliated Companies

Minority interests in earnings of subsidiaries increased ¥1.0 billion, to ¥3.4 billion ($32 million). Equity in net income of affiliated companies increased ¥1.5 billion from the prior year, to ¥2.3 billion ($22 million). Increased profit of joint venture Kubota Matsushitadenko Exterior Works, Ltd., contributed to increase equity in net income of affiliated companies.

Cost of Sales
(Billions of Yen)



Net Income

Due to the factors described previously, net income was ¥117.9 billion ($1,102 million), compared with ¥11.7 billion in the prior year. Return on shareholders' equity improved 23.7 percentage points, to 27.0%, from the prior year.

Income per ADS

Basic net income per ADS (five common shares) was ¥446 ($4.17), as compared to ¥44 in the prior year. The number of shares of treasury stock held by the Company was 40.4 million as of March 31, 2005, and these shares were excluded from the calculation of net income per ADS.

Dividends

The Company's basic policy for the allocation of profit is to maintain or raise dividends. To this end, the Company determines the most appropriate use of retained earnings by considering requirements of maintaining stable current business operations as well as the future business environment. A year-end cash dividend per ADS at the rate of ¥25 ($0.23) was approved at the general meeting of shareholders, held on June 24, 2005. The Company also paid a ¥15 ($0.14) per ADS interim dividend to each shareholder.

Comprehensive Income

Comprehensive income was ¥119.3 billion ($1,115 million), a ¥33.5 billion improvement from the prior year. The increase resulted from the expansion of net income, to ¥117.9 billion ($1,102 million). However, the increase was partially offset by a decrease in unrecognized gains on securities and adjustment to reduce the minimum pension liability.

2. FINANCE AND LIQUIDITY MANAGEMENT

Finance and Liquidity Management

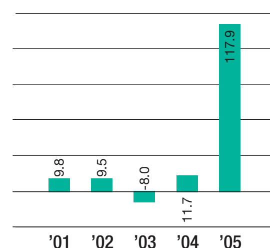
The Company's financial policy is to ensure adequate financing and liquidity for its operations and to maintain the strength of its balance sheet. Through cash and cash equivalents, other current assets, cash flows provided by operating activities, and borrowing, the Company is in a position to fully finance the expansion of its business, R&D, and capital expenditures for current and future business projects. The specific methods of obtaining financing available to the Company are borrowing from financial institutions, the securitization of trade notes and accounts receivables, establishing committed lines of credit, and the issuance of bonds and commercial paper in the capital markets.

Annual interest rates of short-term borrowings ranged primarily from 0.02% to 2.70% at March 31, 2005. The weighted average interest rate on such short-term borrowings was 1.7%. As for long-term debt, interest rates were primarily fixed, and the weighted average interest rate on such long-term debt at March 31, 2005, was 1.6%.

In North America, the Company maintains an accounts receivables securitization program of trade receivables and finance receivables. The Company may sell both trade and finance receivables through independent revolving-period securitization trusts. Trade receivables sold under the securitization program and finance receivables sold under the securitization program are excluded from receivables in the accompanying consolidated balance sheets. In the year under review, a subsidiary in the United States decided to obtain borrowings using finance receivables as collateral instead of selling finance receivables under the securitization program. The Company sold trade receivables totaling ¥84.5 billion ($789.8 million) during the year ended March 31, 2005. The Company also sold finance receivables totaling ¥5.8 billion ($53.8 million) during the year ended March 31, 2005.

Regarding the lines of credit, the Company has established committed lines of credit totaling ¥30.0 billion ($280 million) with some Japanese banks. However, the Company currently does not use these lines as it is focused on the reduction of interest-bearing debt. In the United States, Europe, and Asia, the Company maintains adequate uncommitted lines of credit with financial institutions. The Company also maintains a commercial paper program allowing for the issuance of commercial paper of up to ¥100.0 billion ($935 million). Total commercial paper at the end of March 2005 amounted to ¥6.0 billion ($56.1 million).

The Company utilizes Group financing. With Group financing, the Company is centralizing and pursuing the efficiency of cash management



domestically through the Kubota Cash Management System, under which the excess or shortage of cash at most of its subsidiaries in Japan is invested or funded, as necessary. Considering the financing resources mentioned above, the Company believes it will have no difficulty in securing adequate financing resources to fund its operations and investment.

To maintain the strength of its balance sheet and help secure adequate funding resources, the Company is reducing its interest-bearing debt focusing on debt excluding the effects of reduced cash flow caused by its sales financing programs. The Company is providing comprehensive sales financing to support machinery sales in the United States and Japan. The Company believes an increase of debt related to sales financing programs is a result of business expansion and it is not appropriate to target reduction of the related debt; thus, the additional debt carried on its books to fund this program is excluded when determining the target. At the end of March 2005, the amount of interest-bearing debt excluding the effects of reduced cash flow caused by its sales financing program was ¥158.2 billion ($1,479 million), and the amount of total interest-bearing debt was ¥304.2 billion ($2,843 million). Of the ¥304.2 billion, ¥275.6 billion was borrowings from financial institutions, and the remaining ¥28.6 billion consisted of corporate bonds.

The amount of working capital decreased ¥28.4 billion, to ¥171.3 billion ($1,601 million), from the prior year-end. Additionally, the ratio of current assets to current liabilities decreased 14.2 percentage points, to 134.0%. The primary reason for this decrease was that a large portion of long-term debt moved from long-term liabilities to the current portion of long-term debt. There is some seasonality to the Company's liquidity and capital resources because a high percentage of the notes and accounts receivable from local governments is collected during April through June every year.

All things considered, the Company believes that it can support its current and anticipated capital and operating expenditures for the foreseeable future. The currencies in which the Company has its debt are mainly Japanese yen and U.S. dollars. There are no restrictions regarding the manner in which the funds may be used.

Ratings

The Company has obtained a credit rating from Rating and Investment Information, Inc. (R&I), a rating agency in Japan, to facilitate access to funds from the capital market in Japan. The Company's current rating is A+ as of March 2005 and its outlook is stable. The Company's favorable credit rating provides it access to capital markets and investors.

■ ASSETS, LIABILITIES, AND SHAREHOLDERS' EQUITY

The Company restated its 2004 consolidated balance sheet as a result of reconsideration of its classification of retail finance receivables.

Retail finance receivables were previously classified as current assets in the consolidated balance sheet.

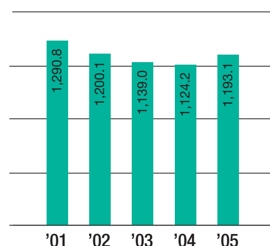
The Company reconsidered its classification of these receivables and restated its 2004 consolidated balance sheet considering Chapter 3, Section A, "Current Assets and Current Liabilities" of Accounting Research Bulletins No. 43, "Restatement and Revision of Accounting Research Bulletins" to reflect amounts expected to be collected one year after the balance sheet date as long-term assets.

See Note 17 to the Consolidated Financial Statements.

Assets

Total assets at the end of March 2005 amounted to ¥1,193.1 billion ($11,150 million), an increase of ¥68.8 billion (6.1%) from the end of the prior year. Current assets were ¥675.4 billion ($6,312 million), an increase of ¥60.9 billion from the end of the prior year. Current assets increased due mainly to increases in notes and accounts receivable, short-term finance receivables, and inventories. The increases of notes and accounts receivable and inventories are mainly due to newly consolidated subsidiaries and a sales increase in overseas markets. In spite of the increase of inventories, inventory turnover improved 0.3 point, to 6.6 times. In addition to the increase in current assets, the sharp increase in long-term finance receivables resulted in an increase in investments and long-term finance receivables. Substantial increases in short- and long-term finance receivables originated from a rapid expansion of business as

Total Assets
(Billions of Yen)



well as a reduction of sales of finance receivables in North America. On the other hand, property, plant, and equipment and other assets decreased. Property, plant, and equipment slightly decreased ¥3.0 billion, to ¥219.8 billion ($2,054 million). The decrease in other assets was owing principally to a decrease in deferred tax assets, which is in connection with the transfer of the substitutional portion of the benefit obligation and related plan assets to the Japanese government.

Liabilities

Total liabilities amounted to ¥690.5 billion ($6,453 million), a decrease of ¥27.0 billion from the prior year-end. Current liabilities increased, reflecting increases in short-term borrowings, current portion of long-term debt, and notes and accounts payable. The increase in short-term borrowings is corresponding to the increase in short-term finance receivables. The increase in notes and accounts payable was due mainly to newly consolidated subsidiaries and the net sales increase.

In contrast, long-term liabilities decreased due mainly to the decrease in long-term debt and the sharp decline in accrued retirement and pension costs. A large portion of long-term debt moved to current liabilities and accrued retirement and pension costs decreased because of the transfer of the substitutional portion of the benefit obligation and related plan assets to the Japanese government.

Minority Interests

Minority interests increased ¥5.9 billion, to ¥21.6 billion ($202 million), due to an increase in the number of subsidiaries that are not 100% owned.

Shareholders' Equity

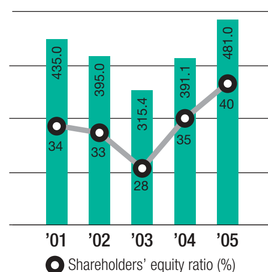
Total shareholders' equity increased ¥89.9 billion, to ¥481.0 billion ($4,495 million). Thanks to the increase in net income, shareholders' equity increased significantly, and the shareholders' equity ratio* exceeded 40%, which is a target at March 31, 2006, in the Medium-Term Management Strategy.

In order to reduce the number of outstanding shares and create more value for shareholders, the Company commenced a program for the purchase of shares of treasury stock in December 2001. During the year under review, the Company retired 69.0 million shares of treasury stock in June 2004 and then additionally purchased 39.8 million shares of treasury stock. As a result, treasury stock at the end of March 2005 was 40.4 million shares, equivalent to ¥21.6 billion that was deducted from shareholders' equity. For these purchases, the Company used net cash provided by operating activities. Next fiscal year, the Company plans to continue the purchase of shares of treasury stock. The debt-to-equity ratio** was 63.2%, 5.0 percentage points lower than at the prior year-end, due to the growth in shareholders' equity that resulted from increased net income.

* Shareholders' equity ratio = shareholders' equity / total assets

** Debt-to-equity ratio = interest-bearing debt / shareholders' equity

Total Shareholders' Equity
(Billions of Yen)



Contractual Obligations

The following summarizes contractual obligations at March 31, 2005.

	Millions of Yen				
		Payments Due by Period			
Year Ended March 31, 2005	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Short-term borrowings	¥119,802	¥119,802	¥ —	¥ —	¥ —
Capital lease obligations	4,841	2,379	2,228	185	49
Long-term debt	179,524	64,498	70,577	37,909	6,540
Deposits from customers	3,322	3,322	—	—	—
Operating lease obligations	1,478	334	513	245	386
Commitments for capital expenditures	1,155	1,155	—	—	—
Expected pension contribution	14,105	14,105	—	—	—
Total	¥324,227	¥205,595	¥73,318	¥38,339	¥6,975

	Thousands of U.S. Dollars				
		Payments Due by Period			
Year Ended March 31, 2005	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Short-term borrowings	$1,119,645	$1,119,645	$ —	$ —	$ —
Capital lease obligations	45,243	22,234	20,822	1,729	458
Long-term debt	1,677,794	602,785	659,598	354,290	61,121
Deposits from customers	31,047	31,047	—	—	—
Operating lease obligations	13,813	3,121	4,795	2,289	3,608
Commitments for capital expenditures	10,794	10,794	—	—	—
Expected pension contribution	131,822	131,822	—	—	—
Total	$3,030,158	$1,921,448	$685,215	$358,308	$65,187

3. CASH FLOWS

The Company reclassified certain amounts between operating and investing activities in its consolidated statements of cash flows as a result of reconsideration of its classification of the cash flow activity related to the retail finance receivables. Activity related to the retail finance receivables on the consolidated statements of cash flows was previously classified into operating activities as "(Increase) decrease in notes and accounts receivable." The Company reconsidered its classification of the cash flow activity related to loans provided by finance subsidiaries to customers of independent dealers of the Company's products and currently classifies such activity into investing activities pursuant to the FASB No. 95, "Statement of Cash Flows," and in consideration of such industry standards as "Increase in finance receivables," "Collection of finance receivables," and "Sales of finance receivables" in the consolidated statements of cash flows. See Note 1 to the consolidated financial statements.

Net cash provided by operating activities during the year under review was ¥66.9 billion ($625 million), a decrease of ¥42.7 billion from the prior year. The primary reason for this decrease was fluctuations in notes and accounts receivable. The sales amount of notes and accounts receivable in North America in the prior year was significantly larger, and it resulted in the substantial decrease in notes and accounts receivable in the prior year. In contrast, notes and accounts receivables increased in the year under review, resulting in the decrease in net cash provided by operating activities.

Net cash used in investing activities was ¥78.2 billion ($731 million), an increase of ¥37.9 billion from the prior year. The increase is primarily attributable to a reduction in sales of finance receivables as the Company obtained funding through increased borrowings.

Net cash provided by financing activities was ¥4.5 billion ($42 million), as compared to ¥55.1 billion of net cash used in financing activities in the prior year. The fluctuation is primarily due to increased borrowings and a reduction in debt repayment.

As a result, including the effect of exchange rate changes on cash and cash equivalents, cash and cash equivalents at the end of March 2005 was ¥74.6 billion ($697 million), a decrease of ¥6.7 billion from the prior year.

4. CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States ("US GAAP"). The preparation of the consolidated financial statements requires management to make estimates and assumptions on the selection and application of significant accounting policies. The Company reviews these estimates and assumptions periodically. Actual results may differ from estimated results. The following critical accounting policies that affect financial conditions and operations require management to make significant estimates and assumptions:

Inventory Valuation

Completed real estate projects are stated at the lower of acquisition cost or fair value, less estimated costs to sell. The fair values of those assets are estimated based on the appraised values in the market. Land to be developed and projects under development are carried at cost unless those assets are impaired. If carrying amounts of those assets exceed the undiscounted future cash flows expected to be realized from them, those assets are considered impaired and an impairment loss is measured based on the amount by which the carrying value exceeds the fair value of those assets. If the market conditions and demand in the housing business are less favorable than management's projection, additional write-downs may be required.

Impairment of Investments

The Company classifies all its debt securities and marketable equity securities as available for sale. When a decline in the value of a marketable security is deemed to be other than temporary, the Company recognizes an impairment loss to the extent of the decline. In determining if and when such a decline in value is other than temporary, the Company evaluates market conditions, trends of earnings, the extent to which cost exceeds market value, the duration of market declines, the ability and intent to hold the marketable securities, and other key measures. If equity markets decline or operating results of the issuer of the security become worse, additional impairment losses may be required in the future.

Allowance for Doubtful Receivables

The Company evaluates the collectibility of the notes and accounts receivable, with the estimate based on various judgments, including the customers' financial conditions, historical experience, and the current economic circumstances. If the customers' financial conditions or current economic circumstances become worse, additional allowances may be required in the future.

Deferred Tax Assets

The Company recognizes deferred tax assets with a valuation allowance to adjust the carrying amount when it is more likely than not that the deferred tax assets will not be realized. The valuation of deferred tax assets principally depends on the estimation of future taxable income and tax planning strategies. If future taxable income is lower than expected due to a change in economic circumstances and poor operating results, significant adjustments to deferred tax assets may be required.

Impairment of Long-Lived Assets

When events and circumstances indicate that the carrying amount of long-lived assets to be held and used may not be recoverable and the carrying amounts of those assets exceed the undiscounted future cash flows, an impairment loss is recognized based on the amount by which the carrying value exceeds the fair value of the long-lived assets. Fair value is determined primarily using anticipated future cash flows discounted at a rate commensurate with the risk involved. If estimates of future cash flows fall below management's projection due to an unexpected change in economic circumstances, additional impairment may be required.

Retirement and Pension Plans

Benefit obligations and periodic benefit cost are valued based on assumptions used by actuaries in calculating such amounts. These assumptions include the discount rate, retirement rate, rate of compensation increase, mortality rate, expected rate of return on plan assets, and other factors. These assumptions are based upon current statistical data and are reviewed every fiscal year. Differences in actual experience or changes in assumptions may affect the benefit obligations and future periodic benefit cost.

The Company recognizes actuarial gains and losses in excess of 20% of the larger of the projected benefit obligations or plan assets in the year following the year in which such gains and losses were incurred, and amortizes actuarial gains and losses between 10% and 20% over the participants' remaining service period (approximately 15 years). Significant unrecognized actuarial gains or losses may have a material effect on periodic benefit cost in the next fiscal year.

To determine the discount rate, the Company considers current market interest rates. To reflect the declining current market interest rates, the Company reduced the discount rate from 3.0% to 2.5% as of March 31, 2003. In fiscal 2003, this change increased the projected benefit obligations by approximately ¥21.9 billion. A further decrease of 50 basis points in the discount rate would increase the benefit obligations as of March 31, 2005, by approximately ¥9.2 billion ($86 million).

To determine the expected rate of return on plan assets, the Company considers actual returns in the past 5 to 10 years and the current and expected components of plan assets, and anticipated market trends. Plan assets are managed by asset management companies and trust banks, and are invested primarily in fixed income and equity securities of Japanese and foreign issuers. The Company assumed that the long-term rate of return on plan assets was 3.5% in fiscal 2004 and fiscal 2005. The Company anticipated that investment managers would continue to generate long-term returns of at least 3.5%, based on an asset allocation assumption of 45% on fixed income securities, with an expected rate of return of 1.0%, and 55% on equity securities, with an expected rate of return of 5.5%. In fiscal 2005, the Company reviewed the components of plan assets and adopted an asset allocation of 55% on fixed income securities and 45% on equity securities to secure stabler returns. The Company's management believes that 3.0% is a reasonable long-term rate of return despite an actual return on plan assets in the past 10 years of 2.3%, as significant losses on plan assets were incurred from fiscal 2001 to fiscal 2003, caused by the market downturn. A decrease of 50 basis points in the expected rate of return on plan assets would result in an increase of periodic benefit costs in fiscal 2006 of approximately ¥0.4 billion ($4 million).

Based on a law issued by the Japanese government in June 2001, the Company made applications for an exemption from the obligation to pay benefits for future employee service related to the substitutional portion of a contributory defined benefit pension plan and received approval from the Japanese Ministry of Health, Labour and Welfare on January 30, 2003. After the approval, the Company made applications for an exemption from the obligation to pay benefits for past employee service related to the substitutional portion and received approval from the Japanese Ministry of Health, Labour and Welfare on September 1, 2004. Based on the approval, the Company transferred the benefit obligation and the related government-specified portion of the plan assets of the contributory defined benefit pension plan to the government on January 31, 2005.

In accordance with EITF No. 03-2, "Accounting for the Transfer to the Japanese Government of the Substitutional Portion of Employee Pension Fund Liabilities," the Company recognized the difference of ¥58.6 billion ($548 million) between the substitutional portion of accumulated benefit obligation settled and the related plan assets transferred to the Japanese government as a government subsidy in Other income (expenses) in the 2005 consolidated statement of income. The Company also recognized derecognition of previously accrued salary progression of ¥11.1 billion ($104 million) and a settlement loss for the proportionate amount of the net unrecognized loss of ¥13.4 billion ($125 million). The net amount of ¥2.3 billion ($21 million) of derecognition of previously accrued salary progression and the settlement loss was allocated to cost of sales of ¥1.5 billion ($14 million) and selling, general, and administrative expenses of ¥0.7 billion ($7 million).

The Company's senior management and the Board of Corporate Auditors had proactive discussions about these critical accounting policies, and they agreed that estimates and assumptions were appropriate in light of the current and expected market conditions, the Company's businesses, and numerous other factors.

5. BUSINESS RISKS

Declines in economic conditions in Kubota's major markets, including private-sector capital expenditure, construction investment, and domestic public investment, may adversely impact the results of operations of the Company.

Industrial and capital goods make up a substantial portion of the Company's products. Accordingly, sales of the Company may be sensitive to declines in general economic conditions, including private-sector capital expenditure, construction investment, and domestic public investment. In addition, governmental agricultural policies, such as a reduction in rice acreage or change in agricultural basic law, may affect domestic sales of agriculture-related products. In overseas markets, especially those of North America and Europe, sales of the Company's products, such as utility/compact tractors, may also be adversely affected by declines in general economic conditions, including private consumption and residential construction investment in those regions.

Fluctuations of foreign exchange rates, including a stronger yen, may reduce net sales and adversely affect the results of operations of the Company.

The Company has overseas sales and manufacturing subsidiaries. The financial results of each overseas subsidiary are consolidated into the results of the parent company after translation into Japanese yen. In addition, the transactions between the parent company and overseas subsidiaries or customers are generally denominated in the local currencies. The payments received in local currencies on such transactions are converted to Japanese yen. As a result, fluctuations in foreign exchange rates will affect the consolidated financial results.

The Company is subject to the risks of international operations.

In some businesses of the Company, substantial overseas operations are conducted. Accordingly, the Company is subject to a number of risks inherent in doing business in those markets. Such risks may affect sales

and profitability of the Company or they may hinder the growth of the Company in specific countries. The following risks are important concerns for the Company:

- Unexpected changes in international, or each country's, tax regulations
- Unexpected legal or regulatory changes in each country
- Difficulties in retaining qualified personnel
- Underqualified technological skills or instability between management and employee unions in developing countries
- Political instability in those countries

The major markets with the above risks are markets in the United States, the EU, and Asian countries.

Among the United States, the EU, and Asian countries, which are major markets for the Company, risks in Asian countries seem to be relatively higher than those of other regions.

The Company utilizes estimations on some accounts in the consolidated financial statements, which may require additional accruals due to unanticipated changes in the basis of assumptions.

The Company appropriately records its employee benefit obligations, valuation of inventories, valuation allowances for deferred tax assets, probability of collection of notes and accounts receivable, and impairment losses on long-lived assets in the consolidated financial statements based on the information that it has available. However, these are based on various assumptions about future economic results. If actual results differ from any of these assumptions, unanticipated additional accruals may be required.

Strategic alliances, mergers, and acquisitions may not generate successful results as planned.

The Company expects to use strategic alliances, mergers, and acquisitions to seek further growth. The success of these activities depends on such factors as the Company's business environment, the ability of its business counterparts, and whether the Company and its counterparts share common goals. Therefore, if these activities are not successful and returns on related investments are lower than expected, the Company may lose competitiveness in relevant markets. Consequently, the Company's profitability may deteriorate.

The Company may not be able to successfully create new businesses or businesses complementary to the current ones.

As part of its structural renovation, the Company is attempting to cultivate new businesses or businesses that are complementary to the current ones. However, in those markets, there are numerous competitors, and competition will be very harsh. If the Company fails to develop the required personnel or abilities to produce and market appropriate products, subsequent impairment charges may be taken, or there may be a negative impact on the Company's financial position.

Impairment losses on investments in marketable securities may occur as a result of stock market fluctuations.

As of March 31, 2005, the Company owns securities with a fair value of approximately ¥135.5 billion. Most of these securities are equity securities, and, accordingly, depending on stock market fluctuations, unrealized and realized losses may occur.

In each of its businesses, Kubota is subject to intensifying competitive pressures. The Company must compete successfully to maintain sales and profits.

The Company is exposed to severe competition in each of its businesses. Unless the Company surpasses other companies in such areas as terms of trade, R&D, and quality, sales and/or net income may decrease in the future.

Damage by Natural Disasters

Japan is a country with frequent earthquakes. In case of a strong earthquake or related tidal wave, the Company may be affected in the operation of manufacturing products, logistics, sales activities, and may lose sales and profits depending on the severity of the earthquake or tidal wave. Japan also is hit by typhoons very frequently. In case major plants are struck by a large and powerful typhoon, the Company's operations may suffer great losses.

6. MARKET RISKS

Derivatives

To offset currency and interest rate fluctuation risks, the Company uses various types of derivatives, including foreign exchange forward contracts, currency swaps, and interest rate swaps. As a basic policy, the Company conducts its derivative transactions within the range of its outstanding credit and obligations, and the Company does not engage in speculative derivative transactions. The counterparties for the Company's derivative transactions are financial institutions with high creditworthiness; therefore, the Company does not anticipate any credit losses on such transactions. For more specific details, please refer to Note 12 to the consolidated financial statements.

Countermeasures for the Removal of Government Deposit Guarantees

Effective from April 2002 in Japan, limits were placed on government guarantees of certain short-term deposits held by financial institutions. As a countermeasure, the Company maintains its deposits with a diverse group of financial institutions with high credit ratings. In addition, the Company centralizes its risk management with financial institutions mainly through concentrating cash within the parent company.

7. RESEARCH AND DEVELOPMENT

R&D expenses were ¥22.0 billion ($205 million), a decrease of ¥1.3 billion from the prior year, and its ratio to net sales declined 0.27 percentage point, to 2.23%. R&D expenses were mainly spent on R&D activities of the Internal Combustion Engine and Machinery segment.

8. CAPITAL EXPENDITURES

Capital expenditures amounted to ¥26.1 billion ($244 million), a 22.0% increase from the prior year. The amount of depreciation expense was ¥25.5 billion ($238 million), ¥1.8 billion less than in the prior year. The funds for these capital expenditures were mainly provided by internal operations. The principal capital expenditures as of March 31, 2005, were related to improving information systems and increasing the efficiency of farm equipment production.

9. OUTLOOK FOR THE NEXT FISCAL YEAR

General Conditions

Although the Japanese economy is expected to break out of its stagnant condition, the prospects are still unpredictable considering current risks, including the potential for higher prices of raw materials and crude oil may have a negative impact on the world economy. All things considered, the Company expects the difficult economic conditions to persist.

Financial Outlook

Under such conditions, the Company formulated its "Medium-Term Management Strategy" (for the two years ending March 31, 2006) in order to further improve profitability and is engaged in a concerted effort to implement the strategy corporate-wide. The strategy consists of three principal concepts: "Reforming the business structure and profit structure," "Reforming operational systems," and "Strengthening the financial position." Building on the progress made in the first year of the Medium-Term Management Strategy, the Company will do its utmost to ensure that the strategy will be implemented with maximum effectiveness.

Looking ahead, the Company forecasts consolidated net sales for the year ending March 31, 2006, of ¥996.0 billion ($9,670 million), up ¥12.8 billion from the prior year. In the domestic market, the Company expects sales in the Internal Combustion Engine and Machinery and Pipes, Valves, and Industrial Castings segments to increase. On the other hand, sales in the Other segment are forecast to decrease. As a result, total domestic sales are expected to be almost the same amount as that of the year under review. As for overseas sales, sales expansion in the Internal Combustion Engine and Machinery segment will continue, and overall overseas sales are expected to increase steadily.

The Company forecasts operating income of ¥96.0 billion ($897 million), an increase of ¥3.7 billion from the year under review. Although the price increases in raw materials and the high appreciation of the yen will result in downward pressure on operating income, increases of overseas sales in the Internal Combustion Engine and Machinery and Pipes, Valves, and Industrial Castings segments, corporate-wide cost cuts, and a decrease in pension costs are expected to contribute to the increase in operating income.

The Company also expects income before income taxes, minority interests in earnings of subsidiaries, and equity in net income of affiliated companies for the next fiscal year to be ¥102.0 billion ($953 million), a sharp decrease of ¥59.6 billion from the year under review. The decrease is mainly due to the significant decrease in other income—net as a result of a government subsidy recorded in the year under review. Accordingly, net income is forecast to be ¥58.0 billion ($542 million), down ¥59.9 billion from the year under review. (These forecasts anticipate an exchange rate of ¥103=US$1.)

10. RECENT EVENT

On May 13, 2005, the Company resolved at the Board of Directors Meeting to retire 39.0 million shares of treasury stock on June 30, 2005.

Cautionary Statements with Respect to Forward-Looking Statements

This document may contain forward-looking statements that are based on management's expectations, estimates, projections, and assumptions. These statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. Therefore, actual future results may differ materially from what is forecast in forward-looking statements due to a variety of factors, including, without limitation, general economic conditions in the Company's markets, particularly government agricultural policies, levels of capital expenditures, both in public and private sectors, housing starts in Japan, foreign currency exchange rates, continued competitive pricing pressures in the marketplace, as well as the Company's ability to continue to gain acceptance of its products.

■ SEGMENT INFORMATION

The following segment information for the years ended March 31, 2005 and 2004, which is required under the regulations of the Securities and Exchange Law of Japan, is not consistent with accounting principles generally accepted in the United States of America.

In December 2003, the Company transferred the building materials business to one of its affiliated companies. Accordingly, the "Building Materials & Housing" segment was considered immaterial, and was included in the "Other" segment. The industry segment information for the year ended March 31, 2004 has been reclassified to conform with the industry segment information for the year ended March 31, 2005.

Industry Segments

	Millions of Yen						
Year Ended March 31, 2005	Internal Combustion Engine & Machinery	Pipes, Valves, & Industrial Castings	Environmental Engineering	Other	Total	Corporate & Eliminations	Consolidated
Net sales:							
Unaffiliated customers	**¥582,664**	**¥170,629**	**¥117,633**	**¥112,300**	**¥ 983,226**	**¥ —**	**¥ 983,226**
Intersegment	**88**	**8,237**	**249**	**14,956**	**23,530**	**(23,530)**	**—**
Total	**582,752**	**178,866**	**117,882**	**127,256**	**1,006,756**	**(23,530)**	**983,226**
Cost of sales and operating expenses	**503,596**	**167,391**	**112,167**	**117,848**	**901,002**	**(10,075)**	**890,927**
Operating income	**¥ 79,156**	**¥ 11,475**	**¥ 5,715**	**¥ 9,408**	**¥ 105,754**	**¥ (13,455)**	**¥ 92,299**
Identifiable assets at March 31, 2005	**¥614,123**	**¥190,669**	**¥105,890**	**¥100,874**	**¥1,011,556**	**¥181,500**	**¥1,193,056**
Depreciation	**14,154**	**6,368**	**930**	**1,678**	**23,130**	**2,338**	**25,468**
Capital expenditures	**17,482**	**1,823**	**358**	**1,388**	**21,051**	**5,046**	**26,097**

	Millions of Yen						
Year Ended March 31, 2004	Internal Combustion Engine & Machinery	Pipes, Valves, & Industrial Castings	Environmental Engineering	Other	Total	Corporate & Eliminations	Consolidated
Net sales:							
Unaffiliated customers	¥501,551	¥175,178	¥115,721	¥137,787	¥930,237	¥ —	¥ 930,237
Intersegment	32	6,923	696	16,581	24,232	(24,232)	—
Total	501,583	182,101	116,417	154,368	954,469	(24,232)	930,237
Cost of sales and operating expenses	447,559	187,783	116,286	162,180	913,808	(5,420)	908,388
Operating income (loss)	¥ 54,024	¥ (5,682)	¥ 131	¥ (7,812)	¥ 40,661	¥ (18,812)	¥ 21,849
Identifiable assets at March 31, 2004	¥512,885	¥204,764	¥101,086	¥109,829	¥928,564	¥195,661	¥1,124,225
Depreciation	12,713	7,440	927	3,777	24,857	2,397	27,254
Capital expenditures	13,096	2,504	2,711	2,117	20,428	968	21,396

	Thousands of U.S. Dollars						
Year Ended March 31, 2005	Internal Combustion Engine & Machinery	Pipes, Valves, & Industrial Castings	Environmental Engineering	Other	Total	Corporate & Eliminations	Consolidated
Net sales:							
Unaffiliated customers	**$5,445,458**	**$1,594,664**	**$1,099,374**	**$1,049,532**	**$9,189,028**	**$ —**	**$ 9,189,028**
Intersegment	**823**	**76,981**	**2,327**	**139,776**	**219,907**	**(219,907)**	**—**
Total	**5,446,281**	**1,671,645**	**1,101,701**	**1,189,308**	**9,408,935**	**(219,907)**	**9,189,028**
Cost of sales and operating expenses	**4,706,505**	**1,564,402**	**1,048,290**	**1,101,383**	**8,420,580**	**(94,159)**	**8,326,421**
Operating income	**$ 739,776**	**$ 107,243**	**$ 53,411**	**$ 87,925**	**$ 988,355**	**$ (125,748)**	**$ 862,607**
Identifiable assets at March 31, 2005	**$5,739,467**	**$1,781,953**	**$ 989,626**	**$ 942,748**	**$9,453,794**	**$1,696,262**	**$11,150,056**
Depreciation	**132,280**	**59,514**	**8,692**	**15,682**	**216,168**	**21,851**	**238,019**
Capital expenditures	**163,383**	**17,037**	**3,346**	**12,972**	**196,738**	**47,159**	**243,897**

Geographic Segments

Year Ended March 31, 2005	Millions of Yen					
	Japan	North America	Other Areas	Total	Corporate & Eliminations	Consolidated
Net sales:						
Unaffiliated customers	**¥659,283**	**¥232,135**	**¥91,808**	**¥ 983,226**	**¥ —**	**¥ 983,226**
Intersegment	**193,242**	**3,000**	**2,792**	**199,034**	**(199,034)**	**—**
Total	**852,525**	**235,135**	**94,600**	**1,182,260**	**(199,034)**	**983,226**
Cost of sales and operating expenses	**772,886**	**215,044**	**87,207**	**1,075,137**	**(184,210)**	**890,927**
Operating income	**¥ 79,639**	**¥ 20,091**	**¥ 7,393**	**¥ 107,123**	**¥ (14,824)**	**¥ 92,299**
Identifiable assets at March 31, 2005	**¥746,627**	**¥259,218**	**¥64,737**	**¥1,070,582**	**¥ 122,474**	**¥1,193,056**

Year Ended March 31, 2004	Millions of Yen					
	Japan	North America	Other Areas	Total	Corporate & Eliminations	Consolidated
Net sales:						
Unaffiliated customers	¥675,442	¥188,767	¥66,028	¥ 930,237	¥ —	¥ 930,237
Intersegment	154,741	2,656	1,949	159,346	(159,346)	—
Total	830,183	191,423	67,977	1,089,583	(159,346)	930,237
Cost of sales and operating expenses	815,158	172,195	63,338	1,050,691	(142,303)	908,388
Operating income	¥ 15,025	¥ 19,228	¥ 4,639	¥ 38,892	¥ (17,043)	¥ 21,849
Identifiable assets at March 31, 2004	¥752,041	¥177,163	¥44,290	¥ 973,494	¥ 150,731	¥1,124,225

Year Ended March 31, 2005	Thousands of U.S. Dollars					
	Japan	North America	Other Areas	Total	Corporate & Eliminations	Consolidated
Net sales:						
Unaffiliated customers	**$6,161,524**	**$2,169,486**	**$858,018**	**$ 9,189,028**	**$ —**	**$ 9,189,028**
Intersegment	**1,806,000**	**28,037**	**26,094**	**1,860,131**	**(1,860,131)**	**—**
Total	**7,967,524**	**2,197,523**	**884,112**	**11,049,159**	**(1,860,131)**	**9,189,028**
Cost of sales and operating expenses	**7,223,234**	**2,009,757**	**815,019**	**10,048,010**	**(1,721,589)**	**8,326,421**
Operating income	**$ 744,290**	**$ 187,766**	**$ 69,093**	**$ 1,001,149**	**$ (138,542)**	**$ 862,607**
Identifiable assets at March 31, 2005	**$6,977,822**	**$2,422,598**	**$605,019**	**$10,005,439**	**$ 1,144,617**	**$11,150,056**

Sales by Region

Years Ended March 31, 2005 and 2004	Millions of Yen				Thousands of U.S. Dollars
	2005		2004		**2005**
Japan	**¥637,902**	**64.9%**	¥643,346	69.2%	**$5,961,701**
Overseas:					
North America	**232,631**	**23.6**	189,273	20.3	**2,174,121**
Other Areas	**112,693**	**11.5**	97,618	10.5	**1,053,206**
Subtotal	**345,324**	**35.1**	286,891	30.8	**3,227,327**
Total	**¥983,226**	**100.0%**	¥930,237	100.0%	**$9,189,028**

Sales by region represent sales to unaffiliated customers based on the customers' locations.