

Management Discussion and Analysis

Overview

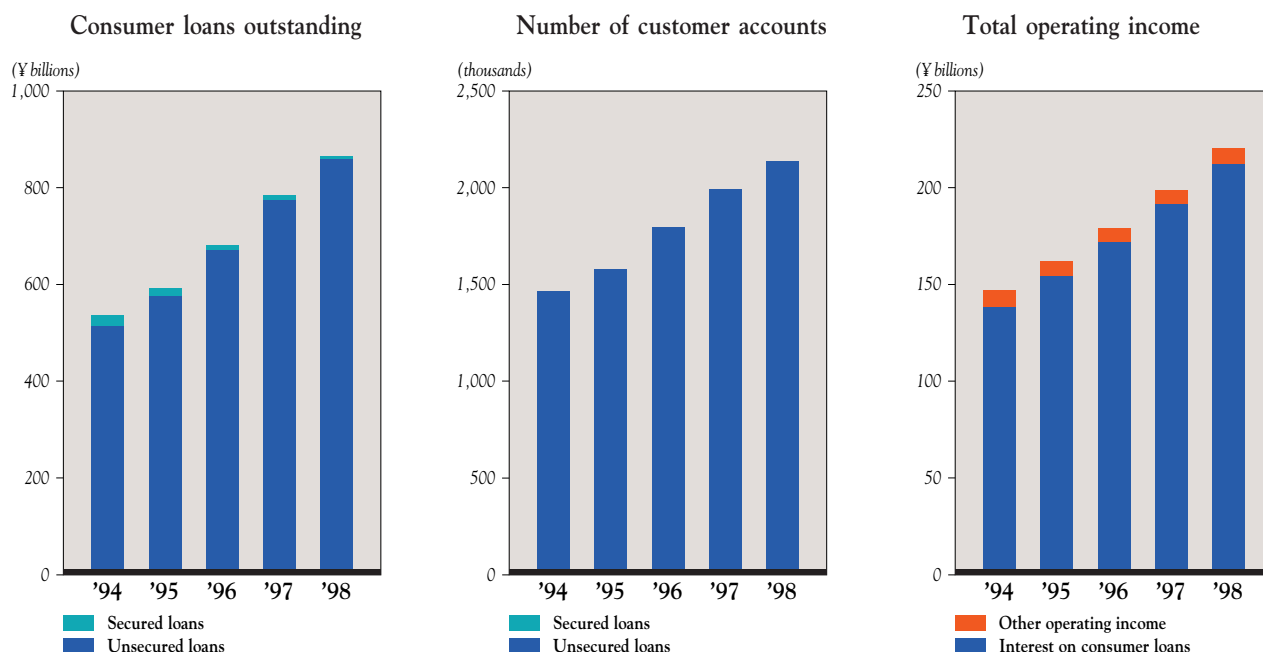
During the year under review, Promise continued to position itself as a leader in the consumer finance market based on the lowest interest rates in the industry, one of the largest, best established marketing networks in the industry, and a highly developed risk management system. The principal strategy pursued by the Company was to increase the number of its unstaffed branches and Irasshai Machines, ATMs, and tie-up ATMs and CDs as part of its continued policy to provide more convenient services that attract new customers and retain existing customers as well as reduce operating costs.

The high pace of growth in unstaffed branches and automated credit providers supported a 10.8% rise in operating income while the average balance per unsecured loan account rose only 3.1%, indicating a large increase in new loan accounts. On the other hand, operating expenses only climbed 10.0%, thanks mainly to finance expenses falling despite the increase in consumer loans due to lower market interest rates and a diversified funding policy. General and administrative (G&A) expenses rose 10.9%, keeping pace with the growth in operating income. Although

growth in advertising and personal expenses was curtailed, this was offset by rising rental, depreciation, and other costs—particularly communication costs—associated with network expansion. Provisions for uncollectible loans were in line with the increase in loans outstanding. The ratio of credit losses written off to the consumer loans outstanding increased slightly, to 2.4%, but still underscored the appropriateness of our credit evaluation system and the efficiency of our collection system. The success of the Company's low cost operations strategy helped operating profit advance 12.0% compared with the 10.8% rise in operating income. After reducing nonoperating expenses, net income was up 11.5%, to ¥38.6 billion.

Operating Income

Total operating income for the year under review advanced 10.8%, to ¥220.3 billion, hitting a record high, with annual growth rates for the period from fiscal 1994 to 1998 ranging from 9.3% to 11.0%. This increase reflected a 10.9% rise in interest on consumer loans to ¥212.3 billion that was primarily due to the 10.5% increase in loans outstanding to ¥866.6 billion. The actual yield per annum on unse-



cured loans fell slightly to 25.7% and the average balance of unsecured loans per account increased by 3.1%, to ¥401,000.

By segment, small-lot unsecured consumer loans, our mainstay business, generated the bulk of operating income. They accounted for ¥858.2 billion or 99.0% of loans outstanding at year end. The remainder of loans outstanding comprised secured loans. Since Promise has frozen the issue of new, large denomination secured loans, total outstanding secured loans dropped to ¥8.4 billion from ¥9.0 billion in the previous fiscal year.

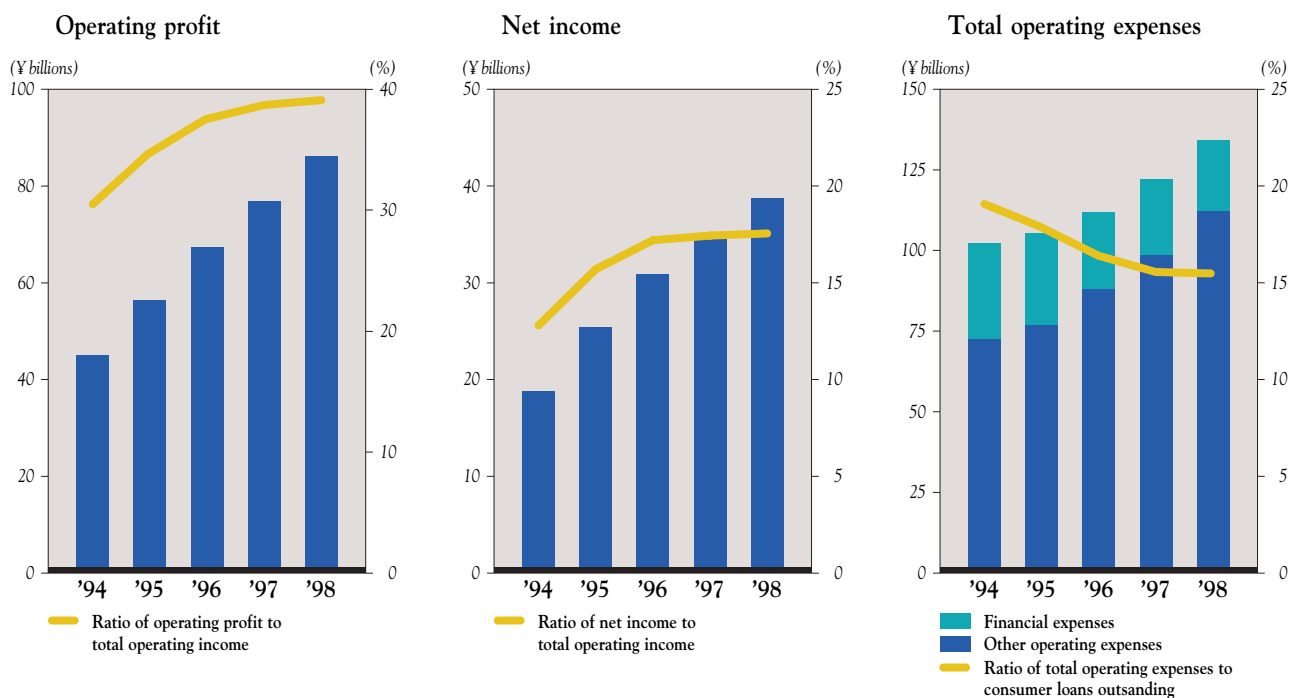
Other operating income rose 6.9% from the year before to ¥8.0 billion, representing 3.6% of total operating income, because of greater collection of credit losses previously written off.

Operating Expenses

Total operating expenses increased 10.0%, to ¥134.2 billion. Financial expenses, which are comprised almost entirely of interest payments, decreased 6.8%, to ¥22.1 billion despite the increase in consumer loans outstanding, reflecting lower market interest rates. The average interest rate on fund procurement fell from 3.193% to 2.872% on long-

term fund procurement, which accounted for 91.8% of total fund procurement. The average interest rate for the year on short-term fund procurement was also lower, falling from 1.509% to 1.458%. This was due to a range of factors, including the reduction in market interest rates and the rollover of high interest rate borrowing. The ratio of fixed-interest rate fund procurement to total fund procurement reached 60.3% as of the end of March 1998. Considering the current low interest rate environment, fixed-rate fund procurement provides a substantial cushion against any future increase in market interest rates.

G&A expenses rose 10.9%, to ¥86.5 billion. Advertisements, which accounted for 13.1% of G&A expenses, gained 3.3%, to ¥13.3 billion while employees' salary and bonuses rose 3.0%, to ¥19.6 billion, reflecting 22.6% of G&A expenses. Rent expenses climbed 17.0%, to ¥10.6 billion, accounting for 12.3% of G&A expenses. Finally, other expenses, which include depreciation expenses, grew 15.5%, to ¥45.0 billion, accounting for 52.0% of G&A expenses. Other and rent expenses rose at a much higher rate especially because of strong growth in communication expenses due to network expansion, reflecting the Company's



aggressive investment in unstaffed branches, tie-up ATMs and CDs, and automated credit providers.

The ratio of provision for uncollectible loans to consumer loans outstanding at the end of the fiscal year, was stable year-on-year at 3.2%, resulting in a provision of ¥25.6 billion for uncollectible loans on the statements of income.

Consequently, operating profit jumped to ¥86.1 billion, a 12.0% year-on-year increase, and our operating profit ratio rose 0.4 percentage points to 39.1%. This improvement mainly resulted from the decline in financial expenses, supported by strong cost control in other areas.

Total other expenses, net increased ¥679 million, to ¥3.7 billion. Notable items included a ¥2.8 billion net loss on sale or disposal of property and equipment, including the sale of unused land to a subsidiary, and a ¥1.7 billion loss on valuation of investments in securities related to the disposal of investment trusts. In recording these losses, the Company made further progress in retiring unrealized losses from its assets. The valuation losses were partially offset by a ¥1.2 billion gain on liquidation of

Tokumei Kumiai (Japanese leveraged leasing transactions).

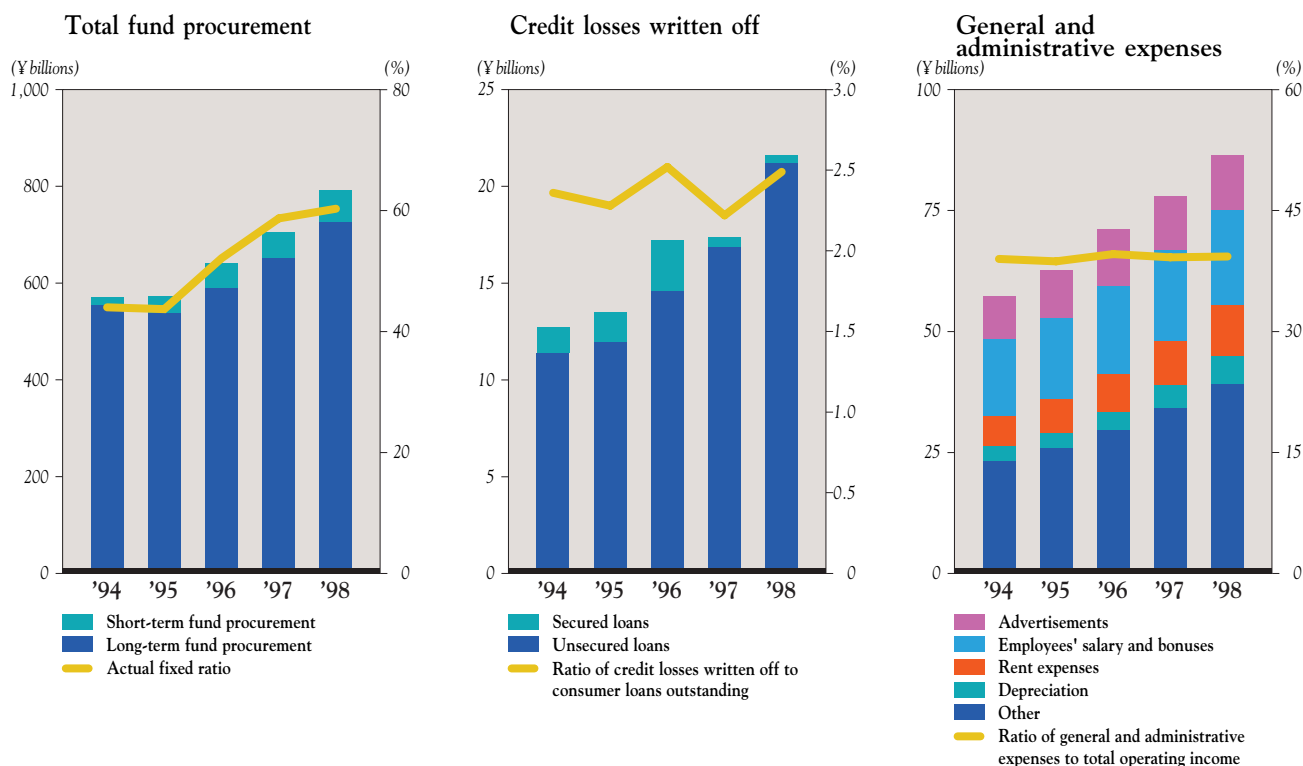
As a result, income before income taxes advanced 11.6%, to ¥82.4 billion. The Company's effective tax rate remained almost unchanged at 51%. Consequently, net income was up 11.5%, to ¥38.6 billion.

Fund procurement

We have further diversified our funding sources by issuing a variety of financial instruments domestically and overseas that make use of our high credit rating, including equity issues, commercial paper, and convertible and unsecured straight bonds.

As of March 31, 1998, our total fund procurement outstanding, including capital market funding, had risen 12.2% over the previous year to ¥792.5 billion, of which ¥727.7 billion, or 91.8%, was accounted for by long-term fund procurement, inclusive of current portion.

Of the Company's outstanding fund procurement, including straight and convertible bonds, as of year-end, a total of 60.3% was accounted for by fixed-rate fund procurement, compared with 58.7% in fiscal 1997. Excluding straight and convertible bonds, the ratio of fixed-rate



borrowing in a narrow sense to total fund procurement reached 55.4% compared with 49.5% in the previous fiscal year. Long-term loans at variable interest rates accounted for 31.5% of outstanding fund procurement with the remaining 8.2% in variable rate short-term loans. Promise has in the past, and will in the future, enter into floating to fixed interest rate swaps to hedge against increased funding costs associated with rising interest rates.

Write off of Credit Losses

Credit losses written off this year totaled ¥21.6 billion, including both secured and unsecured loans. The ratio of credit losses written off to the consumer loans outstanding as of the end of the year was 2.4%, slightly higher than the 2.2% recorded in the previous fiscal year. The higher rate reflects—but is much less than—a substantial rise in personal bankruptcies in recent years. Stringent credit control policies have enabled the Company to keep growth in write-offs to a minimum.

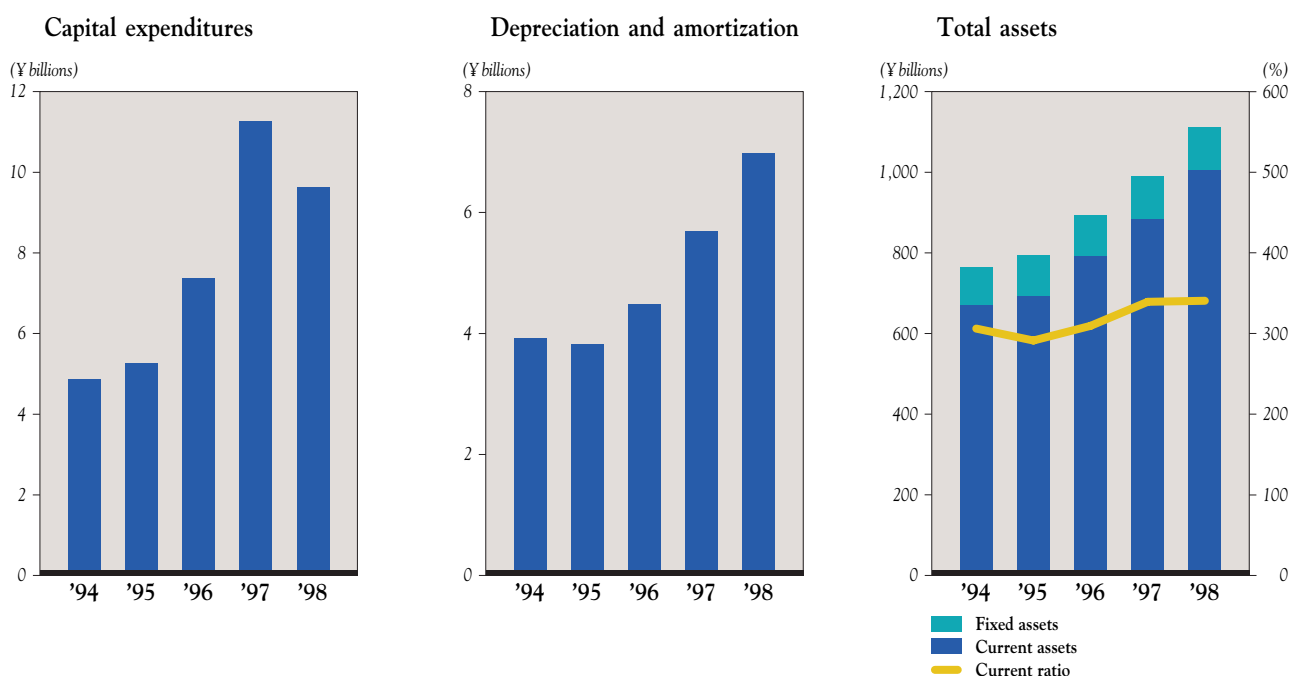
Cash Flow

The Company maintained adequate liquidity for operations during the fiscal year. Net cash pro-

vided by operating activities was ¥72.0 billion, compared with ¥58.6 billion in the previous fiscal year. This increase resulted mainly from greater income. Net cash used in investing activities was ¥107.6 billion, compared with ¥130.1 billion in fiscal 1997. The decline resulted principally from an increase in principal collected on consumer loans offsetting the expanded volume of consumer loans made to customers. Net cash provided by financing activities was ¥81.3 billion, compared with ¥58.3 billion last year, reflecting increased long- and short-term fund procurement. Consequently, the net increase in cash and cash equivalents was ¥45.8 billion, bringing cash and cash equivalents at the end of the year to ¥130.7 billion.

Capital Expenditures

Promise's capital expenditures in fiscal 1998 were mainly used in the establishment of new branches, the upgrading of existing branches, increasing the number of Irasshai Machines and ATMs, and installing computer-related equipment and facilities. The number of unsecured loan branches rose from 748 at the end of last year to 1,003. Meanwhile, the number



of staffed branches declined from 469 to 420, and the number of unstaffed branches soared from 281 to 585. There was also an increase in the number of ATMs, which climbed from 1,056 as of the end of March 1997 to 1,335 as of the end of March 1998.

This enhancement of the Company's facilities resulted in capital expenditures of ¥9.6 billion, compared with ¥11.3 billion in fiscal 1997. The major portion of these expenditures were allocated to the previously mentioned expansion. The Company estimates that capital expenditures for fiscal 1999 and 2000 will amount to ¥9.9 billion and ¥15.0 billion, respectively, and will be used for a similar purpose as in fiscal 1998.

Shareholders' Equity and Dividends

Shareholders' equity continued to rise during the period under review, growing ¥33.7 billion or 14.5%, to ¥265.0 billion. As a result, the shareholders' equity ratio advanced from 23.3% to 23.8%. After the fiscal year end, share offerings made by the Company in June 1998 further raised the shareholders' equity ratio.

We consider technological development and capital expenditures for information processing technology indispensable for meeting the challenge of increasing competition in the consumer finance industry. Therefore, we will strive to accrue internal reserves in conjunction with the increase in shareholders' equity and boost revenue and earnings to enable us to respond with flexibility to future trends.

Promise's dividend policy focuses on increasing the return of profits to shareholders in accordance with revenue and earnings.

Year 2000 Compliance

Along with the development of its next-generation system, Promise has been modifying its computer systems to address the year 2000 issue and believes it will be year 2000 compliant after an upgrade that is scheduled for completion by the end of 1998. The Company expects to invest approximately ¥8 billion during fiscal 1999 for this computer upgrade.

