

To Our Stockholders

Annual Report 2005
Year ended September 30, 2005



*Processing Technologies for Tomorrow*SM

HOSOKAWA MICRON CORPORATION

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A Message to Our Shareholders

During the preceding two fiscal years, the Corporation made significant progress in executing our long term strategies to position ourselves for the future. For example, we were successful in creating a flat organization in which all overseas operations are managed directly by headquarters in Japan resulting in greater efficiency. Additionally, we sold off certain operations and properties in the US and focused our global research and development activities on our core business of powder and particle technology. We consolidated some operations and continued our aggressive cost reduction programs. As a result of meeting these initiatives, we returned our operations to profitability and strengthened our balance sheet. Subsequently, we will pay out a dividend of ¥5 per share for fiscal year 2005.

On October 1st, 2005, we implemented a new three year plan to propel our growth. In these coming years, we are committed to developing new technologies that will help our customers create new products with longer life. We remain steadfast in our goal to continue to be the top enterprise in the field of powder technology. Our business objective is clear as we strive to bring the most innovative technologies and advances in nano particle technologies to our customers to help change and shape the world for the future. Our theme for this Plan period is “Creation and Enhancement” as we work tirelessly to become an excellent corporation while meeting our financial and business objectives.

Last, but not least, your continued support of the Corporation and confidence in our future is greatly appreciated.



**President & C.E.O.
Masuo Hosokawa**

Summary of Global Operations

Following a period of stagnation during the second half of 2004, Japan's economy staged a rebound. The demand for exports continues to grow and this situation creates a favorable outlook. Growth in internal and external demand lifted corporate earnings and household spending, leading to expectations for increases in consumer spending and capital expenditures. However, the corporate price index began to climb along with a much higher cost of crude oil and primary materials. Higher interest rates are another source of concern. As a result, the outlook now calls for a cautious stance.

The U.S. economy continued to stage a generally steady self-sustaining recovery despite the impact of several large hurricanes. However, there were signs of weakness in some real estate statistics. Looking ahead, consumer spending may decline if crude oil prices remain high and the war in Iraq continues.

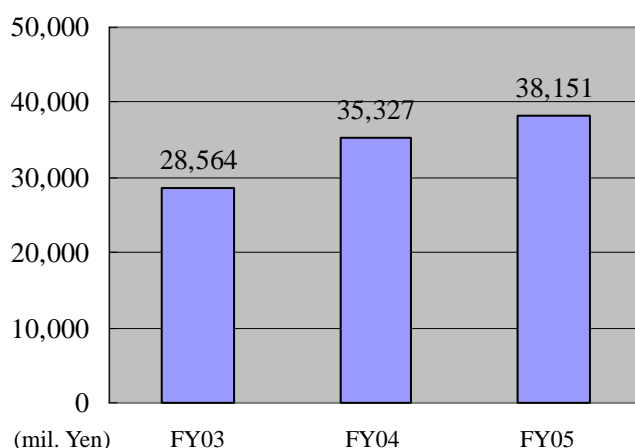
In Europe, economies continue to slowly expand. The economic recovery is expected to continue as the euro's depreciation supports growth in exports. However, this region continues to struggle with problems such as rising competition from emerging nations, mounting budget deficits in major European countries and persistently high unemployment rates.

In Asia, the Chinese economy remains healthy despite the higher cost of crude oil because of investments in fixed assets and strength in consumer spending. External demands remain strong. In the ASEAN countries, consumer spending is weakening, but nations are adopting policies that encourage investments and exports due to the need to maintain the current rate of growth. As a result, the economic outlook remains positive.

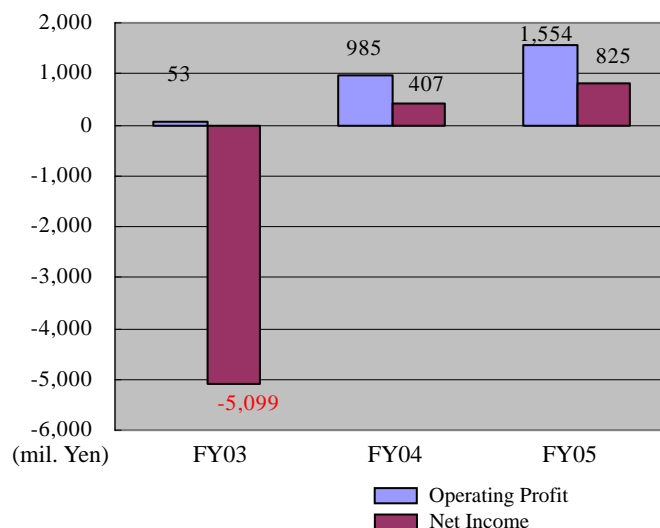
During the fiscal year that ended in September 2005, bookings increased overall by 5.3%, or 1,940 million yen, to 38,802 million yen. The backlog also increased significantly by 12.3%, or 1,230 million yen to 11,223 million yen while net sales showed a strong increase of 8.0%, or 2,824 million yen, to 38,151 million yen from the previous year.

Earnings increased too as the Group continued its cost monitoring programs. Initiatives included raising prices of some products, aggressive negotiations with vendors, strategic outsourcing and cost-cutting programs targeting the cost of sales and selling, general and administrative expenses. The result was a 60% increase in operating profit from 985 million yen to 1,554 million yen. The increase in ordinary profit rose dramatically from 184 million yen to 1,395 million yen. Net income was affected by extraordinary losses, including valuation losses on stock held in privately owned U.S. companies. Nevertheless, net income approximately doubled, rising from 407 million yen to 825 million yen.

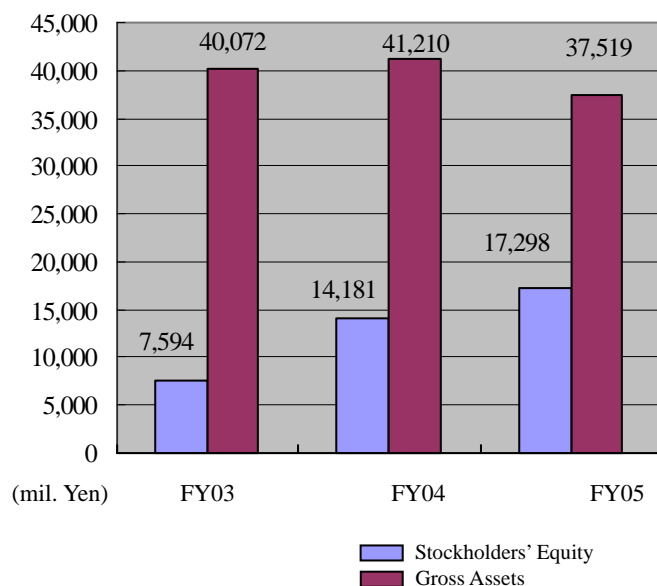
Total Sales Over a Three Year Period



Operating Profit, Net Income



Stockholders' Equity, Gross Assets



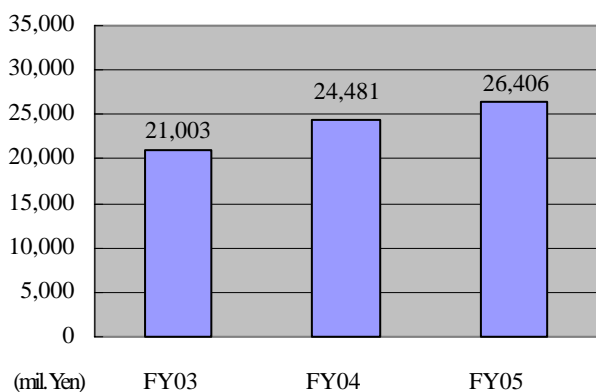
Summary of the Business by Segments

1) Powder and Particle Processing Operations

This segment includes the core products and technologies of the Group, including size reduction, classification, mixing, drying and analytical equipment. During this fiscal year, operations in all market segments were strong, particularly for IT applications (electronic materials, toner and magnets), resins, carbon products and food products.

Bookings increased 10.7%, or 2,666 million yen, to 27,691 million yen, the backlog increased a dramatic 33.1%, or 1,885 million yen, to 7,585 million yen and external sales increased 7.9%, or 1,925 million yen, to 26,406 million yen. Operating profit increased 48.1% to 1,703 million yen.

■ Three Year Sales History of Powder and Particle Processing Operations

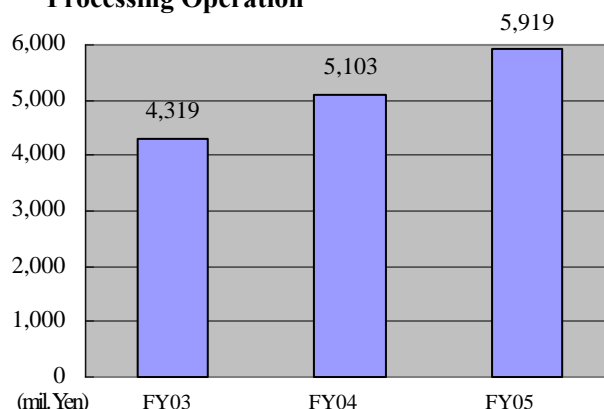


2) Blown Film Processing Operations

This segment designs, manufactures and sells blown film equipment and technologies to manufacture a wide range of products ranging from everyday plastic bags used in grocery stores to sophisticated multi layer films used for packaging in the food and pharmaceutical industries. Most sales for this segment are generated in the United States and Europe. Operations were somewhat challenged due to the appreciation of the euro relative to the U.S. dollar and the higher cost of raw materials associated with the higher price of crude oil. However, the segment achieved solid operating results in Germany, Italy, the U.S. and Japan. Significant contributions to sales were made by equipment for producing functional films for wrapping food products in the United States and by equipment used by electronic component manufacturers in Japan to produce value-added, multilayer film.

Bookings declined sharply, falling 29.1% to 4,755 million yen. However, external sales increased from 16.0% to 5,919 million yen. As a result, the backlog fell 42.1% to 1,662 million yen. Despite these declines, operating profit increased 6.0% to 159 million yen.

■ Three Year Sales History of Blown Film Processing Operation

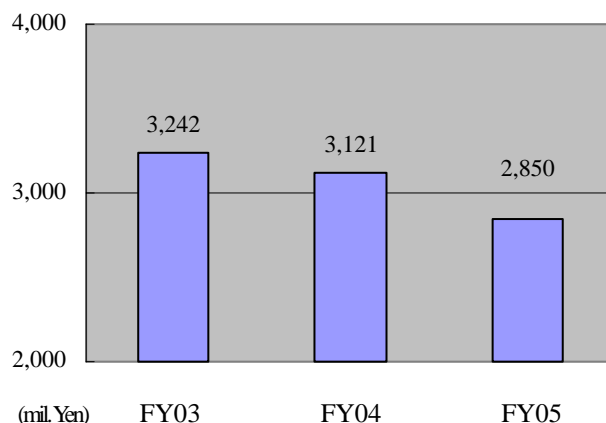


3) Clean Air and Environmental Protection Operations

This business segment is engaged in the manufacture and sale in Japan of environmental protection equipment and clean air control equipment. Strong results were posted by equipment used for product collection of recycling and electronic materials. However, demand for environmental protection equipment was held back primarily by weaknesses in the incinerator market. Demand for precision clean air control equipment was impacted by a downturn in LCD-related capital expenditures.

As a result, bookings decreased 3.9% to 2,529 million yen and the backlog declined by 31.7% to 576 million yen. External sales decreased 8.7% to 2,850 million yen and operating profit was down 15.9% to 362 million yen.

■ Three Year Sales History of Clean Air and Environmental Protection Operation

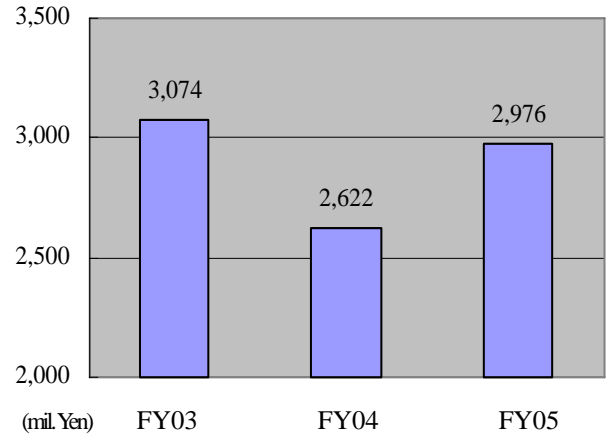


4) Confectionery and Bakery Technology and Systems Operations

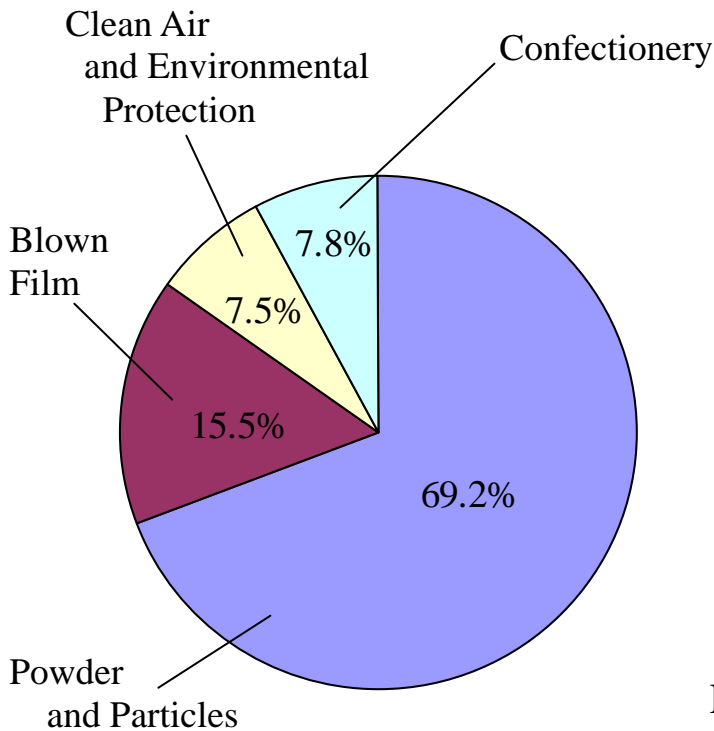
This segment is engaged in the design, manufacture and sale of confectionery (hard candy and bakery) production equipment, mainly in Europe and the United States. Sales activities mainly involved consulting-based sales targeting major U.S. bakery and confectionery companies. This segment focuses on joint development projects and sales involving the technical upgrades of existing equipment. In addition to activities in the core U.S. and European markets, the segment worked on building relationships with customers in new markets such as the Middle East.

Bookings increased 53.3% to 3,825 million yen and the backlog saw significant growth of 142.0% to 1,399 million yen. External sales increased 13.5% to 2,976 million yen and operating profit rose an impressive 56.6% to 192 million yen.

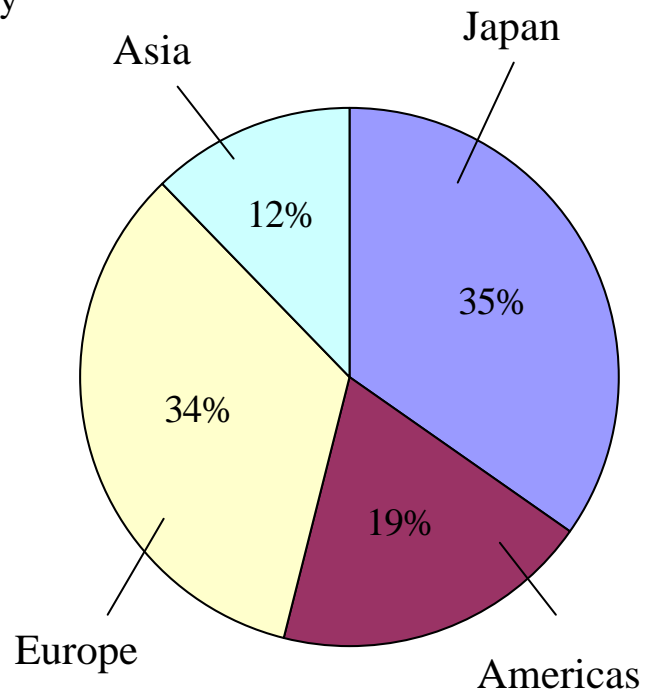
■ Three Year Sales History of Confectionery Production Equipment Operation



Sales by Business Segment



Sales by Geography



Fiscal Year 2006 Plan and 3-Year Plan

The HOSOKAWA MICRON Group is dedicated to strengthening its position as a global leader in powder science by accumulating a veritable "mountain range" of powder technologies. The Company has a broad range of processing equipment and technologies that allows it to bring its customers creative and innovative solutions. During this Plan Term, we will continue to develop, manufacture and commercialize new materials for high value applications and key customers. Additionally, the Group, in concert with the Hosokawa Powder Technology Research Institute will expand our material-related businesses with new and challenging applications which will keep the HOSOKAWA MICRON GROUP at the forefront of powder technology.

In addition, the Group will use its collective global strengths to develop new technologies and focus on product enhancements in our core businesses to meet customer's evolving needs. We believe that these activities will strengthen our market position and build a powerful technological base that will result in higher earnings and increased shareholder value. In 2008, our goals are to achieve net sales of 42 billion yen, operating profits of 2.5 billion yen and an ROE of 8.5%.

To accomplish these goals, the Group is committed to the following initiatives:

- 1) The Group will build a powerful profit structure by developing new advances in powder technology, including nano-particle technology that meet the demands of today's fast moving industries such as electronics, pharmaceuticals, and IT related industries.
- 2) We will continue to leverage the Group's strengths as a global organization by improving the transfer or technology and advanced application knowledge among our Group of companies
- 3) We will continue to improve our operations by making effective investments.
- 4) We will achieve our business goals and strengthen the Group's financial position by raising earnings and conducting diversified fund procurement activities to build a solid infrastructure to enable the Group to take on new challenges.
- 5) We are committed to training and developing our employees and provide them with the tools to become the number one Company in the field of powder sciences throughout the world.

Fiscal Year 2005 Business Highlights

New Advanced Technologies for Medicinal Applications

PLGA (Poly Lactic-co-Glycolic Acid) is a biocompatible organic material which is harmless to the human body. Hosokawa has developed a method for the encapsulation of medical components into PLGA nanospheres which makes composite particles. This technology has wide application in the field of medicine. For example;

--- Drugs can be administered without the necessity of injections, resulting in the reduction of physical strain on patients. We see this with advances in certain medicines that can be released transdermally or through pulmonary inhalation. Great strides are currently being made with dry powder inhalation therapy for diabetics. We believe this is just the beginning of this exciting new time in the development of new patient friendly drug delivery systems.

--- Particle design is a key element with controlled release properties of drugs. Advances in this technology help drugs to be released faster and more efficiently throughout the body allowing medicines to work more effectively.

New Cosmetic Product "NanoCryosphere" Promotes Younger Looking Skin

Our original cosmetic product "NanoCryosphere" incorporates the properties of PLGA nanocomposite particles. The PLGA nanocomposite particles contained in our special anti-aging lotion are specifically designed to a particle size of around 200 nm which is ideally suitable to penetrate the outer layer of the skin by the pulsing motion of the cells and the surface tension of water to reach the dermis. The functional nanoparticles penetrating into the depth of skin remain there until they gradually decompose and release the contained vitamin compounds over a period of time to promote the regeneration of younger looking skin. This product is being met with tremendous enthusiasm. In addition to cosmetics for the transdermal market, we have completed development of a new hair growth product which will soon be introduced. This new area of consumer products holds tremendous opportunities for the Group as marketing plans are in development.

Additionally, last October we succeeded in the encapsulation of NFkB Decoy Oligo, a nucleic acid drug developed by AnGes MG Inc. into our PLGA nanocomposites. The nanocomposites have the potential to be incorporated into a new drug for external use to treat skin diseases such as atopic dermatitis and psoriasis. The drug efficacy will be increased by the construction of the particle with our technology. We are currently evaluating the pharmacological effect of this drug against skin diseases and remain optimistic at preliminary results.

Air Shower “Stratosphere” for the Removal of High Dust Concentrations

Hosokawa’s new air shower “Stratosphere” is ideally suited for worker safety as it protects the operator from contamination, when workers are handling powders with scattering characteristics.

Application examples;

- * Chemical Plants handling Carbon, Toner, Ceramics.
- * Food processing environments
- * Pharmaceutical manufacturing.
- * Environmental protection, recycling operations, etc.



“Stratosphere”

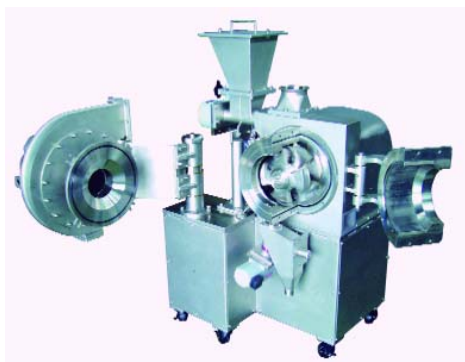
High Speed Ultra Fine Grinding Machine “Super Micron Mill E-Type”

The Super Micron Mill E-Type is a unique high speed grinding technology that combines attrition and impact-sharing forces. It also incorporates classification mechanisms using extraction nozzles to remove foreign materials.

This new design offers a compact design, significant energy savings and lower noise operation.

Application examples;

- * Fibrous materials requiring removal of foreign impurities;
 - Herbal medicines
 - Fresh soy bean with husks
- * Cosmetic raw materials
- * Pharmaceutical materials



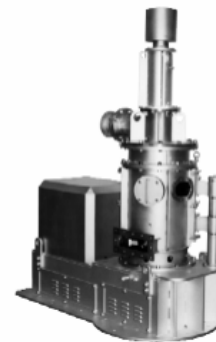
“Super Micron Mill E-Type”

The Drymeister Receives Award for Excellence

At the 8th Meeting of Japan Food Processing Equipment and Materials Association

The Drymeister is a unique dryer that can dry grind and classify in a single piece of equipment with its continuous operation, it simplifies normally complicated multistage operations.

The Drymeister is ideally suited for feed materials with high moisture content such as slurries. In addition to its simplicity in operation, the equipment also offers an easy access for cleaning and maintenance.



“Drymeister”

Sponsored by Japan Food-Stuff Paper Co. Ltd., for the recognition and acknowledgement of excellence, five food processing machines and five relative materials were recognized at the 8th annual award ceremony.



Above: Mr. Miyata, Vice President of Corporation receives the award.
Place: Daiichi Hotel Tokyo
Date: September 8th, 2005

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Balance Sheets

September 30, 2005 and 2004

Assets	Millions of yen		Thousands of U.S. dollars (Note 1)
	2005	2004	2005
Current assets:			
Cash on hand and at bank (Notes 5 and 13)	¥ 3,815	¥ 6,218	\$ 33,761
Trade receivables	10,395	10,711	91,991
Less allowance for doubtful receivables	(136)	(149)	(1,204)
Net trade receivables	10,259	10,562	90,787
Inventories (Note 4)	4,491	4,593	39,743
Securities	409	-	3,620
Deferred tax assets (Note 7)	574	398	5,080
Assets of discontinued operations held for sale (Note 3)	-	797	-
Other current assets	557	692	4,929
Total current assets	20,105	23,260	177,920
Property, plant and equipment (Notes 5 and 10):			
Land	4,912	4,912	43,469
Buildings and structures	12,202	12,185	107,982
Machinery and equipment	9,720	9,506	86,018
Construction in progress	32	12	283
	26,866	26,615	237,752
Less accumulated depreciation	(13,621)	(12,884)	(120,540)
Net property, plant and equipment	13,245	13,731	117,212
Investments and other assets:			
Investments in securities (Note 11)	833	778	7,372
Goodwill	2,834	2,862	25,080
Deferred charges (Note 5)	36	38	319
Deferred tax assets (Note 7)	121	134	1,071
Other assets	345	407	3,053
Total investments and other assets	4,169	4,219	36,895
	¥ 37,519	¥ 41,210	\$ 332,027

See accompanying notes to consolidated financial statements.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Balance Sheets

September 30, 2005 and 2004

Liabilities and Stockholders' Equity	Millions of yen		Thousands of U.S. dollars (Note 1)
	2005	2004	2005
Current liabilities:			
Short-term borrowings, including current portion of long-term debt (Note 5)	¥ 1,109	¥ 8,020	\$ 9,814
Trade payables	4,824	4,874	42,690
Accrued expenses	3,397	2,961	30,062
Accrued income taxes (Note 7)	396	34	3,504
Deferred tax liabilities (Note 7)	36	75	319
Advances from customers	1,536	1,351	13,593
Liabilities of discontinued operations held for sale	-	997	-
Other current liabilities	1,091	1,003	9,655
Total current liabilities	12,389	19,315	109,637
Noncurrent liabilities:			
Long-term debt (Note 5)	3,400	3,342	30,088
Retirement and severance benefits (Note 6)	3,456	3,396	30,584
Retirement allowances for directors and statutory auditors	356	354	3,151
Deferred tax liabilities (Note 7)	266	245	2,354
Other liabilities	41	48	363
Total noncurrent liabilities	7,519	7,385	66,540
Minority interests	313	329	2,770
Stockholders' equity (Note 8):			
Common stock:			
Authorized - 99,347,000 shares			
Issued -39,881,640 shares (37,184,434 shares in 2004)	13,193	11,991	116,752
Capital surplus	3,909	2,711	34,593
Retained earnings	2,707	1,882	23,956
Net unrealized holding gains on securities	114	23	1,009
Foreign currency translation adjustments	(2,578)	(2,414)	(22,814)
Treasury stock, at cost 62,731 shares in 2005 and 21,507 shares in 2004	(47)	(12)	(416)
Total stockholders' equity	17,298	14,181	153,080
Contingent liabilities (Note 14)	_____	_____	_____
	¥ 37,519	¥ 41,210	\$ 332,027

See accompanying notes to consolidated financial statements.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Statements of Income

Years ended September 30, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2005	2004	2005
Net sales	¥ 38,151	¥ 35,327	\$ 337,619
Cost of sales	<u>25,171</u>	<u>23,161</u>	<u>222,752</u>
Gross profit	12,980	12,166	114,867
Selling, general and administrative expenses (Note 9)	<u>11,426</u>	<u>11,181</u>	<u>101,115</u>
Operating profit	1,554	985	13,752
Other income (expenses):			
Interest and dividend income	31	61	274
Interest expense	(168)	(677)	(1,487)
Equity in (loss) earnings of affiliates	(1)	4	(9)
Net gain on sale of securities	18	145	159
Devaluation loss on securities	(186)	(230)	(1,646)
Net gain (loss) on sale or disposals of property, plant and equipment	(1)	156	(9)
Net exchange loss	(19)	(70)	(168)
Restructuring costs	(61)	(36)	(540)
Environmental remediation related costs	(56)	-	(495)
Settlement costs for indemnification	(41)	-	(363)
Reversal of allowance for doubtful receivables	-	184	-
Relocation expenses for head office	-	(164)	-
Reversal of deferred income from discontinued operations for prior period	-	134	-
Loss from discontinued operations, net (Note 3)	-	(181)	-
Other, net	<u>(29)</u>	<u>(48)</u>	<u>(256)</u>
	<u>(513)</u>	<u>(722)</u>	<u>(4,540)</u>
Income before income taxes and minority interests	1,041	263	9,212
Income taxes (Note 7):			
Current	463	50	4,097
Deferred	<u>(233)</u>	<u>(194)</u>	<u>(2,062)</u>
	<u>230</u>	<u>(144)</u>	<u>2,035</u>
Income before minority interests	811	407	7,177
Minority interests	<u>14</u>	<u>-</u>	<u>124</u>
Net income	¥ <u>825</u>	¥ <u>407</u>	\$ <u>7,301</u>

See accompanying notes to consolidated financial statements.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Statements of Income

Years ended September 30, 2005 and 2004

	Yen		U.S. dollars (Note 1)
	2005	2004	2005
Net income per share of common stock:			
Basic	¥ 20.98	¥ 14.52	\$ 0.19
Diluted	19.81	14.11	0.18
	Number of shares		
Average number of common shares outstanding (thousands)	37,906	27,992	
Average number of diluted common shares outstanding (thousands)	40,136	28,863	

See accompanying notes to consolidated financial statements.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Statements of Stockholders' Equity

Years ended September 30, 2005 and 2004

	Millions of yen						
	Number of common shares issued	Common stock	Capital surplus	Retained earnings (accumul- -ated deficit)	Net unrealized holding gains (losses) on securities	Foreign currency translation adjust- ments	Treasury stock
Balance at September 30, 2003	27,905,360	¥ 9,273	¥ 9,637	¥ (8,154)	¥ 62	¥ (2,780)	¥ (444)
Net income for year				407			
Issuance of common stock	3,420,000	964	964				
Issuance of common stock for conversion of bonds	5,859,074	1,754	1,746				
Transfer from capital surplus to accumulated deficit (Note 8)			(9,636)	9,636			
Repurchase of treasury stock							(16)
Sale of treasury stock				(7)			448
Net unrealized holding losses on securities					(39)		
Foreign currency translation adjustments						366	
Balance at September 30, 2004	<u>37,184,434</u>	<u>¥ 11,991</u>	<u>¥ 2,711</u>	<u>¥ 1,882</u>	<u>¥ 23</u>	<u>¥ (2,414)</u>	<u>¥ (12)</u>
Net income for year				825			
Issuance of common stock for conversion of bonds	2,697,206	1,202	1,198				
Purchase of treasury stock							(35)
Net unrealized holding gains on securities					91		
Foreign currency translation adjustments						(164)	
Balance at September 30, 2005	<u>39,881,640</u>	<u>¥ 13,193</u>	<u>¥ 3,909</u>	<u>¥ 2,707</u>	<u>¥ 114</u>	<u>¥ (2,578)</u>	<u>¥ (47)</u>

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Statements of Stockholders' Equity

Years ended September 30, 2005 and 2004

	Thousands of U.S dollars (Note 1)					
	Common stock	Capital surplus	Retained earnings (accumul -ated deficit)	Net un- realized holding gains (losses) on securities	Foreign currency translation adjust- ments	Treasury stock
Balance at September 30, 2004	\$ 106,115	\$ 23,991	\$ 16,655	\$ 204	\$ (21,363)	\$ (106)
Net income for year			7,301			
Issuance of common stock for conversion of bonds	10,637	10,602				
Purchase of treasury stock						(310)
Net unrealized holding losses on securities				805		
Foreign currency translation adjustments					(1,451)	
Balance at September 30, 2005	\$ 116,752	\$ 34,593	\$ 23,956	\$ 1,009	\$ (22,814)	\$ (416)

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Statements of Cash Flows

Years ended September 30, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2005	2004	2005
Cash flows from operating activities:			
Net income	¥ 825	¥ 407	\$ 7,301
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	892	931	7,894
Equity in loss (earnings) of an affiliate	1	(4)	9
Net gain on sale of securities	(18)	(145)	(159)
Devaluation loss on securities	186	230	1,646
Net loss (gain) on sale or disposals of property, plant and equipment	1	(89)	9
Deferred income taxes	(233)	(194)	(2,062)
Minority interests	14	-	124
Reversal of deferred income from discontinued operations for prior period, net	-	(134)	-
Loss from discontinued operations	-	181	-
Changes in assets and liabilities:			
Decrease (increase) in trade receivables	289	(1,327)	2,558
Decrease in inventories	94	119	832
Decrease in other current assets	143	65	1,265
Increase in trade payables	71	1,304	628
Decrease (increase) in advances from customers	(69)	716	(611)
Increase in accrued income taxes	295	183	2,611
Decrease (increase) in accrued expenses	(89)	457	(788)
Increase in other current liabilities	71	82	628
Increase(decrease) in retirement and severance benefits	66	(100)	584
Decrease (increase) in other liabilities	(8)	6	(71)
Other, net	359	(223)	3,177
Net cash provided by operating activities	2,890	2,465	25,575

See accompanying notes to consolidated financial statements.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Consolidated Statements of Cash Flows

Years ended September 30, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2005	2004	2005
Cash flows from investing activities:			
Proceeds from sales of securities	¥ 859	¥ 1,102	\$ 7,602
Purchase of securities	(900)	(227)	(7,965)
Purchase of investments in an affiliate	(30)	-	(265)
Capital expenditures	(393)	(369)	(3,478)
Proceeds from sales of property, plant and equipment	44	326	389
Proceeds from collection of loan receivable	-	519	-
Decrease in time deposits	800	600	7,080
Increase in cash and cash equivalents of changes from discontinued operations to continuing operations	-	304	-
Other, net	(1)	(3)	(9)
Net cash provided by investing activities	379	2,252	3,354
Cash flows from financing activities:			
Decrease in short-term borrowings	(4,687)	(6,165)	(41,478)
Proceeds from long-term debt	1,300	-	11,504
Repayment of long-term debt	(2,059)	(1,819)	(18,221)
Proceeds from issuance of bonds	4,982	3,480	44,088
Payment for stock issuance costs	(18)	-	(159)
Repayment of bonds	(4,000)	-	(35,398)
Proceeds from issuance of common stock	-	1,894	-
Proceeds from minority interests	-	174	-
Proceeds from sale of treasury stock	-	440	-
Increase in treasury stock	(35)	(16)	(309)
Net cash used in financing activities	(4,517)	(2,012)	(39,973)
Effect of exchange rate changes on cash and cash equivalents	54	(13)	478
Net increase (decrease) in cash and cash equivalents	(1,194)	2,692	(10,566)
Cash and cash equivalents at beginning of year	5,418	2,726	47,947
Cash and cash equivalents at end of year (Note 13)	¥ 4,224	¥ 5,418	\$ 37,381
Supplemental disclosure of cash flow information:			
Cash paid during the year for:			
Interest	¥ 178	¥ 662	\$ 1,575
Income taxes	90	264	796

See accompanying notes to consolidated financial statements.

HOSOKAWA MICRON CORPORATION AND CONSOLIDATED SUBSIDIARIES

Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(1) Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with accounting principles generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

For consolidated financial statement purposes, the financial statements of foreign subsidiaries have been mainly prepared in a manner and reflect the adjustments, which are necessary to conform to generally accepted accounting principles in the United States.

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

The translation of Japanese yen amounts into U.S. dollars are included solely for the convenience of readers outside Japan, using the prevailing exchange rate at September 30, 2005, which was ¥113 to U.S.\$1. The translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

(2) Significant Accounting Policies

(a) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and all subsidiaries except for Hosokawa Micron (Shanghai) Powder Machinery Co., Ltd. which was established in August 2005. All significant intercompany balances and transactions are eliminated in consolidation. Investment in an affiliate is carried at cost.

(b) Cash and Cash Equivalents (Note 13)

For the purpose of the Consolidated Statements of Cash Flows, cash and cash equivalents consist of cash in hand, deposits at call held with banks, and all highly liquid debt investments with a maturity of three months or less.

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

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(c) *Investment in Securities (Note 11)*

The Company and its domestic subsidiaries adopted the Accounting Standard for Financial Instruments, which was issued by the Business Accounting Deliberation Council. In accordance with this standard, all securities held by the Company and its domestic subsidiaries are classified as other securities. Other securities are carried at fair value with the unrealized gains or losses, net of tax reported in stockholders' equity.

(d) *Allowance for Doubtful Receivables*

Allowance for doubtful receivables of the Company and domestic subsidiaries is provided principally at an amount computed based on the actual ratio of bad debts in the past and the estimated uncollectible amounts based on the analysis of certain individual receivables. Foreign subsidiaries account for the estimated uncollectible amounts based on the analysis of certain individual receivables.

(e) *Inventories (Note 4)*

Finished goods and work in process of the Company and domestic subsidiaries are stated at cost, principally by the specific identification method. Raw materials of the Company and domestic subsidiaries are stated at cost, principally by the moving-average method. Supplies of the Company and domestic subsidiaries are stated at cost, principally by the first-in, first-out method. Inventories of the foreign subsidiaries are stated at the lower of cost or market and cost is determined by either specific identification or the average cost method.

(f) *Long-term Construction-type Contracts*

The Company accounts for long-term construction-type contracts under the completed-contract method.

Foreign subsidiaries account for significant long-term contracts under the percentage-of-completion method and for all other cases under the completed - contract method.

(g) *Property, Plant and Equipment*

Property, plant and equipment are stated at cost. The properties at Tsukuba Technical Development Center, Nara plant, Tokyo branch of the Company and buildings (other than leasehold improvements), which were acquired on or after April 1, 1998, are depreciated using the straight-line method over their estimated useful lives. Other property, plant and equipment of the Company are depreciated using the declining-balance method over their estimated useful lives. Domestic subsidiaries compute depreciation primarily using the declining-balance method. Foreign subsidiaries compute depreciation primarily using the straight-line method.

**HOSOKAWA MICRON CORPORATION
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The principal estimated useful lives are as follows:

Buildings and structures	2 to 47 years
Machinery and equipment	2 to 17 years

(h) *Goodwill and Other Assets*

Goodwill represents the excess of the total acquisition cost over the fair market value of the net assets acquired.

United States Statement of Financial Accounting Standard No. 142 “Goodwill and Other Intangible Assets” (SFAS No. 142) requires goodwill to be tested for impairment on an annual basis and between annual tests in certain circumstances, and written down when impaired, rather than being amortized as previous accounting standards required. Furthermore, SFAS No. 142 requires purchased intangible assets, other than goodwill, to be amortized over their useful lives unless these lives are determined to be indefinite.

(i) *Computer Software*

Expenditure relating to computer software developed for internal use is charged to income when incurred, except if it contributes to the generation of income or to future cost savings. Such expenditure is capitalized as an asset and is amortized using the straight-line method over its estimated useful life, which is usually 5 years.

(j) *Leases (Note 10)*

The Company and its subsidiaries lease various facilities and equipment.

The Company and its domestic subsidiaries account for leases as operating leases, except for those in which ownership is deemed to be transferred to the lessee. The foreign subsidiaries account for finance leases as capital leases.

(k) *Product Warranty*

The Company and its subsidiaries currently provide for the estimated cost to repair or replace products sold under warranties. Such warranties generally cover a 12-month period.

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

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(I) Retirement and Severance Benefits (Note 6)

Upon retirement or termination of employment, employees of the Company and its domestic subsidiaries are entitled to lump-sum or annuity payments based on the current rate of pay and length of service.

The Company and its domestic subsidiaries have adopted the Financial Accounting Standard for Retirement Benefits which was issued by the Business Accounting Deliberation Council. In accordance with this standard, retirement and severance benefits are provided based on the estimated retirement benefit obligation and the pension assets.

Actuarial gains and losses are amortized, from the next year in which the actuarial gains and losses are incurred, using the straight-line method, over 15 years, representing the estimated average remaining service years of employees.

The foreign subsidiaries have pension and supplemental retirement plans covering substantially all employees. Those foreign subsidiaries have adopted United States Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions" and No. 132, "Employees' Disclosure about Pensions and Other Postretirement Benefits." Certain of the Company's foreign subsidiaries' unrecognized net transition liability is being amortized over 15 years, and the amortization is presented in the consolidated statement of income.

To supplement the above, the Company and domestic subsidiaries participate in a multi-employers' contributory defined benefit welfare pension plan (the "welfare pension plan") covering substantially all of their employees. The welfare pension plan is funded in conformity with the funding requirements of the Japanese Welfare Pension Insurance Law, and covers a portion of the governmental welfare pension program and an additional portion under which contributions are made by the respective companies and their employees.

Regarding the welfare pension plan, contributions made by the Company and most of its domestic subsidiaries are expensed out when paid since the pooled fund assets and the entire pension obligations for the welfare pension plan can not be reasonably determined by each of the participants. The pooled fund assets of the Company and most of its domestic subsidiaries at fair value as of September 30, 2005 amounted to ¥1,657 million (\$14,664 thousand).

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(m) Retirement Allowance for Directors and Statutory Auditors

The Company has provided for directors' and statutory auditors' retirement and severance benefits in the financial statements for the estimated unfunded liability.

In 1998, the Company's foreign subsidiaries in the United States established a Supplemental Executive Retirement Plan (SERP). The SERP, which is unfunded, provides certain executives upon retirement, a maximum annual amount of 48% of final average salary for the three highest consecutive years in the last ten years of the executive's credited service.

(n) Income Taxes (Note 7)

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

(o) Foreign Currency Translation

The Company and its domestic subsidiaries have adopted the Financial Accounting Standard for Foreign Currency Transactions which was issued by the Business Accounting Deliberation Council. In accordance with this standard, all monetary assets and liabilities denominated in foreign currencies are converted into Japanese yen at the rate of exchange prevailing on the balance sheet date.

Foreign currency financial statements of foreign subsidiaries are translated into Japanese yen at year-end rates for all assets and liabilities and at weighted average rates for income and expense accounts. Adjustments resulting from the translation of financial statements are reflected in foreign currency translation adjustments in stockholders' equity.

(p) Derivatives and Hedging Activities

The Company has adopted the Financial Accounting Standard on Accounting for Financial Instruments, which was issued by the Business Accounting Deliberation Council. The Company uses derivative financial instruments to manage their exposures to fluctuations in foreign currencies and interest rate on the swap transactions.

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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(q) *Net Income per share*

The basic net income per share of common stock shown for each year in the accompanying consolidated statement of income is computed based upon the weighted average number of common shares outstanding during the year. The diluted net income per share assumes full exercise of potentially dilutive securities outstanding at the date of issuance.

(r) *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

(s) *Reclassifications*

Certain reclassifications have been made to the prior year's consolidated financial statements to conform with the presentation used for the year ended September 30, 2005.

(t) *New Accounting Pronouncements*

Accounting standard for impairment of fixed assets

In the year ended September 30, 2005, the Company and its domestic consolidated subsidiaries did not adopt early the new accounting standard for impairment of fixed assets ("Opinion Concerning Establishment of Accounting Standard for Impairment of Fixed Assets" issued by the Business Accounting Deliberation Council on August 9, 2002) and the implementation guidance for the Accounting Standard for impairment of fixed assets (the Financial Accounting Standard Implementation Guidance No. 6 issued by the Accounting Standards Board of Japan on October 31, 2003). The new accounting standard is required to be adopted in periods beginning on after April 1, 2005, but the standard does not prohibit earlier adoption.

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

The Company and its domestic consolidated subsidiaries will adopt the new standard effective October 1, 2005. Management believes that adoption of this new accounting standard will have no significant effect on the Company's financial statements.

(3) Discontinued Operations

On March 30, 2003 (measurement date), the Board of Directors of Hosokawa Micron International Inc. (HMII), a subsidiary of the Company, adopted a plan to divest certain of the Powder processing equipment operations in the United States. In accordance with United States Statements of Financial Accounting Standards No.144, "Accounting for the Impairment or Disposal of Long-Lived Assets", net losses for the group from October 1, 2002 through the measurement date together with any losses in the realizable value of these assets have been recognized in discontinued operation.

The results of operation of certain of the Powder processing equipment operations in the United States have been presented as discontinued operations in the Company's consolidated statement of income for the year ended September 30, 2004 and sales of those operations were completed in November 2004.

(4) Inventories

Inventories at September 30, 2005 and 2004 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	<u>2005</u>	<u>2004</u>	<u>2005</u>
Finished goods	¥ 1,187	¥ 1,258	\$ 10,504
Work in process	1,733	1,750	15,336
Raw materials	1,501	1,522	13,283
Supplies	<u>70</u>	<u>63</u>	<u>620</u>
	¥ <u>4,491</u>	¥ <u>4,593</u>	\$ <u>39,743</u>

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(5) Long-term Debt and Short-term Borrowings

Long-term debt at September 30, 2005 and 2004 is set forth below:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2004</u>	<u>2005</u>
The Company and domestic subsidiaries:			
Straight bonds with 1.65 % interest, due November 2004	¥ -	¥ 2,000	\$ -
Straight bonds with 3.5 % interest, due September 2008	-	2,000	-
Unsecured convertible type bonds with stock purchase rights with no interest due February 2008	2,600	-	23,009
Secured bank loans with interest 2.24%, due in installments through 2008	1,200	1,600	10,619
Foreign subsidiaries:			
Unsecured loans from banks with variable interest based on EURIBOR plus an additional 1%, repayable through 2006	-	369	-
	<u>3,800</u>	<u>5,969</u>	<u>33,628</u>
Less current portion	<u>400</u>	<u>2,627</u>	<u>3,540</u>
	<u>¥ 3,400</u>	<u>¥ 3,342</u>	<u>\$ 30,088</u>

The aggregate annual maturities of long-term debt after September 30, 2005 are as follows:

<u>Year ending September 30</u>	<u>Millions of yen</u>	<u>Thousands of U.S. dollars</u>
2006	¥ 400	\$ 3,540
2007	400	3,540
2008	3,000	26,548

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At September 30, 2005, assets pledged as collateral for short-term borrowings and long-term debt are as follows:

	<u>Millions of yen</u>	<u>Thousands of U.S. dollars</u>
Land	¥ 4,045	\$ 35,796
Buildings, net of accumulated depreciation	2,681	23,726

As is customary in Japan, short-term and long-term bank loans are made under general agreements which provide that security and guarantees for future and present indebtedness will be given upon request of the bank, and that the bank shall have the right, as the obligations become due, or in the event of their default, to offset cash deposits against such obligations due to the bank.

The Company issued straight bonds amounting to ¥2,000 million in September 2003 and November 2002 respectively, all of which were repaid in November and December 2004.

In June 2004 the Company issued unsecured convertible type bonds with stock purchase rights amounting to ¥3,500 million, all of which were converted to Common stock.

In February 2005 the Company issued unsecured convertible type bonds with stock purchase rights amounting to ¥5,000 million (\$44,248 thousand), of which ¥2,400 million (\$21,239 thousand) were converted to Common Stock. The remaining convertible type bonds with stock purchase rights of ¥2,600 million are convertible into 3,193,710 shares at the applicable exercise price of ¥814.1 per share as of September 30, 2005.

The Company amortized issuing costs associated with the bonds using the straight-line method over three years. The balance of unamortized issuing costs included in deferred charges at September 30, 2005 and 2004 amounted to ¥12 million (\$106 thousand) and ¥15 million, respectively.

(6) Retirement and Severance Benefits

(a) *The Company and its Domestic Subsidiaries*

The Company has non-contributory qualified funded pension plans for regular employees under Japanese tax regulations. The pension benefits under these plans cover approximately 35% of total benefits in respect of such employees. The remaining balance of the pension benefits is covered by unfunded lump-sum plans.

(b) *Foreign Subsidiaries*

The Company's foreign subsidiaries in the United States have three defined contribution plans, which are structured as Section 401(k) type plans under the Internal Revenue Code, covering substantially all employees. The Company's foreign subsidiaries, other than in the United States, have non-contributory defined benefit pension plans covering substantially all employees with varying terms and amounts depending upon salary levels and length of service. The defined benefit plans are funded to accumulate sufficient assets to provide for all accrued benefits.

**HOSOKAWA MICRON CORPORATION
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September 30, 2005 and 2004

The following tables set forth the details of benefit obligation, plan assets and funded status of the Company and its subsidiaries at September 30, 2005 and 2004:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2004</u>	<u>2005</u>
Benefit obligation at end of year	¥ (4,597)	¥ (4,627)	\$ (40,681)
Fair value of plan assets at end of year	<u>560</u>	<u>560</u>	<u>4,955</u>
Funded status (benefit obligation in excess of plan assets)	(4,037)	(4,067)	(35,726)
Unrecognized actuarial loss	566	335	5,009
Unrecognized net transition liability	<u>15</u>	<u>336</u>	<u>133</u>
Retirement and severance benefits recognized in the consolidated balance sheets	¥ <u>(3,456)</u>	¥ <u>(3,396)</u>	\$ <u>(30,584)</u>

The components of net periodic benefit costs for the years ended September 30, 2005 and 2004 were as follows:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2004</u>	<u>2005</u>
Service cost	¥ 322	¥ 308	\$ 2,850
Interest cost	164	177	1,451
Expected return on plan assets	(25)	(31)	(221)
Amortization:			
Actuarial losses	15	20	133
Net transition asset (liability)	6	(26)	53
Contribution to defined contribution plans	<u>23</u>	<u>75</u>	<u>203</u>
Net periodic benefit costs	¥ <u>505</u>	¥ <u>523</u>	\$ <u>4,469</u>

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Assumptions used in accounting for retirement benefits for the years ended September 30, 2005 and 2004 are as follows:

	2005	2004
Method of attributing benefit to period of service	straight-line basis	straight-line basis
Discount rate	2.0% ~ 4.8%	2.4% ~ 4.8%
Expected return on plan assets	4.0% ~ 7.0%	4.0% ~ 7.0%
Amortization period for actuarial gains or losses	15 years	15 years
Amortization period for net transition liability	15 years	15 years

(7) Income Taxes

The Company and its domestic subsidiaries are subject to a number of taxes based on earnings which, in the aggregate, resulted in an average normal tax rate of approximately 40.7% and 42.5% for the years ended September 30, 2005 and 2004 respectively.

The effective tax rates for the year ended September 30, 2005 and 2004 differ from the normal tax rates for the following reasons:

	2005	2004
Normal tax rate:	40.7 %	42.5 %
Expenses not deductible for tax purposes	1.7	4.8
Per capita taxes	1.6	7.2
Tax rate differentials of overseas subsidiaries	16.0	20.4
Foreign tax credit	-	(36.9)
Change in valuation allowance allocated to income tax expenses	(41.6)	(131.9)
Adjustments of deferred income taxes for enacted changes in tax laws and rates	-	37.5
Other	3.7	1.8
Effective tax benefit rates	22.1 %	(54.6) %

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The components of the temporary differences that gave rise to significant portions of the deferred tax assets and liabilities at September 30, 2005 and 2004 are as follows:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2004</u>	<u>2005</u>
Net operating losses	¥ 11,989	¥ 12,019	\$ 106,097
Retirement and severance benefits	922	880	8,159
Reserves, primarily warranty and inventory	967	1,240	8,558
Gross deferred tax assets	<u>13,878</u>	<u>14,139</u>	<u>122,814</u>
Valuation allowance	<u>(12,865)</u>	<u>(13,267)</u>	<u>(113,849)</u>
Total deferred tax assets	<u>1,013</u>	<u>872</u>	<u>8,965</u>
Accumulated depreciation	295	362	2,611
Percentage of completion	106	123	938
Other	219	175	1,938
Gross deferred tax liabilities	<u>620</u>	<u>660</u>	<u>5,487</u>
Net deferred tax assets	<u>¥ 393</u>	<u>¥ 212</u>	<u>\$ 3,478</u>

Total net deferred tax assets and liabilities shown above include current and noncurrent elements.

The net change in the total valuation allowance for the years ended September 30, 2005 and 2004 was a decrease of ¥402 million (\$3,558 thousand) and of ¥201 million, respectively. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making the assessment. Valuation allowances have been established primarily for deferred tax assets relating to future utilization of net operating loss carryforwards in various taxing jurisdictions. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the periods in which those temporary differences become deductible. Based upon projections for future taxable income in the various taxing jurisdictions, management believes that the certain portions of the deferred tax assets have not been met the more likely than not criteria for realization of these deferred tax assets.

At September 30, 2005, the Company had net operating loss carryforwards available of approximately, ¥16,054 million (\$142,071 thousand) expiring in 2010.

HOSOKAWA MICRON CORPORATION AND CONSOLIDATED SUBSIDIARIES

Notes to Consolidated Financial Statements

September 30, 2005 and 2004

At September 30, 2005, Hosokawa Micron International Inc., a subsidiary of the Company in the United States, had United States net operating loss carryforwards available of approximately ¥10,358 million (\$91,664 thousand) expiring between the years 2008 and 2025. Foreign subsidiaries, other than those in the United States, also had foreign net operating loss carryforwards amounting to ¥2,119 million (\$18,752 thousand) available for local tax purposes, a significant portion of which is not subject to expiration.

(8) Stockholders' Equity

Under the Commercial Code of Japan, the entire amount of the issue price of shares is required to be accounted for as capital, although a company may, by resolution of its Board of Directors, account for an amount not exceeding one-half of the issue price of the new shares as additional paid-in capital, which is included in capital surplus.

The Commercial Code provides that an amount equal to at least 10% of appropriations paid in cash shall be appropriated and set aside as a legal earnings reserve until the total amount of legal earnings reserve and additional paid-in capital equals to 25% of common stock. The legal earnings reserve and additional paid-in capital may be used to eliminate or reduce a deficit by resolution of the stockholders' meeting or may be capitalized by resolution of the Board of Directors. On condition that the total amount of legal earnings reserve and additional paid-in capital remains being equal to or exceeding 25% of common stock, they are available for distribution by resolution of the stockholders' meeting. The legal earnings reserve is included in retained earnings in the accompanying financial statements.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Commercial Code.

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(9) Research and Development Costs

Research and development expenditure is charged to income when incurred. Research and development costs charged to income for the years ended September 30, 2005 and 2004 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2004
Research and development costs	¥ 834	¥ 838	\$ 7,381

(10) Leases

The Company and its domestic subsidiaries account for leases as operating leases, except those in which ownership is deemed to be transferred to the lessee.

The following pro-forma amounts represent the acquisition costs and accumulated depreciation as of September 30, 2005 and 2004, which would have been reflected in the consolidated balance sheets if finance lease accounting had been applied to these leases.

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Machinery and equipment:			
Acquisition cost	¥ 418	¥ 396	\$ 3,699
Accumulated depreciation	(230)	(168)	(2,035)
	188	228	1,664
Furniture and fixtures:			
Acquisition cost	342	384	3,027
Accumulated depreciation	(201)	(207)	(1,779)
	141	177	1,248
	¥ 329	¥ 405	\$ 2,912

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Future lease payments at September 30, 2005, which include the portion of interest thereon, are as follows:

	<u>Millions of yen</u>	<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2005</u>
Due within one year	¥ 109	\$ 965
Due after one year	220	1,947
	¥ 329	\$ 2,912

The amount of lease payments and depreciation costs at September 30, 2005 and 2004 consist of the following:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2005</u>	<u>2004</u>	<u>2005</u>
Lease payments	¥ 126	¥ 126	\$ 1,115
Depreciation costs	126	126	1,115

(11) Investments in Securities

Marketable equity and debt securities included in investments in securities (noncurrent assets), at September 30, 2005 and 2004 are summarized as follows:

				<u>Millions of yen</u>		
				<u>2005</u>		
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized gain, net</u>			
Equity securities	¥ <u>526</u>	¥ <u>717</u>	¥ <u>191</u>			
				<u>2004</u>		
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized gain, net</u>			
Equity securities	¥ <u>467</u>	¥ <u>506</u>	¥ <u>39</u>			
				<u>Thousands of U.S. dollars</u>		
				<u>2005</u>		
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized gain, net</u>			
Equity securities	\$ <u>4,655</u>	\$ <u>6,345</u>	\$ <u>1,690</u>			

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September 30, 2005 and 2004

(12) Foreign Exchange Contracts

Foreign exchange contracts at September 30, 2005 and 2004 are summarized as follows:

		Millions of yen		
		2005		
		<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized loss, net</u>
Forward:				
To buy foreign currencies	¥	685	¥ 662	¥ 23
To sell foreign currencies		20	20	0

		2004		
		<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized gain, net</u>
Forward:				
To buy foreign currencies	¥	649	¥ 653	¥ 4
To sell foreign currencies		45	44	1

		Thousands of U.S. dollars		
		2005		
		<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized loss, net</u>
Forward:				
To buy foreign currencies	\$	6,062	\$ 5,858	\$ 204
To sell foreign currencies		177	177	0

The above amounts exclude contracts entered into in order to hedge receivables and payables denominated in foreign currencies, which have been translated and reflected at the corresponding contracted rates in the accompanying consolidated balance sheets at September 30, 2005 and 2004.

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(13) Supplemental Information to Consolidated Statements of Cash Flows

Reconciliations of cash on hand and at bank shown in the consolidated balance sheets and cash and cash equivalents shown in the consolidated statements of cash flows as of September 30, 2005 and 2004 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Cash on hand and at bank	¥ 3,815	¥ 6,218	\$ 33,761
Cash equivalents included in Securities	409	-	3,620
Deposits pledged as collateral	-	(800)	-
	¥ 4,224	¥ 5,418	\$ 37,381

At September 30, 2005 and 2004, noncash financing activities are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Conversion of convertible type bonds with stock purchase rights into common stock and capital surplus	¥ 2,400	¥ 3,500	\$ 21,239

(14) Contingent Liabilities

At September 30, 2005, contingent liabilities for notes discounted with recourse amounted to ¥ 81 million (\$717 thousand) and for guarantees of loans of affiliates amounted to ¥25 million (\$221 thousand).

Various lawsuits and claims are pending against the Company and its subsidiaries, including product liability suits. Although the outcome of such suits and claims cannot be predicted with certainty, the disposition thereof will not, in the opinion of the management of the Company, result in a material adverse effect on the consolidated financial position of the company, its operating results or cash flows.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(15) Segment Information

Information by segment for fiscal years 2005 and 2004 is shown in the tables below.

(a) By Business Segment

	Millions of yen						
	2005						
	Powder processing equipment	Plastic processing equipment	Air pollution control equipment	Confec- tionery equip- ment	Total	Elimina- tions and corporate items	Consoli- dated total
Sales:							
External sales	¥ 26,406	¥ 5,919	¥ 2,850	¥ 2,976	¥ 38,151	¥ -	¥ 38,151
Intersegment sales	27	-	715	-	742	(742)	-
Total	26,433	5,919	3,565	2,976	38,893	(742)	38,151
Operating expenses	24,730	5,760	3,203	2,784	36,477	120	36,597
Operating profit	¥ <u>1,703</u>	¥ <u>159</u>	¥ <u>362</u>	¥ <u>192</u>	¥ <u>2,416</u>	¥ <u>(862)</u>	¥ <u>1,554</u>
Identifiable assets	¥ 22,379	¥ 7,219	¥ 2,237	¥ 2,837	¥ 34,672	¥ 2,847	¥ 37,519
Depreciation	561	73	104	45	783	70	853
Capital expenditure	320	41	2	11	374	1	375
	2004						
	Powder processing equipment	Plastic processing equipment	Air pollution control equipment	other	Total	Elimina- tions and corporate items	Consoli- dated total
Sales:							
External sales	¥ 24,481	¥ 5,103	¥ 3,121	¥ 2,622	¥ 35,327	¥ -	¥ 35,327
Intersegment sales	-	4	547	-	551	(551)	-
Total	24,481	5,107	3,668	2,622	35,878	(551)	35,327
Operating expenses	23,331	4,958	3,238	2,499	34,026	316	34,342
Operating profit	¥ <u>1,150</u>	¥ <u>149</u>	¥ <u>430</u>	¥ <u>123</u>	¥ <u>1,852</u>	¥ <u>(867)</u>	¥ <u>985</u>
Identifiable assets	¥ 21,842	¥ 7,831	¥ 2,380	¥ 2,516	¥ 34,569	¥ 6,641	¥ 41,210
Depreciation	607	74	105	41	827	73	900
Capital expenditure	285	38	-	3	326	43	369

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

	Thousands of U.S. dollars						
	2005						
	Powder processing equipment	Plastic processing equipment	Air pollution control equipment	Confec- tionery equip- ment	Total	Elimina- tions and corporate items	Consoli- dated total
Sales:							
External sales	\$ 233,681	\$ 52,381	\$ 25,221	\$ 26,336	\$ 337,619	\$ -	\$ 337,619
Intersegment sales	239	-	6,327	-	6,566	(6,566)	-
Total	233,920	52,381	31,548	26,336	344,185	(6,566)	337,619
Operating expenses	218,849	50,974	28,345	24,637	322,805	1,062	323,867
Operating profit	\$ 15,071	\$ 1,407	\$ 3,203	\$ 1,699	\$ 21,380	\$ (7,628)	\$ 13,752
Identifiable assets	\$ 198,044	\$ 63,885	\$ 19,797	\$ 25,106	\$ 306,832	\$ 25,195	\$ 332,027
Depreciation	4,965	646	920	398	6,929	620	7,549
Capital expenditure	2,832	363	18	97	3,310	9	3,319

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(b) By Geographical Location

Millions of yen							
2005							
	Location					Elimina- tions and corporate items	Consoli- dated total
	Japan	Americas	Europe	Asia	Total		
Sales:							
External sales	¥ 15,199	¥ 5,309	¥ 17,527	¥ 116	¥ 38,151	¥ -	¥ 38,151
Intersegment sales	84	58	3,006	60	3,208	(3,208)	-
Total	15,283	5,367	20,533	176	41,359	(3,208)	38,151
Operating expenses	13,240	5,583	19,884	177	38,884	(2,287)	36,597
Operating profit (loss)	¥ <u>2,043</u>	¥ <u>(216)</u>	¥ <u>649</u>	¥ <u>(1)</u>	¥ <u>2,475</u>	¥ <u>(921)</u>	¥ <u>1,554</u>
Identifiable assets	¥ 13,602	¥ 3,147	¥ 16,341	¥ 78	¥ 33,168	¥ 4,351	¥ 37,519
2004							
	Location					Elimina- tions and corporate items	Consoli- dated total
	Japan	Americas	Europe	Asia	Total		
Sales:							
External sales	¥ 13,301	¥ 4,713	¥ 17,195	¥ 118	¥ 35,327	¥ -	¥ 35,327
Intersegment sales	76	47	2,413	45	2,581	(2,581)	-
Total	13,377	4,760	19,608	163	37,908	(2,581)	35,327
Operating expenses	11,658	4,844	19,313	162	35,977	(1,635)	34,342
Operating profit (loss)	¥ <u>1,719</u>	¥ <u>(84)</u>	¥ <u>295</u>	¥ <u>1</u>	¥ <u>1,931</u>	¥ <u>(946)</u>	¥ <u>985</u>
Identifiable assets	¥ 13,368	¥ 3,611	¥ 16,053	¥ 111	¥ 33,143	¥ 8,067	¥ 41,210

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

Thousands of U.S. dollars							
2005							
	Location					Elimina- tions and corporate items	Consoli- dated total
	Japan	Americas	Europe	Asia	Total		
Sales:							
External sales	\$ 134,504	\$ 46,982	\$ 155,106	\$ 1,027	\$ 337,619	\$ -	\$ 337,619
Intersegment sales	<u>743</u>	<u>513</u>	<u>26,602</u>	<u>531</u>	<u>28,389</u>	<u>(28,389)</u>	<u>-</u>
Total	<u>135,247</u>	<u>47,495</u>	<u>181,708</u>	<u>1,558</u>	<u>366,008</u>	<u>(28,389)</u>	<u>337,619</u>
Operating expenses	<u>117,168</u>	<u>49,407</u>	<u>175,965</u>	<u>1,566</u>	<u>344,106</u>	<u>(20,239)</u>	<u>323,867</u>
Operating profit (loss)	<u>\$ 18,079</u>	<u>\$ (1,912)</u>	<u>\$ 5,743</u>	<u>\$ (8)</u>	<u>\$ 21,902</u>	<u>\$ (8,150)</u>	<u>\$ 13,752</u>
Identifiable assets	\$ 120,372	\$ 27,850	\$ 144,611	\$ 690	\$ 293,523	\$ 38,504	\$ 332,027

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(c) *Overseas Sales*

Millions of yen				
2005				
	Americas	Europe	Asia	Total
Overseas sales	¥ 7,360	¥ 12,856	¥ 4,690	¥ 24,906
Ratio of overseas sales to consolidated sales	19.3%	33.7%	12.3%	65.3%
2004				
	Americas	Europe	Asia	Total
Overseas sales	¥ 6,478	¥ 12,411	¥ 5,003	¥ 23,892
Ratio of overseas sales to consolidated sales	18.3%	35.1%	14.2%	67.6%
Thousands of U.S. dollars				
2005				
	Americas	Europe	Asia	Total
Overseas sales	\$ 65,133	\$ 113,770	\$ 41,504	\$ 220,407
Ratio of overseas sales to consolidated sales	19.3%	33.7%	12.3%	65.3%

Note: (1) Overseas sales are sales to countries outside of Japan by the Company and consolidated subsidiaries.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2005 and 2004

(16) Related Party Transactions

The transactions of the Company with its related parties are as follows:

Name of Related Parties • Status • Equity ownership percentage by the Company	Millions of yen		Notes
	Transactions made during the year ended September 30, 2004		
	Description of transactions	Amounts	
Masuo Hosokawa Main Personal Stockholder Honorary Chairman of Hosokawa Micron Corporation 10.52%	Underwriting of capital stock	¥ 564	(1)
Fukiko Sawamura Main Personal Stockholder Daughter of Masuo Hosokawa 0.27%	Underwriting of capital stock	¥ 56	(1)
Yukiko Hosokawa Main Personal Stockholder Daughter of Masuo Hosokawa 0.27%	Underwriting of capital stock	¥ 56	(1)
Toho Sangyo Corp. Main Corporate Stockholder 8.07%	Warehouse and office rent	¥ 4	(2)
	Expense reimbursement	¥ 5	
Hosokawa Enterprise Co., Ltd. Main Corporate Stockholder The majority of voting rights held by Main Personal Stockholder 0%	Lease fee for cars and equipment	¥ 123	(3)
	Expense reimbursement	¥ 15	

**HOSOKAWA MICRON CORPORATION
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Notes to Consolidated Financial Statements

September 30, 2005 and 2004

Name of Related Parties • Status • Equity ownership percentage by the Company	Millions of yen			Notes
	Transactions made during the year ended September 30, 2004			
	Description of transactions	Amounts	Amounts	
Juno International Co., Ltd. Main Corporate Stockholder The majority of voting rights held by Main Personal Stockholder 0%	Purchase of coffee beans, etc.	¥	3	(4)

- Notes: 1. Terms and conditions for underwriting of capital stock have been determined on an arm's length basis.
2. Terms and conditions for leases on warehouses and offices rooms have been determined on an arm's length basis and by reference to normal market price levels.
3. Terms and conditions for leases on cars and equipment have been determined on an arm's length basis and by reference to normal market price levels by comparison with estimation from other third parties.
4. Terms and conditions for purchase of coffee beans have been determined on an arm's length basis and by reference to normal market price levels.

The transactions of the Hosokawa Micron Corporation with its related parties are as follows;

Name of Related Parties • Status • Equity ownership percentage by the Company	Millions of yen		Thousands of U.S. dollars		Notes
	Transactions made during the year ended September 30, 2005		Transactions made during the year ended September 30, 2005		
	Description of transactions	Amounts	Amounts	Amounts	
Masuo Hosokawa Main Personal Stockholder Honorary Chairman of Hosokawa Micron Corporation 9.81%	Redemption of Bond	¥ 800	\$	7,080	(1)
Masuo Hosokawa Main Personal Stockholder Chairman of Hosokawa Powder Technology Foundation 0%	Redemption of Bond	¥ 1,200	\$	10,619	(1)

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2005 and 2004

Name of Related Parties • Status • Equity ownership percentage by the Company	Millions of yen		Thousands of U.S. dollars		Notes
	Transactions made during the year ended September 30, 2005		Transactions made during the year ended September 30, 2005		
	Description of transactions	Amounts	Amounts	Amounts	
Toho Sangyo Corp. Main Corporate Stockholder 8.07%	Warehouse and offices rent	¥ 3	\$ 27		(2)
	Expense reimbursement	¥ 5	\$ 44		
	Purchase of coffee beans, etc.	¥ 0	\$ 0		(4)
Hosokawa Enterprise Co., Ltd. Main Corporate Stockholder The majority of voting rights held by Main Personal Stockholder 0%	Lease fee for cars and equipment	¥ 116	\$ 1,027		(3)
	Expense reimbursement	¥ 13	\$ 115		
Juno International Co., Ltd. Main Corporate Stockholder The majority of voting rights held by Main Personal Stockholder 0%	Purchase of coffee beans, etc.	¥ 1	\$ 9		(4)

Juno International Co., Ltd. was liquidated at August 29, 2005 and its business was transferred to the food sales division of Toho Sangyo Corp.

- Notes: 1. Terms and conditions for underwriting of the bond have been determined on an arm's length basis and by reference to normal market interest levels.
2. Terms and conditions for leases on warehouses and office rooms have been determined on an arm's length basis and by reference to normal market price levels.

**HOSOKAWA MICRON CORPORATION
AND CONSOLIDATED SUBSIDIARIES**

Notes to Consolidated Financial Statements

September 30, 2005 and 2004

3. Terms and conditions for leases on cars and equipment have been determined on an arm's length basis and by reference to normal market price levels by comparison with estimations from other third parties.
4. Terms and conditions for purchase coffee beans have been determined on an arm's length basis and by reference to normal market price levels.

(17) Subsequent Event

The number of shares outstanding increased by 368,505 on October 6, 2005 due to the exercise of ¥300 million worth of the third unsecured convertible type bonds with stock purchase rights.

The number of shares outstanding increased by 982,680 on November 25, 2005 due to the exercise of ¥800 million worth of the third unsecured convertible type bonds with stock purchase rights.

The number of shares outstanding increased by 1,842,525 on December 13, 2005 due to the exercise of ¥1,500 million worth of the third unsecured convertible type bonds with stock purchase rights.

**HOSOKAWA MICRON CORPORATION
AND SUBSIDIARIES**

Consolidated Performance Evaluation

September 30, 2005, 2004, 2003, 2002 and 2001

Index	Fiscal Year	2001	2002	2003	2004	2005
	Unit					
Sales	Millions of yen	41,157	36,452	28,564	35,327	38,151
Income(loss) from continuing operations	Millions of yen	638	(1,139)	(198)	184	1,395
Net income(loss) for the year	Millions of yen	45	(5,061)	(5,099)	407	825
Net assets (= Shareholders' Equity)	Millions of yen	16,955	12,005	7,594	14,181	17,298
Gross assets	Millions of yen	54,196	48,091	40,072	41,210	37,519
Net assets worth	Yen	607.64	441.71	279.90	381.59	433.66
Net income(loss) worth	Yen	1.63	(184.54)	(187.80)	14.52	20.98
Adjusted net income worth	Yen	-	-	-	14.11	19.81
Pre tax income(loss) to sales ratio	Yen	4.2	(14.1)	(14.2)	0.7	2.7
Stockholder's equity to total capital ratio	%	31.3	25.0	19.0	34.4	46.1
Net income to shareholder's equity ratio	%	0.3	(42.2)	(67.1)	2.9	4.8
Net income to stock price ratio	Yen	331.3	-	-	34.9	43.1
Current assets	Millions of yen	25,762	21,477	21,773	23,260	20,105
Current liabilities	Millions of yen	25,490	28,471	22,171	19,315	12,389
Current ratio	%	101.1	75.4	98.2	120.4	162.3
Noncurrent liabilities	Millions of yen	11,636	7,552	10,153	7,385	7,519
Debt ratio	%	219.0	300.1	425.7	188.3	115.1
Cash flows from operating activities	Millions of yen	(771)	2,335	(271)	2,465	2,890
Cash flows from investing activities	Millions of yen	(377)	(1,327)	(306)	2,252	379
Cash flows from financial activities	Millions of yen	(1,760)	(1,957)	(1,163)	(2,012)	(4,517)
Cash and cash equivalent at end of year	Millions of yen	5,470	4,551	2,726	5,418	4,224
Employee	Persons	1,920	1,836	1,327	1,617	1,522

Major Subsidiaries and Divisions

(As of October 1, 2005)

Country	Name	Principal Business
Japan	Hosokawa Powder Technology Research Institute	Research of Nano Particle Technology, Development of Powder Processing System, Measurement and Toll Processing
	Wagner Hosokawa Micron Ltd.	Sales of powder coating equipment
	Hosokawa Alpine AG Japan Branch	Sales of blown film equipment / systems
Asia		
China	Hosokawa Micron(Shanghai) Powder Machinery Co., Ltd.	Sales of powder processing equipment / systems
Korea	Hosokawa Micron (Korea) Ltd.	Sales of powder processing equipment / systems
Malaysia	Hosokawa Micron (Malaysia) Sdn. Bhd.	Sales of powder processing equipment / systems
Americas		
U.S.A.	Hosokawa Micron International Inc.	
(Division)	(Hosokawa Micron Powder Systems)	Manufacture and sales of powder processing equipment / systems
	(Hosokawa Alpine American)	Sales of blown film processing equipment / systems
	(Hosokawa Polymer Systems)	Manufacture and sales of plastic granulating equipment
Canada	Hosokawa Micron Ltd.	Sales of powder processing equipment / systems
Mexico	Hosokawa Micron de Mexico SA de CV	Sales of powder and thermal processing systems
Europe		
Germany	Hosokawa Alpine AG	Manufacture and sales of powder processing equipment / systems and blown film processing equipment / systems
	Hosokawa Micron GmbH	Manufacture and sales of powder processing equipment and Toll Processing
	Hosokawa Bepex GmbH	Manufacture and sales of powder processing / systems and confectionery equipment/systems
Netherlands	Hosokawa Finance International B.V.	Financing
	Hosokawa Micron B.V.	Manufacture and sales of powder and thermal processing Equipment / systems
	Hosokawa Ter Braak B.V.	Manufacture and sales of confectionery equipment / systems
U.K.	Hosokawa Micron Ltd.	Manufacture and sales of powder processing equipment and containment systems
Spain	Hosokawa Micron Espana S.A.	Sales of powder processing equipment / systems

Board of Directors
(As of February 13, 2006)

Hosokawa Micron Corporation

President

Masuo Hosokawa * Chief Executive Officer

Vice President

Kiyomi Miyata * Chief Operating Officer

Senior Director

Takamichi Yasuoka Director of Japan Operation

Directors

Kiyoshi Nogi Chief Technology Officer
(Director of “Hosokawa Powder Technology Research Institute”)
(Professor, Joining and Welding Research Institute of Osaka University)

Takashi Arakawa Division Director of General Affairs Division and Director of Hirakata Office

Hitoshi Kihara Director of International Operations and Division Director of International Management and Sales Division

Shouzo Maede Division Director of Powder Processing Systems Division

Tadamichi Fukunaga Division Director of Clean Air and Environmental Protection Division

Makio Naito (Professor, Smart Processing Research Center, Joining and Welding Research Institute of Osaka University)

Outside Director

Ichiro Chibata (Ph. D.)

Standing Auditor

Shuntaro Ukita

Auditors

Kiichi Kokubu
Keiichiro Azuta

Executive Officers

Yoshihiro Nakamura Chief Financial Officer and Division Director of Accounting Division

Yasuo Takagi Assistant Division Director of General Affairs Division

Tetsuya Inoue Assistant Division Director of Accounting Division

Minoru Yoshida Director of Tokyo Branch

Mitsuru Imachi Division Director of After Sales Service Division

Arata Yokoyama Assistant Division Director of Powder Processing System Division

Tadami Hanakawa Assistant Division Director of Powder Processing System Division

Yoshinori Uchida President of Americas Operation and Assistant Division Director of International Management and Sales Division

*Representative Director



HOSOKAWA MICRON CORPORATION

Investor Information
(As of September 30, 2005)

Year of Incorporation
1916

Common Stock
¥ 13,193 Million

Common Stock
Par Value ¥50
Authorized 99,347,000 shares
Issued 39,881,640 shares

Number of Shareholders
7,404

Securities Traded
Tokyo Stock Exchange (First Section)
Osaka Securities Exchange (First Section)

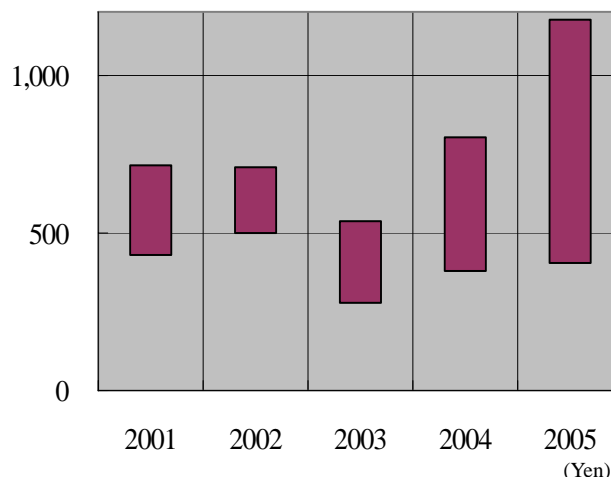
Independent Auditors
Shin Nihon & Co.
AZUSA & Co.

Transfer Agent
The Mitsubishi UFJ Trust & Banking Co., Ltd

Further Information
For further information, please contact Accounting Division of Hosokawa Micron Corporation

Address: 9, 1-chome, Shoudai Tajika, Hirakata-shi, Osaka 573-1132, Japan
Telephone: 81-72-855-2225
URL: <http://www.hosokawamicron.co.jp/>

Common Stock Price Range
FY2001-2005



	2001	2002	2003	2004	2005
Highest	712	705	538	802	1,174
Lowest	430	499	280	380	407

HOSOKAWA MICRON CORPORATION and its Representative offices Directory

Hirakata Corporate Office & Hirakata Plant

9, 1-chome, Shoudai Tajika, Hirakata-shi,
Osaka 573-1132, Japan
Tel: 81-72-855-2226
Fax: 81-72-855-2410

Nara Plant

9-3 Nara Industrial Estimate, Techno-Park-Nara,
Sumikawa-cho, Gojo-shi, Nara 637-0014, Japan
Tel: 81-7472-6-3960
Fax: 81-7472-6-3970

Tsukuba Office

2345-1, Higashida, Shinozaki, Tsukuba-shi,
Ibaraki 300-0873, Japan
Tel: 81-298-64-3961
Fax: 81-298-64-8822

Tokyo Branch

Itabashi Center Bldg., 9-7, 3-chome, Itabashi,
Itabashi-ku, Tokyo, 173-0004, Japan
Tel: 81-3-5248-5730
Fax: 81-3-5248-5737

Kashiwa Office

472, Nakatoyofuta, Kashiwa-shi, Chiba
277-0873, Japan
Tel: 81-4-7131-6612
Fax: 81-4-7132-2516

Other Sales Offices (Japan)

Toukai, Shimonoseki, Fukuoka



HOSOKAWA MICRON CORPORATION

Hosokawa Micron Corporation is a member of the Hosokawa Micron Group, responding to global needs through emphasis on materials science and engineering. The Group is an international provider of equipment and technology for powder and particle processing, plastic processing and confectionery products. The Group maintains facilities for research, engineering, manufacturing and service in each of the world's major industrial market.

(0604PC1)