



namco[®]

FINANCIAL STATEMENTS

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Profile

Namco Limited has been engaged in the amusement business for more than 40 years and is a world leader in the R&D, production and sales of coin-operated game machines and home video-game software, as well as in amusement facility operations. The Company has set the year 2001 as the starting point for a renewed Namco—one that will focus on creating services that fuse digital media with a spirit of adventure under the theme of “High Touch Digital Entertainment.”

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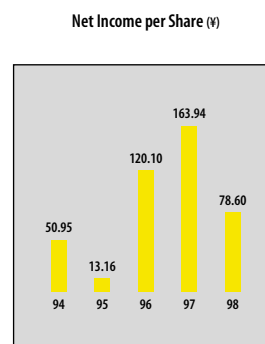
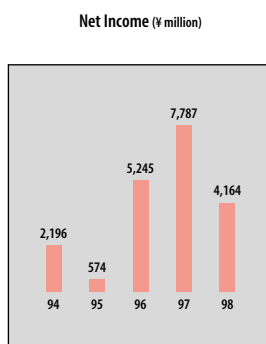
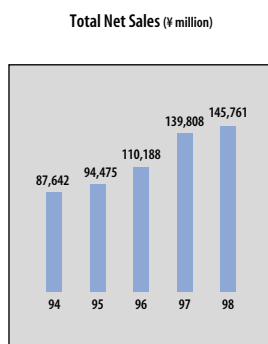


Six-Year Summary

NAMCO LIMITED AND SUBSIDIARIES
YEARS ENDED 31ST MARCH

	Millions of yen						Thousands of U.S. dollars
	1993	1994	1995	1996	1997	1998	1998
For the year:							
Total net sales	¥74,212	¥ 87,642	¥ 94,475	¥110,188	¥139,808	¥145,761	\$1,026,486
Product and merchandise sales	29,856	37,761	39,764	48,401	64,390	62,176	437,859
Revenues from amusement facility operations	41,227	47,244	50,850	57,463	71,286	78,361	551,838
Restaurant sales	2,845	2,491	2,986	3,195	3,470	4,102	28,887
Royalties	284	146	875	1,129	662	1,122	7,902
Operating income	5,233	5,697	4,011	11,217	14,902	11,772	82,901
Income before income taxes	4,680	5,365	2,668	10,565	15,824	9,337	65,753
Net income	2,038	2,196	574	5,245	7,787	4,164	29,324
Per share of common stock (in yen and U.S. dollars):							
Net income	48.87	50.95	13.16	120.10	163.94	78.60	0.5535
Cash dividends applicable to the year	15.00	16.00	16.00	25.00	30.00	30.00	0.2112
At year-end:							
Shareholders' equity	34,366	41,585	41,238	45,882	76,110	84,355	594,049
Total assets	93,725	100,572	125,932	139,181	141,492	142,992	1,006,986
Number of shares outstanding (thousands):							
	41,700	43,644	43,660	43,716	51,544	53,625	

Note: U.S. dollar amounts have been translated, for convenience only, at the exchange rate of ¥142=U.S.\$1.



Family Bowl



Time Crisis II



Motocross Go!



Namco has achieved notable success with sports simulation games equipped with next-generation System 23 for real-time, three-dimensional computer graphics. *Motocross Go!*, for example, provides the excitement of motocross racing without the dirt or the danger. The game offers three courses—novice, intermediate and advanced—and players develop such riding skills as cornering and jumping. These techniques must be mastered to win the race.

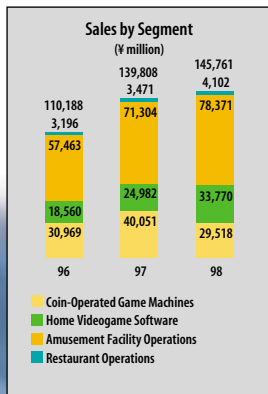
Rapid River



Final Furlong



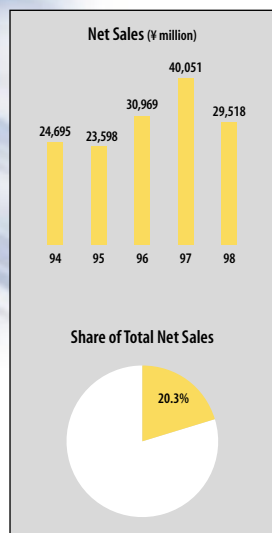
Management's Discussion and Analysis



Major Consolidated Companies

Namco Holding Corp.
 Namco America Inc.
 Namco Hometek Inc.
 Namco Cyberentertainment Inc.
 XS Entertainment Inc.
 Namco Europe Ltd.
 Namco Ireland Ltd.
 Namco Operations Europe Ltd.
 Namco Operations Spain S.L.
 Namco Operations France S.A.
 Namco Operations Germany GmbH
 Namco Operations F.E.C. Israel Ltd.
 Namco Enterprises Asia Ltd.
 Happiland Singapore Private Ltd.
 JPN-Namco Taiwan Co., Ltd.
 Italian Tomato Ltd.
 I&K Co., Ltd.
 T&E Co., Ltd.

Coin-Operated Game Machines



Scope of Consolidation

In accordance with generally accepted accounting principles in Japan, the consolidated financial statements include the accounts of Namco Limited and its 20 major subsidiaries. Of these, one company, XS Entertainment Inc., was newly established and included in consolidation for the first time in the fiscal year ended March 31, 1998. In addition, one subsidiary and four affiliated companies are included in consolidation through the use of the equity method. Two companies, Dream Pictures Studio Inc. and Dream Pictures Studio U.S.A. Inc., were accounted for using the equity method for the first time during the term.

Business Environment

The Japanese economy was adversely affected by stagnant consumer spending, a slowdown in private-sector capital investment and growing concerns over the financial system. Economic weakness was compounded by repercussions of the currency crisis in Asia, leading to a harsh business climate.

Overseas, the U.S. economy continued on a path of robust growth, supported mainly by domestic demand. Although economic activity in Europe turned upward, performance in Asia was marked by a substantial deceleration in growth as a result of currency and economic turmoil in the region.

Hardware and software developed by Japanese companies play a central role in world markets for amusement arcades and home videogames, and the global marketplace, led by Japan, is becoming increasingly integrated. During the term, demand for coin-operated game machines was depressed by restrained capital investment by arcade operators in Japan, the United States and Europe. Moreover, economic turmoil resulted in falling exports to Asian markets. In the home videogame market, consumers continued to respond favorably to attractive new titles in major markets.

Analysis of Sales

Consolidated net sales rose 4.3% to ¥145,761 million, supported by record-high sales in the home videogame software segment and growth in amusement facility and restaurant operations. Sales in coin-operated game machines, however, declined sharply as a result of unfavorable conditions in Japan and overseas.

Overseas sales edged up 1.7% to ¥50,552 million, accounting for 34.7% of total net sales, compared with 35.6% during the previous term. Domestic sales grew 5.7% to ¥95,209 million, or 65.3% of the total.

Coin-Operated Game Machines

Namco targets opportunities in the world marketplace for amusement game machines with integrated operations from development to manufacturing and marketing. The parent company markets products in Japan, other Asian markets and Oceania. Namco America Inc. of the United States and Namco Europe Ltd., based in the United Kingdom, are responsible for North American and European markets, respectively.

During the fiscal year under review, Namco's definitive hand-to-hand combat game *Tekken 3* recorded outstanding performance throughout world markets, with accumulated sales breaking the 36,000 unit mark. Amid harsh conditions in the domestic market, the horseracing simulation game *Final Furlong* stood apart in the market as a major hit. The whitewater rafting game *Rapid River* and the motocross simulation game *Motocross Go!*, equipped with our next-generation



Namco proved its ability to reproduce the excitement of the *Tekken 3* arcade game on the PlayStation console. With sharper graphics, faster gameplay, more moves, secret modes and exclusive new characters for PlayStation, *Tekken 3* became an immediate hit with domestic sales hitting the one million mark. Namco plans to release the title on overseas markets during the current term.

KLONOA



Time Crisis



KLONOA



Tekken 3



Tales of Destiny

Tales of Destiny



System 23 for real-time, three-dimensional computer graphics, also attracted considerable attention in the marketplace. However, with arcade operators in major world markets scaling back their capital investment programs, unit sales were stagnant. Namco Europe Ltd. turned in especially weak results, with sales on the European continent adversely impacted by the appreciation of the pound sterling. Exports to Asia declined owing to the unfolding financial crisis.

Namco stepped up marketing activities in a wide range of game machines including the following: *Star Audition*, adapted from a popular attraction at the Namco Wonder Eggs 2 theme park; *Beauty Club*, which allows users to make photographic seals with a variety of simulated hair styles; the quiz game *Kosodate Quiz, My Angel*; and the prize game *Sweet-Go-Round*.

In other initiatives, the Company began exclusive marketing of *New Japan Pro Wrestling Match*, jointly developed with Tomy Company, Ltd., and *EHRGEIZ*, a hand-to-hand combat simulation game jointly developed with Square Co., Ltd. Both of these games are based on Namco's System 12 for advanced three-dimensional computer graphics.

Despite these efforts, severe market conditions and the delay of new game releases into the current term led to a 26.3% decline in net sales for the segment to ¥29,518 million, or 20.3% of net sales, compared with 28.6% in the previous term.

Home Videogame Software

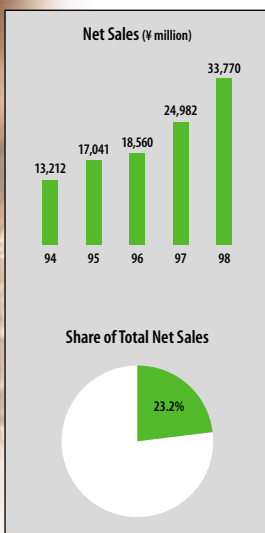
Namco's home videogame software operations are organized to fully consider the cultural, geographic and timing differences of world markets. The Company's bases in Japan and the United States develop and produce software for local markets and for export to Europe and Asia. Development efforts, centered on titles for Sony's PlayStation, the dominant platform in world markets, are engaged in both the adaptation of popular arcade games for home use and the creation of original titles.

During the fiscal year under review, the Company aggressively marketed games in world markets, including the aerial combat game *Ace Combat 2* and the shooting simulation *Time Crisis*. A special shooting accessory, Guncon, was also launched for use with home videogame systems and recorded sales in excess of 1.5 million units.

In Japan, *Tekken 3* was launched ahead of its overseas release to become a major hit with sales reaching one million units during the term. Titles developed originally for the home market included the role-playing game *Tales of Destiny*, which sold more than 800,000 units and made a solid contribution to sales. The fantasy action game *KLONOA* also earned a strong reputation in the marketplace. For the NINTENDO 64 platform, Namco released *Famista 64*, a version of its highly popular professional baseball game, *Family Stadium*. Also during the term, the Company introduced and began the full-scale marketing of a new book that discusses gaming techniques and other issues. *Namco History*, a compilation of past hits, was released for personal computers. The Company also began licensing operations for character goods based on its software titles.

In the United States, such titles as *Tekken 2*, *Soul Blade* (the overseas version of *Soul Edge*), *Rage Racer*, *Ace Combat 2* and *Time Crisis* recorded favorable performance. Namco Hometek Inc., a publisher of exclusive game software titles, released the adventure game *Treasures of the Deep* and continued to market *Pac-Man*, the long-time best seller for Nintendo's Game Boy.

Home Videogame Software

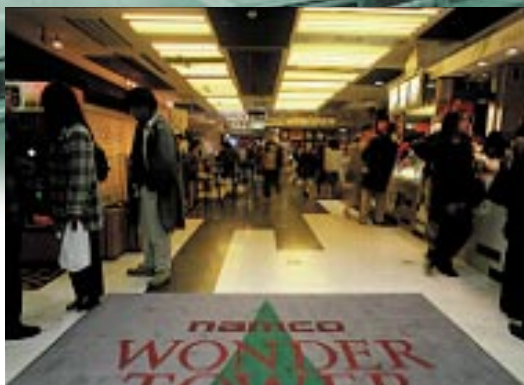




INTI Shibuya is located in a stylish area of Tokyo frequented by active, style-conscious consumers. INTI means "sun," and comes from the ancient language of the Incas. The concept is based on providing a new form of entertainment for young adults that combines amusement facilities with a dining bar in a classic atmosphere suitable for the information age.



Namco NamjaTown

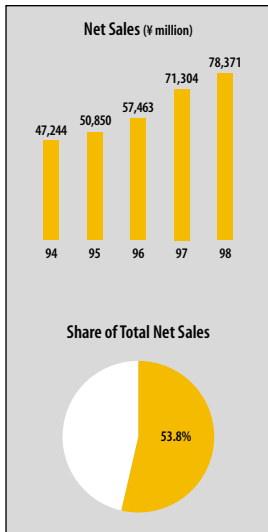


Namco Wonder Tower



Wonder Bowl

Amusement Facility Operations



In Europe, along with strong sales of *Soul Blade*, *Rage Racer* and *Tekken 2*, running royalties on licenses granted at the time of the Company's market entry were up sharply.

These initiatives supported net sales for the segment of ¥33,770 million, an all-time high and 35.2% above the previous term. The segment accounted for 23.2% of net sales, an increase of 5.3 percentage points.

Amusement Facility Operations

In Japan, Namco had 1,674 facilities at fiscal year-end comprising 452 directly managed arcades, two theme parks and 1,220 facilities where the Company's amusement machines were operated under revenue sharing arrangements.

The term marked the beginning of full-scale, nationwide development of Namco Wonder City, a multifunctional entertainment format, and Namco Wonder Park, an indoor amusement park format designed to be a key tenant of shopping centers. The Company also opened directly managed multifunctional outlets that combine amusement facilities with bowling and "iceless" ice skating.

Major outlets established during the term included Namco Wonder City complexes in Nagoya and in Minami-Kumamoto (Kyushu), Namco Wonder Parks in Imabari and Saijo (Shikoku), and a Namco-Land in Ogawamachi (Kyushu). To target adult consumers, the Company opened INTI in Shibuya, a new form of entertainment that combines amusement with a dining bar.

At the urban theme park Namco Wonder Eggs 2, performance was boosted by special events such as the *Star Audition* talent search and the *Nikotama* Festival, which was held in cooperation with the local community. At the Company's other domestic theme park, Namco NamjaTown, a new theme "town" and a new attraction that simulates spy training were well-received by visitors. Namco NamjaTown has also been included as a site frequented by popular bus tours of Tokyo.

In the United States, Namco Cyberentertainment Inc., the largest arcade operator in the country, filed for Chapter 11 under the federal bankruptcy code to reorganize its operations and create a sound profit and financial structure. Amid declining revenues owing to lower customer traffic at its amusement facilities in shopping malls, the company took this step to lower its fixed costs through the revision of leasing contracts. During the term, operating initiatives were aimed at expanding revenue sharing operations, closing unprofitable facilities and preparing to close other facilities in line with Chapter 11 reorganization.

In Europe, Namco is proceeding with the expansion of its arcade network. Efforts are centered on the cities of London, Islington and Nottingham in the United Kingdom, and in France, where the Company acquired arcades in the city of Nantes. Plans also call for expansion in Germany, Spain and Israel. In London, Namco Station, a large-scale facility in the County Hall, a redeveloped public office, began full-fledged operations during the term. This development is part of a cultural zone on the Thames River, which also features an opera house along with art and historical museums. Other tenants in the County Hall include an aquarium, hotel and restaurants. A national project is underway on an adjacent site to build the world's largest Ferris wheel, and the area promises to become a major entertainment district representative of Europe in the 21st century. At fiscal year-end, Namco had 18 facilities in Europe, including Israel, of which nine were directly managed arcades and nine were amusement facilities where Namco's amusement machines were operated under revenue sharing arrangements.

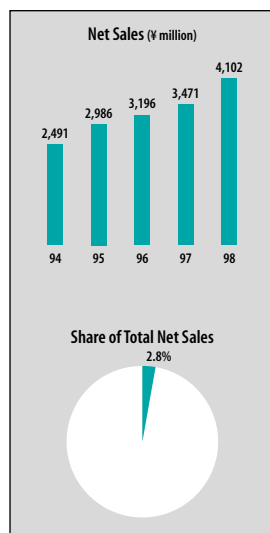


Namco Wonder City

Namco Cybertainment Inc., the largest arcade operator in the United States, is restructuring its operations to improve profitability and create a sounder operating structure. Further, Namco is expanding the number of arcades with Italian Tomato restaurants in Japan, achieving synergies between its restaurant and amusement facility operations.



Restaurant Operations



In Asia, the Company tailored its operations to the conditions of each market. Results in Hong Kong were negatively affected by the economic downturn as a result of the stock market crash and the closing of shopping centers where amusement facilities were located. However, such major facilities as the World Trade Center Namco Wonder Park turned in a favorable performance, and Namco continued efforts to create a sound operating base. In Taiwan, amid tightening regulations concerning amusement facilities, Namco differentiated itself as an operator of family oriented arcades that fully conform with all laws and regulations. Market research is currently underway in ASEAN countries from our base in Singapore. At fiscal year-end, amusement facilities in these three markets totaled 28, comprising 11 directly managed arcades and 17 facilities where Namco's amusement machines were operated under revenue sharing arrangements.

Sales for the segment rose 9.9% to ¥78,371 million, or 53.8% of net sales.

Sales by Segment

(¥ million)

	1996	1997	1998
Coin-Operated Game Machines	¥ 30,969	¥ 40,051	¥ 29,518
Home Videogame Software	18,560	24,982	33,770
Amusement Facility Operations	57,463	71,304	78,371
Restaurant Operations	3,196	3,471	4,102
Total	¥110,188	¥139,808	¥145,761

Overseas Sales*

(¥ million)

	1996	1997	1998
Overseas Sales	¥ 31,831	¥ 49,723	¥ 50,552
Net Sales	110,188	139,808	145,761
Percentage of Net Sales	28.9%	35.6%	34.7%

*Overseas sales include exports and sales by overseas subsidiaries.

Operating Income by Segment

(¥ million)

	1996	1997	1998
Coin-Operated Game Machines	¥ 5,359	¥ 5,907	¥ 2,344
Home Videogame Software	6,907	10,584	12,496
Amusement Facility Operations	2,580	2,237	1,001
Restaurant Operations	19	26	(6)
Elimination	(128)	654	201
Total	¥14,737	¥19,408	¥16,036
Unallocated Administrative Expenses	3,520	4,506	4,264
Operating Income	¥11,217	¥14,902	¥11,772

Namco is building an amusement facility network in China (excluding Hong Kong) through Shanghai Namco Ltd., which is accounted for using the equity method. Geographic penetration was extended beyond the Shanghai area during the term with the opening of a Namco Entertainment World arcade in Guilin, a representative tourist destination in southern China. This brought the number of directly operated arcades in China to nine at fiscal year-end. In April 1998, following the close of the fiscal year, another arcade was opened in Dalian.

The Namco Group's amusement facilities at fiscal year-end totaled 2,253 worldwide, consisting of 826 directly managed arcades, 1,425 facilities where Namco's amusement machines were operated under revenue sharing arrangements and two theme parks.

Restaurant Operations

The business climate for restaurant operations continued to be harsh, adversely impacted by weak consumer spending as a result of a hike in the consumption tax rate and general economic uncertainty. Namco continued its strategy of network expansion. Italian Tomato, a chain of Italian restaurants and cake shops, opened 49 outlets, eight directly managed and 41 franchise outlets. Outlets at fiscal year-end totaled 245, comprising 55 directly managed outlets and 190 franchise outlets. Especially strong network growth was recorded by Italian Tomato Cafe Jr. self-service restaurants operated through a joint venture with KEY COFFEE Inc. New outlets opened during the term totaled 16, bringing the fiscal year-end total to 29 outlets, five of which were directly managed.

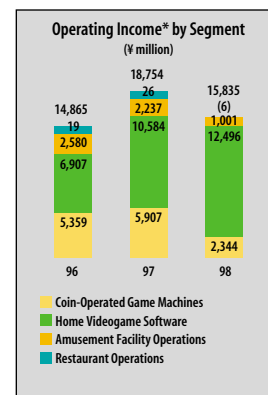
Achieving synergy with arcade operations is an important element of Namco's strategy for network development. Restaurants operated within amusement facilities include Trattoria Italian Tomato Ikebukuro NamjaTown, a cafe in Namco Wonder Eggs 2 and a Karaoke Park Italian Tomato at the Namco Wonder City in Tsurumi. During the term, a cafe was opened at the Namco Wonder City in Minami-Kumamoto.

Restaurant operations recorded sales of ¥4,102 million, an increase of 18.2%.

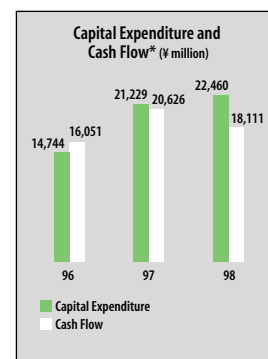
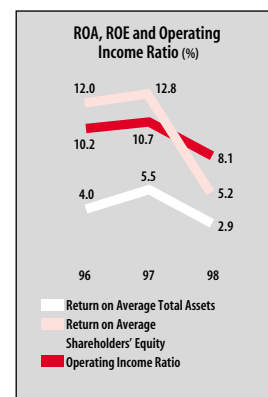
Analysis of Net Income

Total cost of sales was ¥111,771 million, an increase of 8.2%, due primarily to a rise in cost of revenues from amusement facility operations. As a result, the gross profit margin worsened 2.8 percentage points from the previous fiscal year to 23.3%. Selling, general and administrative (SG&A) expenses rose 3.0% to ¥22,218 million. SG&A expenses as a percentage of net sales declined from 15.4% to 15.2%. As a result of the lower gross profit margin, the operating income ratio declined 2.6 percentage points to 8.1%, and operating income fell 21.0% to ¥11,772 million.

By segment (excluding unallocated administrative expenses), the amusement facility operations segment contributed ¥1,001 million to operating income. This was 55.3% below the previous fiscal year's level, reflecting costs related to the reorganization of operations in the United States, high initial investment costs in Europe as a result of network expansion and acquisitions, and adverse market conditions in Asia. Operating income for the coin-operated game machines segment decreased 60.3% to ¥2,344 million, reflecting lower net sales and harsh market conditions. In the home videogame software segment, operating income increased 18.1% to ¥12,496 million, supported by high sales growth of titles for Sony's PlayStation. Restaurant operations recorded an operating loss of ¥6 million, compared with an operating income of ¥26 million in the previous fiscal year,



* Excluding unallocated administrative expenses and eliminations



* Cash flow equals net income plus depreciation and amortisation, minus dividends and bonuses to directors and statutory auditors.

owing to costs related to active network expansion.

Other income decreased 52.4% to ¥973 million, as interest and dividends decreased ¥381 million. Other expenses increased 203.5% to ¥3,408 million. The main factors for this rise were the absence of a ¥1,355 million gain from non-interest bearing convertible bonds, which reduced interest expenses in the previous term, and a ¥734 million loss on closure of amusement facilities, primarily in the United States.

As a result, income before income taxes decreased 41.0% to ¥9,337 million. Income taxes were ¥5,173 million, and the effective tax rate was 55.4% compared with 50.8% during the previous fiscal year. Net income fell 46.5% to ¥4,164 million. The number of shares outstanding at fiscal year-end was 53,625 thousand, an increase of 4.0% from a year earlier as a result of the conversion of convertible bonds. Net income per share of common stock was ¥78.60, compared with ¥163.94 in fiscal 1997. Management maintained cash dividends applicable to the year at ¥30.00 per share.

Analysis of Cash Flows and Financial Position

Net cash provided by operating activities decreased 6.4% to ¥18,774 million. Depreciation and amortisation rose 12.4% to ¥15,979 million.

Net cash used in investing activities was ¥25,373 million, virtually unchanged from the previous fiscal year. Capital expenditure used cash of ¥22,460 million, an increase of 5.8% from the previous fiscal year. This rise reflects aggressive expansion of our arcade networks in Japan and overseas.

There have been no significant fund-raising activities since two convertible bond issues were floated in 1995. During the fiscal year, net cash used in financing activities declined 41.4% to ¥3,672 million, reflecting the absence of ¥5,022 million for the repayment of convertible bonds in the previous fiscal year. Cash dividends paid increased 49.8% to ¥1,832 million, reflecting an increase in the number of shares outstanding.

In aggregate, cash and cash equivalents at end of year decreased 23.3% to ¥33,718 million.

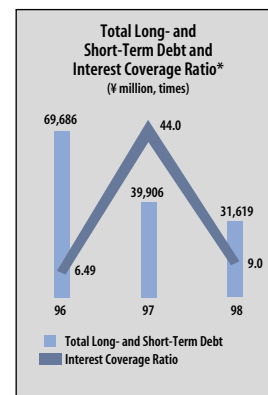
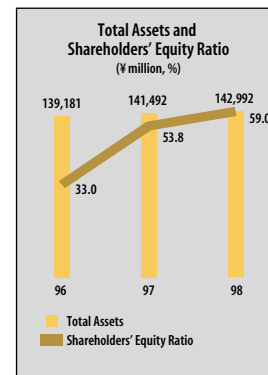
The decrease in cash and cash equivalents led to a 9.9% decline in total current assets to ¥65,513 million. At the same time, total current liabilities climbed 43.5% to ¥43,259 million, and as a result, net working capital decreased 47.8% to ¥22,254 million. The current ratio was 1.5 times, compared with 2.4 times a year earlier.

Net property and equipment increased 13.1% to ¥44,841 million, reflecting the high level of capital investment in amusement facilities. Total other assets rose 12.1% to ¥32,638 million, which reflects an increase of ¥3,194 in leasehold deposits, which were primarily related to expansion of our amusement facility network, to ¥21,371 million. Total assets edged up 1.1% to ¥142,992 million.

Interest-bearing debt, defined as short-term bank loans, the current portion of long-term debt and long-term debt, decreased 20.8% to ¥31,619 million, resulting in a 10.3% decline in total liabilities to ¥58,637 million.

Net shareholders' equity increased 10.8% to ¥84,355 million. The largest reason for both the decrease in debt and for the increase in equity was the conversion of convertible bonds. The equity ratio at fiscal year-end was 59.0%, compared with 53.8% a year earlier.

Return on average total assets was 2.9%, a decrease of 2.6 percentage points, and return on average total equity was 5.2% compared with 12.8% a year earlier.



* Interest coverage ratio equals income before income taxes plus interest expense, divided by interest expense.

Consolidated Balance Sheets

NAMCO LIMITED AND SUBSIDIARIES
31ST MARCH, 1997 AND 1998

Assets	Millions of yen		Thousands of U.S. dollars (Note 2)
	1997	1998	1998
Current assets:			
Cash, mainly time deposits	¥ 32,101	¥ 30,545	\$ 215,105
Marketable securities (Note 3)	11,888	3,173	22,345
Monetary claims in trusts (Note 4)	1,750	250	1,760
Trade receivables	13,952	16,389	115,415
Allowance for doubtful accounts	(456)	(491)	(3,458)
Inventories (Note 5)	10,665	12,097	85,190
Other current assets	2,843	3,550	25,002
Total current assets	72,743	65,513	461,359
Property and equipment:			
Amusement machines and facilities	74,906	85,448	601,746
Buildings and structures	4,980	6,251	44,021
Machinery and equipment	9,297	10,500	73,944
Land	5,174	5,560	39,155
Construction in progress	100	172	1,211
Accumulated depreciation	(54,821)	(63,090)	(444,295)
Net property and equipment	39,636	44,841	315,782
Other assets:			
Investments in:			
Non-consolidated subsidiaries and affiliates	3,457	3,382	23,817
Other securities (Note 3)	207	1,010	7,113
Monetary claims in trusts (Note 4)	250	—	—
Leasehold deposits (Note 6)	18,177	21,371	150,500
Goodwill	1,259	1,725	12,148
Long-term prepaid expenses	2,144	2,079	14,641
Other non-current assets	3,619	3,071	21,626
Total other assets	29,113	32,638	229,845
Total assets	¥141,492	¥142,992	\$1,006,986

See accompanying notes to consolidated financial statements.

Liabilities and Shareholders' equity	Millions of yen		Thousands of U.S. dollars (Note 2)
	1997	1998	1998
Current liabilities:			
Short-term bank loans	¥ 6,222	¥ 4,620	\$ 32,535
Current portion of long-term debt (Note 7)	—	13,879	97,739
Trade payables	11,230	13,530	95,282
Other payables	2,907	3,237	22,796
Accrued income taxes	4,688	2,477	17,444
Accrued expenses	3,313	3,633	25,584
Other current liabilities	1,778	1,883	13,261
Total current liabilities	30,138	43,259	304,641
Long-term debt (Note 7)	33,684	13,120	92,394
Accrued retirement allowances	1,436	1,600	11,268
Other long-term liabilities	124	658	4,634
Total liabilities	65,382	58,637	412,937
Shareholders' equity (Note 8):			
Common stock of ¥50 par value:			
Authorized—120,000,000 shares			
Issued—53,625,916 shares (1997—51,544,903 shares)	21,923	25,147	177,091
Additional paid-in capital	20,956	24,179	170,275
Legal reserve	724	927	6,528
Retained earnings	32,509	34,438	242,521
Total shareholders' equity	76,112	84,691	596,415
Less costs of common shares of treasury stock	2	336	2,366
Net shareholders' equity	76,110	84,355	594,049
Contingent liabilities (Note 12)			
Total liabilities and shareholders' equity	¥141,492	¥142,992	\$1,006,986

Consolidated Statements of Income

NAMCO LIMITED AND SUBSIDIARIES
YEARS ENDED 31ST MARCH, 1997 AND 1998

	Millions of yen		Thousands of U.S. dollars (Note 2)
	1997	1998	1998
Net sales:			
Product and merchandise sales	¥ 64,390	¥ 62,176	\$ 437,859
Revenues from amusement facility operations	71,286	78,361	551,838
Restaurant sales	3,470	4,102	28,887
Royalties	662	1,122	7,902
Total net sales	139,808	145,761	1,026,486
Cost of sales:			
Cost of product and merchandise sales	35,937	36,197	254,908
Cost of revenues from amusement facility operations	64,751	72,464	510,310
Cost of restaurant sales	2,599	3,031	21,345
Cost of royalties	41	79	557
Total cost of sales	103,328	111,771	787,120
Gross profit	36,480	33,990	239,366
Selling, general and administrative expenses	21,578	22,218	156,465
Operating income	14,902	11,772	82,901
Other income:			
Interest and dividends	1,129	748	5,268
Other	916	225	1,584
	2,045	973	6,852
Other expenses:			
Interest, net of gain on conversion of non-interest bearing convertible bonds of ¥1,355 million in 1997	368	1,163	8,190
Other (Note 10)	755	2,245	15,810
	1,123	3,408	24,000
Income before income taxes	15,824	9,337	65,753
Income taxes (Note 11)	8,037	5,173	36,429
Net income	¥ 7,787	¥ 4,164	\$ 29,324
Per share of common stock:	Yen		U.S. dollars (Note 2)
Net income:			
Primary	¥ 163.94	¥ 78.60	\$ 0.5535
Fully diluted	132.17	72.91	0.5134
Cash dividends applicable to the year	30.00	30.00	0.2112

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

NAMCO LIMITED AND SUBSIDIARIES
YEARS ENDED 31ST MARCH, 1997 AND 1998

	Millions of yen		Thousands of U.S. dollars (Note 2)
	1997	1998	1998
Common stock:			
Balance at beginning of year	¥10,013	¥21,923	\$154,387
Conversion of convertible bonds	11,910	3,224	22,704
Balance at end of year	¥21,923	¥25,147	\$177,091
Additional paid-in capital:			
Balance at beginning of year	¥ 9,050	¥20,956	\$147,578
Conversion of convertible bonds	11,906	3,223	22,697
Balance at end of year	¥20,956	¥24,179	\$170,275
Legal reserve:			
Balance at beginning of year	¥ 587	¥ 724	\$ 5,098
Transfer from retained earnings	137	203	1,430
Balance at end of year	¥ 724	¥ 927	\$ 6,528
Retained earnings:			
Balance at beginning of year	¥26,232	¥32,509	\$228,936
Net income	7,787	4,164	29,324
Appropriations:			
Cash dividends	(1,223)	(1,832)	(12,901)
Bonuses to directors and statutory auditors	(150)	(200)	(1,408)
Transfer to legal reserve	(137)	(203)	(1,430)
Balance at end of year	¥32,509	¥34,438	\$242,521

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

NAMCO LIMITED AND SUBSIDIARIES
YEARS ENDED 31ST MARCH, 1997 AND 1998

	Millions of yen		Thousands of U.S. dollars (Note 2)
	1997	1998	1998
Cash Flows from Operating Activities:			
Net income	¥ 7,787	¥ 4,164	\$ 29,324
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation and amortisation	14,212	15,979	112,528
Loss on disposal of property and equipment	559	875	6,162
Devaluation loss on securities	383	955	6,725
Other non-cash items	(1,841)	164	1,155
Changes in operating assets and liabilities:			
Trade receivables	(518)	(2,402)	(16,915)
Inventories	(1,391)	(1,432)	(10,084)
Trade payables	632	2,300	16,197
Accrued income taxes	(101)	(2,211)	(15,570)
Accrued expenses	206	320	2,253
Other, net	274	262	1,844
Other payments	(152)	(200)	(1,408)
Net cash provided by operating activities	20,050	18,774	132,211
Cash Flows from Investing Activities:			
Capital expenditure	(21,229)	(22,460)	(158,169)
Decrease in monetary claims in trusts	2,100	1,750	12,324
Increase in leasehold deposits	(4,150)	(3,194)	(22,493)
Increase in investments in securities	(2,747)	(1,570)	(11,056)
Purchase of common shares of treasury stock	—	(447)	(3,148)
Other, net	696	548	3,859
Net cash used in investing activities	(25,330)	(25,373)	(178,683)
Cash Flows from Financing Activities:			
Repayment of convertible bonds	(5,022)	—	—
Bank borrowings, net	(23)	(1,840)	(12,958)
Cash dividends paid	(1,223)	(1,832)	(12,901)
Net cash used in financing activities	(6,268)	(3,672)	(25,859)
Net decrease in cash and cash equivalents	(11,548)	(10,271)	(72,331)
Cash and cash equivalents at beginning of year	55,537	43,989	309,781
Cash and cash equivalents at end of year	¥ 43,989	¥ 33,718	\$ 237,450

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

NAMCO LIMITED AND SUBSIDIARIES
31ST MARCH, 1997 AND 1998

1. Summary of Significant Accounting Policies

The accompanying consolidated financial statements of Namco Limited (the "Company") and its consolidated subsidiaries (together referred to as the "Companies") have been prepared in conformity with financial accounting standards in Japan. Certain items presented in the original financial statements have been reclassified for presentation solely for the convenience of readers outside Japan.

The Company and its domestic subsidiaries maintain their books of account in conformity with generally accepted accounting principles in Japan, and its foreign subsidiaries in conformity with those of the United States and other generally accepted accounting principles, based on where the subsidiaries are incorporated. No adjustments have been reflected in the accompanying consolidated financial statements to present the accounts of the foreign subsidiaries in compliance with Japanese accounting principles as followed by the Company. However, it is the opinion of the management of the Company that the accounting principles followed by the foreign subsidiaries do not substantially differ from those followed by the Company, except for methods of depreciation and amortisation of property and equipment and goodwill.

Significant accounting policies are as follows:—

(a) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and of its significant subsidiaries, whether directly or indirectly controlled. All significant intercompany balances and intercompany transactions have been eliminated on consolidation.

In order to facilitate consolidation, subsidiaries adopt an annual fiscal period that ends on the last day of February.

Minority interests in net assets and income are not significant and, accordingly, are not presented separately in the accompanying balance sheets and statements of income.

The Company has applied the equity method, after elimination of unrealised intercompany profit, for investments in non-consolidated subsidiaries and significant affiliates.

At 31st March, 1997 and 1998, 100% and 85.71% of Nikkatsu Corporation's shares are owned by the Company.

The main business of Nikkatsu is the production and distribution of cinema films in Japan.

Because the business of Nikkatsu has been operating under the Company Reorganisation Law since 27th September, 1996, the accounts of Nikkatsu are not consolidated. Investment in Nikkatsu amounting to ¥3,000 million (U.S.\$21,126 thousand) is stated at cost.

(b) Statements of Cash Flows

The Company considers cash and marketable securities to be cash and cash equivalents.

(c) Marketable Securities and Investments

Listed securities are stated at the lower of cost or market on an individual basis, cost being determined by the moving-average method. Other securities are stated at cost, determined by the moving-average method.

(d) Inventories

Inventories of the Company and the domestic subsidiaries are stated at cost, determined by the moving-average method, adjusted for any substantial and permanent decline in value. Inventories of the foreign subsidiaries are stated at the lower of cost (principally first in, first out) or market (net realisable value).

(e) Property and Equipment

Property and equipment are stated at cost. Depreciation is computed for all depreciable assets of the Company and the domestic subsidiaries by the declining-balance method and for all depreciable assets of the foreign subsidiaries by the straight-line method, at rates based on estimated useful lives of the assets according to general class, type of construction, and use.

Repairs and maintenance which do not improve or extend the life of the related assets are expensed currently.

(f) Goodwill

Goodwill represents the excess of the purchase price over the fair market value of net assets acquired in business combinations. Goodwill incurred by foreign subsidiaries in the United States is amortised using the straight-line method over 15 years. Goodwill incurred by the Company and the domestic subsidiaries is charged to income when incurred.

(g) Research and Development Expenses

Research and development expenses are charged to income as selling, general and administrative expenses of the period in which they are incurred. When the management of the Company indicates its intention to produce and market a product, related research and development expenses are accounted for as production costs of the product.

(h) Retirement Benefits

Under the Company's and its domestic subsidiaries' employees' retirement plan, employees are entitled to receive lump-sum or periodic payments based on length of service and current basic salary. Amounts payable under the plan are provided by a funded pension plan. Amounts payable to employees who are not covered by the pension plan are provided by unfunded retirement allowances.

While the Company has no legal obligation, it is customary practice in Japan to make lump-sum payments to directors or statutory auditors upon retirement, with the approval of shareholders at the annual shareholders' meeting. According to established guidelines, the amount of such allowance is computed based upon payment factors determined by position and length of service as director or statutory auditor.

Amounts required under the plan have been provided by unfunded retirement allowances, of which, the balances at 31st March, 1997 and 1998 were ¥1,433 million (U.S.\$10,091 thousand) and ¥1,597 million (U.S.\$11,246 thousand), respectively.

The foreign subsidiaries have defined benefit pension plans that provide pension benefits to substantially all employees.

(i) Income Taxes

The Company records income taxes currently payable based upon the determination of taxable income.

(j) Translation of Foreign Subsidiaries' Financial Statements

The accounts of the foreign subsidiaries are translated into yen at current exchange rates—that is, the rates in effect at the end of the year.

(k) Net Income and Cash Dividends per Share

In computing primary net income per share, the average number of shares of common stock outstanding during each year has been used.

The computation of fully diluted net income per share reflects the effect of common shares contingently issuable upon the conversion of convertible bonds as if such bonds had been converted at the beginning of the year or at the time of issue in the case of newly issued bonds after giving effect to the elimination of interest expenses, less income tax effect, applicable to the convertible bonds.

Cash dividends per share represent dividends declared for the respective year.

2. U.S. Dollar Amounts

The financial statements presented herein are expressed in yen and, solely for the convenience of the readers, have been translated into United States dollars at the rate of ¥142 = U.S.\$1, the approximate exchange rate at 27th June, 1998.

This translation should not be construed as a representation that all amounts shown could be converted into U.S. dollars.

3. Marketable Securities and Investments

Marketable securities and investments in other securities at 31st March, 1997 and 1998 are summarised as follows:

	Millions of yen		Thousands of
	1997	1998	U.S. dollars
Marketable securities:			1998
Listed corporate shares	¥ 2,485	¥1,384	\$ 9,746
Corporate bonds	9,403	1,789	12,599
	¥11,888	¥3,173	\$22,345
Investments in other securities:			
Listed corporate shares	¥ —	¥ 1	\$ 7
Non-listed corporate shares	207	1,009	7,106
	¥ 207	¥1,010	\$7,113

The market value of listed securities exceeds book value.

4. Monetary Claims in Trusts

Monetary claims in trusts as long-term investments at 31st March, 1997 and 1998 are summarised as follows:

	Millions of yen		Thousands of
	1997	1998	U.S. dollars
Loan claims in trusts, interest at prime minus 0.1%, maturing ¥1,000 million on 31st October, 1997	¥1,000	¥ —	\$ —
Lease claims in trusts, maturing in installments through 1998	1,000	250	1,760
	2,000	250	1,760
Less current portion	1,750	250	1,760
	¥ 250	¥ —	\$ —

On 31st October, 1994, the Company purchased the beneficiary rights to a loan agreement with a consumer finance company created as trust assets by a certain leasing company. The beneficiary rights are collateralised by receivables owned by the consumer finance company.

On 22nd July, 1994 and 24th July, 1995, the Company purchased the rights to receive payment as the beneficiary of lease proceeds on lease contracts, which are accepted as trust assets by a certain trust bank. The purchase agreement does not include a guarantee of principal.

5. Inventories

Inventories at 31st March, 1997 and 1998 are summarised as follows:

	Millions of yen		Thousands of
	1997	1998	U.S. dollars
Merchandise	¥ 884	¥ 660	\$ 4,648
Products	4,409	4,560	32,113
Material	1,784	2,456	17,296
Work in process	2,969	3,548	24,986
Supplies	619	873	6,147
	¥10,665	¥12,097	\$85,190

6. Leasehold Deposits

Leasehold deposits at 31st March, 1997 and 1998 are summarised as follows:

	Millions of yen		Thousands of
	1997	1998	U.S. dollars
Deposits for amusement facility operations and restaurant operations	¥16,563	¥19,758	\$139,141
Deposits for office space	1,436	1,430	10,070
Other deposits	178	183	1,289
	¥18,177	¥21,371	\$150,500

Such leasehold deposits do not bear interest and are generally refundable when the lease is terminated.

The Companies conduct amusement facility operations and restaurant operations on properties leased from lessors under long-term lease contracts. Lease expenses for amusement facility operations and restaurant operations for the years ended 31st March, 1997 and 1998 amounted to ¥20,857 million (U.S.\$146,880 thousand) and ¥21,551 million (U.S.\$151,767 thousand), respectively.

7. Long-term Debt

Long-term debt at 31st March, 1997 and 1998 is summarised as follows:

	Millions of yen		Thousands of
	1997	1998	U.S. dollars
4.7% unsecured convertible bonds due 30th September, 1998 convertible into common stock at ¥3,075 per share	¥14,944	¥13,233	\$93,190
0.8% unsecured convertible bonds due 28th September, 2001 convertible into common stock at ¥3,106 per share	5,853	3,587	25,260
0.9% unsecured convertible bonds due 30th September, 2003 convertible into common stock at ¥3,106 per share	9,896	7,426	52,296
Bank loans	2,991	2,753	19,387
	33,684	26,999	190,133
Less current portion	—	13,879	97,739
	¥33,684	¥13,120	\$92,394

For the benefit of the holders of the 4.7% convertible bonds, the Company has agreed that the aggregate amount of payments of cash dividends may not exceed ¥4,000 million (U.S.\$28,169 thousand) plus the aggregate amount of net income of the Company starting from the year ended 31st March, 1992.

For the benefit of the holders of the 0.8% and 0.9% convertible bonds, the Company has agreed that the aggregate amount of payments of cash dividends may not exceed ¥4,400 million (U.S.\$30,985 thousand) plus the aggregate amount of net income of the Company starting from the year ended 31st March, 1995.

8. Shareholders' Equity

The Japanese Commercial Code requires that at least 50% of the issue price of new shares be transferred to the common stock account, provided 50% of the issue price is greater than the par value of common stock. In accordance with such requirement, 50% of the proceeds from the new shares issue based upon the conversion of convertible bonds was transferred to the common stock account and the remaining 50% was credited to additional paid-in capital.

The Commercial Code provides that an amount equal to at least 10% of the amount to be disbursed as distribution of retained earnings be appropriated as a legal reserve until such reserve equals 25% of stated capital.

Additional paid-in capital and legal reserve are not available for dividends but may be used to reduce a deficit or may be transferred to stated capital.

Cash dividends, directors' and statutory auditors' bonuses and appropriations to the legal reserve charged to retained earnings during the years ended 31st March, 1997 and 1998 represent dividends and bonuses paid out during such period and the related appropriations to the legal reserve.

The accompanying consolidated financial statements do not include any provision for a dividend of ¥15 per share aggregating ¥803 million (U.S.\$5,654 thousand)

and bonuses to the directors and statutory auditors aggregating ¥165 million (U.S.\$1,161 thousand) declared in June 1998 nor for the related appropriation to legal reserve amounting to ¥97 million (U.S.\$683 thousand).

9. Research and Development Expenses

Total research and development expenses for the years ended 31st March, 1997 and 1998 amounted to ¥8,087 million (U.S.\$56,951 thousand) and ¥8,944 million (U.S.\$62,986 thousand), respectively.

10. Other Expenses

The composition of other expenses—other for the years ended 31st March, 1997 and 1998 was as follows:

	Millions of yen		Thousands of U.S. dollars
	1997	1998	1998
Devaluation loss of securities	¥384	¥ 955	\$ 6,725
Loss on closure of amusement facilities	—	734	5,169
Amortisation of goodwill	125	186	1,310
Other	246	370	2,606
	¥755	¥2,245	\$15,810

11. Income Taxes

The Company is subject to a number of taxes based on income which, in the aggregate, result in a statutory tax rate of approximately 52%.

12. Contingent Liabilities

At 31st March, 1997 and 1998 contingent liabilities for loans guaranteed by the Company principally on behalf of affiliates amounted to ¥274 million (U.S.\$1,929 thousand) and ¥2,747 million (U.S.\$19,345 thousand), respectively.

In the opinion of management of the Company, it is not anticipated that substantial loss will result from these contingencies.

13. Stock Option Plan

In June 1997, the Company's shareholders approved a stock option plan (the 1997 plan), which permitted the Company to grant options for up to 115,000 shares of its common stock to all directors (except the chairman and chief executive officer) and eligible key employees.

The 1997 plan is exercisable from 1st April, 1998 to 31st March, 2001, and the option price per share was set at ¥4,165 on the date the options were granted.

A summary of changes in common stock options during 1998 is:

	Number of Shares
Outstanding at 1st April, 1997	¥ 0
Granted	115,000
Exercised	(0)
Cancelled	(1,000)
Outstanding at 31st March, 1998	¥114,000

In addition, on 27th June, 1998, shareholders approved a stock option plan (the 1998 plan), which permitted the Company to grant options for up to 119,000 shares of its common stock to all directors (except chairman and chief executive officer) and eligible key employees.

The 1998 plan is exercisable from 1st July, 2000 to 30th June, 2003, and options may be granted at a price of 105% of the average market value in the month preceding the date the option is granted.

14. Segment Information

(a) Business Segment Information

The Companies operate in four business segments, as indicated below.

Certain corporate administrative expenses have not been allocated to segments due to the nature of the expense.

	Millions of yen					
	Business segments					Consolidated
	Amusement Facility Operations	Coin-Operated Game Machines	Home Videogame Software	Restaurant Operations	Corporate Items	
1997:						
Net sales to customers	¥71,304	¥40,051	¥24,982	¥3,471	¥ —	¥139,808
Intersegment sales	58	1,425	—	122	(1,605)*	—
Total net sales	71,362	41,476	24,982	3,593	(1,605)	139,808
Operating income	2,237	5,907	10,584	26	(3,852)**	14,902
Identifiable assets	55,482	19,695	5,387	2,400	58,528	141,492
Depreciation and amortisation	12,494	941	366	101	310	14,212
Capital expenditure	19,375	959	452	87	356	21,229
1998:						
Net sales to customers	¥78,371	¥29,518	¥33,770	¥4,102	¥ —	¥145,761
Intersegment sales	54	660	—	89	(803)*	—
Total net sales	78,425	30,178	33,770	4,191	(803)	145,761
Operating income	1,001	2,344	12,496	(6)	(4,063)**	11,772
Identifiable assets	65,451	20,903	9,359	2,781	44,498	142,992
Depreciation and amortisation	14,230	906	383	102	358	15,979
Capital expenditure	19,297	1,188	395	121	1,459	22,460

* Elimination of intersegment sales

** Includes unallocated administrative expenses of ¥4,506 million in 1997 and ¥4,264 million in 1998

(b) Geographical Segment Information

Summarised data for the Companies' operations (sales within Japan and outside Japan) is as follows:

	Millions of yen			
	Within Japan	Outside Japan	Corporate Items	Consolidated
1997:				
Net sales to customers	¥98,113	¥41,695	¥ —	¥139,808
Intersegment sales	6,326	175	(6,501)*	—
Total net sales	104,439	41,870	(6,501)	139,808
Operating income	16,013	3,641	(4,752)**	14,902
Identifiable assets	61,251	22,464	57,777	141,492
1998:				
Net sales to customers	¥107,685	¥38,076	¥ —	¥145,761
Intersegment sales	4,260	191	(4,451)*	—
Total net sales	111,945	38,267	(4,451)	145,761
Operating income	14,511	1,533	(4,272)**	11,772
Identifiable assets	75,178	24,013	43,801	142,992

* Elimination of intersegment sales

** Includes unallocated administrative expenses of ¥4,506 million in 1997 and ¥4,264 million in 1998

(c) Overseas Sales Information

Overseas sales of the Companies for the years ended 31st March, 1997 and 1998 amounted to ¥49,723 million (35.6% of consolidated net sales) and ¥50,552 million (34.7% of consolidated net sales).

Independent Auditors' Report



The Board of Directors
Namco Limited

We have examined the consolidated balance sheets of Namco Limited and subsidiaries as of 31st March, 1997 and 1998 and the related consolidated statements of income, shareholders' equity and cash flows for the years then ended. Our examinations were made in accordance with generally accepted auditing standards in Japan, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Namco Limited and subsidiaries as of 31st March, 1997 and 1998 and the results of their operations and their cash flows for the years then ended, in conformity with generally accepted accounting principles in Japan applied on a consistent basis.

The accompanying consolidated financial statements expressed in United States dollars have been translated into dollars solely for the convenience of the reader. We have reviewed the translation and, in our opinion, the consolidated financial statements expressed in yen have been translated into dollars on the basis described in Note 2 to the consolidated financial statements.

Century Audit Corporation

Tokyo, Japan
27th June, 1998

Corporate Data

Corporate Headquarters

NAMCO LIMITED

2-1-21, Yaguchi, Ota-ku, Tokyo 146-8655, Japan

Tel: 03-3756-2311

Fax: 03-3757-2553

Date of Establishment

June 1, 1955

Number of Employees (Parent Company)

2,407 (As of June 30, 1998)

Number of Shareholders

5,326 (As of March 31, 1998)

Listing of the Company's Shares

First Section of the Tokyo Stock Exchange

Independent Certified Public Accountants

Century Audit Corporation

The Japan Red Cross Bldg.

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Directors and Statutory Auditors

Chairman and Chief Executive Officer

Masaya Nakamura*

Executive Vice President

Ryuji Hashiguchi*

Senior Managing Directors

Kunio Kawakami

Shigeichi Nakamura

Managing Directors

Masahiro Tachibana*

Akiyoshi Sarukawa

Kyushiro Takagi

Yasuhiko Asada

Directors

Katsutoshi Endo

Kazunori Sawano

Tsuyoshi Otsuka

Hirofumi Tashiro

Tsugio Kinoshita

Keiji Tanaka

Jun Higashi

Seiichi Hirota

Shukuo Ishikawa

Yutaka Asakage

Mitsuo Kanehira

Yoshitaka Yamauchi

Yoichi Haraguchi

Statutory Auditors

Shigeru Yamada

Nobuo Okabe

Toshinori Hayashida

Toru Okuyama

(As of June 30, 1998)

*Representative Directors

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Namco Ireland Ltd.

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I&K Co., Ltd.

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T&E Co., Ltd.

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Mil Ltd.

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Namcot Ltd.

2-1-21, Yaguchi, Ota-ku, Tokyo 146-8655, Japan

* Effective October 1, 1998, the company will move to the following
address: 2055 Junction Avenue, San Jose, CA 95131, USA
(Telephone and fax numbers are planned to be unchanged.)

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