SONY

do you dream in Sony?

Annual Report 1998

Year Ended March 31, 1998

Sony is a company devoted to the celebration of life.
We create things for every kind of imagination.
Products that stimulate the senses and refresh the spirit.
Ideas that always surprise, and never disappoint.
Innovations that are easy to love, and effortless to use.
Things that are not essential, but hard to live without.
We are not here to be logical. Or predictable.
We're here to pursue infinite possibilities.
We allow the brightest minds to interact freely,
so the unexpected can emerge.
We invite new thinking, so even more fantastic ideas can evolve.
Creativity is our essence.
We take chances. We exceed expectations.
We help dreamers dream.

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Cautionary Statement With Respect to Forward-Looking Statements
Statements made in this annual report with respect to Sony's plans, strategies and beliefs, and other statements that are not historical facts are forward-looking statements about the future performance of Sony, which are based on management's assumptions and beliefs in light of the information currently available to it, and involve risks and uncertainties. Potential risks and uncertainties include, without limitation, general economic conditions in Sony's markets, particularly levels of consumer spending; exchange rates, particularly between the yen and the U.S. dollar, and other currencies in which Sony makes significant sales or in which Sony's assets and liabilities are denominated; and Sony's ability to continue to win acceptance of its products and services, which are offered in highly competitive markets characterized by continual new product introductions, rapid developments in technology (particularly in the Electronics business), and subjective and changing consumer preferences (particularly in the Game, Music, and Pictures businesses).

[Financial Highlights]

Sony Corporation and Consolidated Subsidiaries · Year ended March 31

OPERATING RESULTS	Yen in millions except per share amounts 1997	1998	Percent change 1998/1997	Dollars in thousands except per share amounts 1998
FOR THE YEAR				
Sales and operating revenue	¥5,663,134	**¥6,755,490**	+19.3%	**$51,177,955**
Operating income	370,330	**520,210**	+40.5	**3,940,985**
Income before income taxes	312,429	**453,749**	+45.2	**3,437,492**
Net income	139,460	**222,068**	+59.2	**1,682,333**
Per share data:				
Net income — Basic	¥ 367.7	**¥ 557.7**	+51.7%	**$ 4.23**
— Diluted	309.2	**483.4**	+56.3	**3.66**
Cash dividends	55.0	**60.0**		**0.45**
AT YEAR-END				
Stockholders' equity	¥1,459,332	**¥1,815,555**	+24.4%	**$13,754,205**
Total assets	5,680,246	**6,403,043**	+12.7	**48,507,902**
Number of employees	163,000	**173,000**		

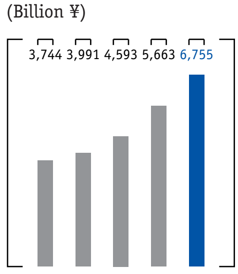
Notes: 1. U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥132=U.S.$1, the approximate Tokyo foreign exchange market rate as of March 31, 1998.

2. As of March 31, 1998, the Company had 1,142 consolidated subsidiaries. It has applied the equity accounting method in respect to its 61 affiliated companies.

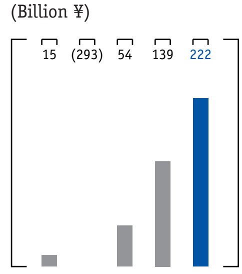
3. Net income per share amounts for the fiscal year ended March 31, 1997 have been restated to conform with Statement of Financial Accounting Standards No. 128, "Earnings per Share." Refer to Notes 2 and 4 of Notes to Consolidated Financial Statements, regarding the earnings per share computation.

4. Stockholders' equity and total assets as of March 31, 1997 have been reclassified to conform to the 1998 presentation.

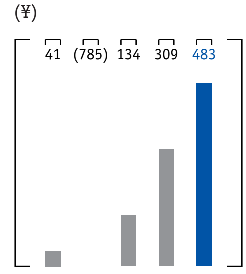
Sales and Operating Revenue
(Billion ¥)



Net Income (Loss)
(Billion ¥)



Net Income (Loss) per Share*
(¥)



*Diluted

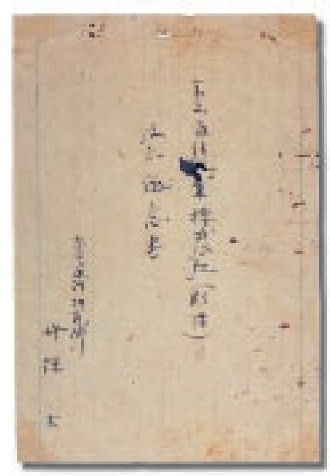
Remembering Masaru Ibuka

Sony Founder and Chief Advisor Masaru Ibuka passed away on December 19, 1997. Mr. Ibuka founded Sony in 1946 along with Akio Morita, Founder and Honorary Chairman. In the ensuing years, his creativity and innovative thinking as an engineer and corporate leader were the driving force behind Sony's phenomenal growth.

An Ideal Factory "The establishment of an ideal factory, free, dynamic and pleasant, where technical personnel of sincere motivation can exercise their technological skills to the highest levels." These are the words of Mr. Ibuka in the Founding Prospectus for Tokyo Tsushin Kogyo Kabushiki Kaisha (Tokyo Telecommunications Engineering Corporation), the former name for Sony Corporation. Mr. Ibuka was an engineer with an overwhelming curiosity and sensitivity to events around him. He combined these qualities with foresight and enthusiasm to propel the development of the entire electronics industry. Among his many achievements are the development of Japan's first tape recorder and transistor radio, as well as Sony's Trinitron color TV. These breakthroughs formed the foundation for today's Sony. Mr. Ibuka's vision went beyond existing technology. He created entirely new products and markets by following a unique research and development path. This same spirit, which has thrived since the establishment of Sony, still exists more than half a century later.

Fostering Curiosity in Science Deeply interested in leading-edge technologies, Mr. Ibuka also distinguished himself through a strong devotion to education. In particular, he recognized the importance of science programs in elementary and junior high schools. In 1959, Sony extended its first science education grants to 28 elementary schools in Japan based on his proposal. In 1972, the Sony Foundation of Science Education was formed to carry on this tradition. In 1969, Mr. Ibuka formed the Early Development Association for the purpose of conducting a variety of studies on education for young children.

Order of Culture Awarded to an Entrepreneur Mr. Ibuka, who had outstanding insight and creativity in technology, contributed to the development and commercialization of many types of electronics equipment. He was a pioneer in applying leading electronics technology to a broad range of consumer products. He also originated a new direction in the Japanese electronics industry from modifying existing technologies to creating new business opportunities. In recognition of these achievements, Mr. Ibuka received the Order of Culture in 1992. His role in the development and prosperity of the electronics industry led to a series of other honors: the First Class Order of the Sacred Treasure in 1978; the First Class Order of the Rising Sun with the Grand Cordon in 1986; and the Grand Cordon of the Order of the Rising Sun, Paulownia Flowers, which was conferred posthumously in 1997.



[above] *Masaru Ibuka*

[left] *Masaru Ibuka was awarded many honors. This photo was taken when he received the Order of Culture in 1992.*

[right] *The Founding Prospectus of Tokyo Tsushin Kogyo Kabushiki Kaisha, the former name of Sony Corporation.*

[To Our Shareholders]

Performance for the Fiscal Year

The fiscal year ended March 31, 1998 was an excellent one for Sony. Sales and earnings both reached record highs for the second consecutive year.

Consolidated sales and operating revenue were up substantially to ¥6,755 billion ($51,178 million). Earnings improved along with the sales growth and the yen's depreciation. Operating income was ¥520 billion ($3,941 million), income before income taxes ¥454 billion ($3,437 million), and net income ¥222 billion ($1,682 million). This performance lifted the return on equity from 11% during the previous fiscal year to 14%.

In the Electronics business, Sony had a number of hit products. Among them were MiniDisc systems, home-use digital camcorders, Wega color TVs featuring flat-surface cathode ray tubes, VAIO notebook PCs, digital cellular phones, and electronic components such as optical pickups. A weakening PC market, however, brought down growth rates in sales of computer displays and caused memory chip sales to decline. In the Game business, which Sony first entered in December 1994, cumulative worldwide production shipments of our game consoles has topped 30 million units in just over three years. This business sector has grown to account for approximately 10% of consolidated sales and 22% of consolidated operating income. In the Music business, Celine Dion's *Let's Talk About Love* and the *Titanic* soundtrack each sold in excess of 19 million units worldwide. Additionally, in the Pictures business, there were several highly successful releases, including *Men in Black, Air Force One,* and *My Best Friend's Wedding*. In the Insurance segment, the life insurance business in Japan saw an expansion.

During the second half of 1997, currency and economic turmoil took place in Asia. However, the overall impact of this situation was positive for Sony's earnings in the fiscal year under review. One reason is that Asia plays a major role in Sony's operations as a production and export base. Furthermore, our financial center in Singapore took appropriate measures to deal with the turmoil.

Outlook for the Business Climate

The fiscal year that began in April 1998 is expected to be a challenging one for Sony. The operating environment in Japan has become even more difficult and the Asian economy remains sluggish. Furthermore, the future direction of exchange rates is unclear and competition is expected to intensify in the world audiovisual equipment market. Given this challenging environment, Sony will market value-added products like MiniDisc systems, and the Wega color TV series on a global scale to enhance profitability.

In terms of financial performance, Sony focuses on improving the earnings and cash flows of each business unit to increase shareholder value of the entire group. We plan to continue to improve profit margins, carefully select new investments, and reduce inventories.

Continuously Improving the Management System

In June 1997, Sony drastically altered the composition of the Board of Directors and established the new position of corporate executive officer. This move was made to reinforce corporate governance by speeding up decision-making, making management more efficient, and clarifying the responsibilities of managers. The Board of Directors is now much smaller and includes more external directors. Additionally, the new management system separates individuals responsible for policy-making and oversight from those who are responsible for operational management. Furthermore, Sony introduced incentive programs that are linked to Sony's stock price as a reflection of the company's performance. Directors, corporate executive officers, and high-level management in Japan and overseas, including at Sony Group companies, are covered by the programs. This action more closely aligns the interests of Sony's management with shareholder value.

Norio Ohga
Chairman and Chief Executive Officer

Nobuyuki Idei
President and Co-Chief Executive Officer

In January 1998, Sony reorganized its ten-company structure in the Electronics business to make operations more efficient and better able to adapt to the proliferation of networks. One action was the merger of the two companies in charge of broadcast- and professional-use equipment to form the Broadcasting & Professional Systems Company. Another action was the establishment of the Digital Network Solutions Company. This new organization encompasses broadcasting and reception systems for digital satellite broadcasts and digital TV, and network-related businesses.

In April 1998, we created Corporate IS Solutions, a new organization whose task is to drastically realign and upgrade our information network systems including construction of Sony's global supply chain. To bolster quality assurance activities, we adopted the Six Sigma method and began applying it to all management processes in September 1997.

Through these steps, Sony is assembling a quality management system and infrastructure that is both efficient and capable of swiftly adapting to change.

The Sony Mission

Since its inception, Sony has constantly created markets and proposed new lifestyles. Our mission is to offer the opportunity to create and fulfill dreams to all kinds of people, including shareholders, customers, employees, and business partners. We pledge to continue to take on the challenge of preserving Sony's position as a unique and creative company.

May 7, 1998

Norio Ohga
Chairman and Chief Executive Officer

Nobuyuki Idei
President and Co-Chief Executive Officer

Key Themes at Sony

In each of the past two fiscal years, Sony has posted all-time-high sales and earnings. Even so, the company's markets present intensifying challenges. What direction should Sony go at a time like this? President Nobuyuki Idei addresses this question in the context of three key themes.

Strategies to Foster Competitive Strengths and Growth

Today, Sony needs a competitive strategy to bolster existing businesses, and a growth strategy to guide us into new fields of business.

Our competitive strategy aims to add more value to products through the digitization of audiovisual equipment, our core business, and the fusion of this equipment with information technology. Reinforcing our supply chain, from development, design, procurement, and production through logistics and sales, is another goal of this strategy. By pursuing these objectives, we will continue to aim for higher earnings.

Sony's growth strategy entails much more than merely selling electronics products and content. We also need to expand opportunities to earn profits by building a new value chain, where we receive a steady stream of revenues following each sale. During the year under review, we invested in Japan Sky Broadcasting Co., Ltd (JSkyB), a digital satellite broadcasting venture in Japan, enabling us to take part in its management as part of our content distribution business. Following JSkyB's May 1998 merger with PerfecTV Corporation, the service provided by this venture is now called SKY PerfecTV! Sony intends to promote aggressively these businesses, which center on platforms for network services.

Sony, a "Complex" Corporation

The business domains of Sony extend beyond electronics to include games, music, pictures, insurance, and other fields. To make these businesses function smoothly, a bottom-up and a top-down strategy must be implemented simultaneously and interactively. A bottom-up strategy comes from each business unit, and a top-down strategy from the head office. Sony is an organization made up of many elements. We must adhere to the concept of "complex system," in which the various elements interact with each other to create new values and make the whole greater than the sum of its parts.

"do you dream in Sony?"

The term "Digital Dream Kids" defines the future direction of new product development at Sony. This concept embodies our belief that Sony must continue to be a source of unique and enjoyable products that fulfill the dreams of our customers who are captivated by the potential of digital technology. In addition, we have created the "do you dream in Sony?" concept to convey the centripetal force of Sony and its diverse business domains. This concept expresses the idea of making dreams come true at a place called Sony, in the Sony way, and along with the Sony family. Dreams are common to all people who come into contact with Sony including shareholders, customers, employees, business partners, and others. "do you dream in Sony?" therefore means that people enjoy Sony products and gather at a place called Sony to make their dreams come true.

digital

content

dream

Sony is making an effort to harness the full potential of digital technology for the purpose of providing enjoyment to people around the world, with a concept called Digital Dream Kids. To achieve this digital dream requires a seamless merging of content, hardware, and technology, which Sony is uniquely qualified to accomplish as a world leader in each of these areas.

for making digital dreams come true Even in today's digital age, people seek out the same kinds of entertainment they have always enjoyed, such as great music, memorable films, and captivating games. Sony has a rich collection of music, films, games, and other forms of entertainment **content**. What's more, many talented experts such as musicians and vocalists, film producers, game creators, and others produce this collection, and their collective efforts produce a steady steam of exciting content. ✥ Content holds immense promise. Packaged media such as CDs and videos represent just one channel for music, films, games, and other forms of entertainment to reach consumers. There are other distribution channels including digital satellite, terrestrial, and cable broadcasting, and the Internet. All this points to the potential of content as a means to convey emotions and dreams to audiences around the world. ✥ Sony will continue to be a creative haven where the world's most talented artists and creators can generate superior content. At the same time, Sony will retain an aggressive stance in the dissemination of that content through digital networks. All these efforts target a single goal of making digital dreams come true.

digital
tools
dream

for making digital dreams come true Content that originates from dreams should be enjoyed on hardware conceived from dreams. Sony believes that these **tools**, which originate in dreams, should have creativity as well as offer a variety of elements such as superior sound and picture quality, easy operation and portability, and an innovative design and pleasing feeling. ✥ Throughout its history, Sony has been a source of unique products based on advanced technology. Sony products have continuously surprised and intrigued customers over the years. The reason lies in the superiority of each element including performance, ease-of-operation, and design. Sony is always trying to exceed the expectations of customers. To this end, Sony conducts exhaustive studies to determine everything from easy-to-use, sophisticated designs to the desired performance and functions of each product. ✥ During the year under review, Sony launched a series of products including: Digital Handycam camcorders, MD Walkman models, and CD Walkman portable CD players. All deliver high performance, low power consumption, and compact size. Other examples include the Wega Series of color TVs with the industry's first flat-surface cathode ray tube, and the VAIO notebook PCs, beautifully designed to be both slender and lightweight. These products have been well-received in the market by satisfying customers through their excellent fundamental performance and elegant exteriors. ✥ In the field of electronics, Sony remains dedicated to developing leading-edge technology and creating hardware that achieves the highest standards possible by blending performance, quality, and design. This drive is central to our aim of making digital dreams come true.

digital

linkage

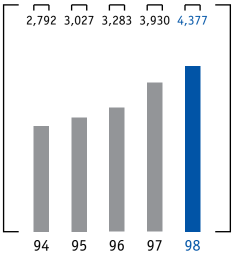
dream

for making digital dreams come true The easy enjoyment of tools and content, both created from dreams, requires innovative **linkage** technology. This is why Sony is hard at work on developing interface and software technologies. The goal is to let users operate products with much more freedom by connecting hardware to networks. ✦ Sony is aggressively promoting the IEEE 1394 standard, which is currently being proposed by Sony under the name i.Link, for interactive communications between digital audiovisual equipment and PCs. Sony was among the first to incorporate a digital interface conforming to this standard in its products. The Digital Handycam camcorders and VAIO home-use PCs are two examples. In May 1998, Sony, along with seven major Japanese and European electronics companies, formulated the core specifications of HAVi (Home Audio Video interoperability) for audiovisual equipment that can connect to a home network based on IEEE 1394. This specification will offer new benefits to customers allowing interactive connection and operation between digital audiovisual equipment from different manufacturers. ✦ Sony alone is developing the Aperios operating system, which meets audiovisual equipment requirements that demand real-time processing. Sony is studying the loading of appropriate software in audiovisual equipment such as Windows™ CE, PersonalJava™, and MHEG multimedia international standard script language, which is expected to be adopted for digital broadcasting. As part of this drive, Sony has announced plans to begin collaboration with Microsoft Corporation to create a home-networking environment by the convergence of PCs to digital TVs and audiovisual platforms. Sony intends to license Windows CE for use in certain products. Similarly, Microsoft intends to license Sony's Home Networking Modules for use with certain versions of Windows CE. In addition, Sony has entered into a licensing agreement with Sun Microsystems, Inc. for the development of applications based on Java™ technology for the home network environment. Under the agreement, Sony incorporates applications based on Java technology into its advanced digital audiovisual products, and Sun creates PersonalJava software development tools for digital audiovisual products. ✦ Sony is now putting these technologies to work. This knowledge is expected to lead to a home network in which customers can access specific video and audio selections whenever they want. The ultimate goal is making digital dreams come true.

Electronics

Electronics business consists of Audio, Video, Televisions, Information and communications, and Electronic components and other.

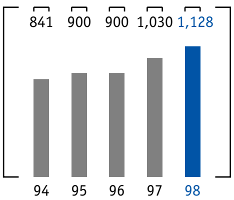
Sales to Customers
(Billion ¥)



Audio

Audio encompasses MD systems, CD players, headphone stereos, personal component stereos, hi-fi components, radio-cassette tape recorders, tape recorders, digital audio tape (DAT) recorders/players, IC recorders, radios, headphones, car audio, professional-use audio equipment, audiotapes, and blank MDs.

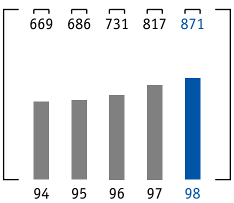
Sales to Customers
(Billion ¥)



Video

Video comprises 8mm, VHS, and DV-format VTRs, DVD-Video players, video CD players, digital still cameras, broadcast- and professional-use video equipment, and videotapes.

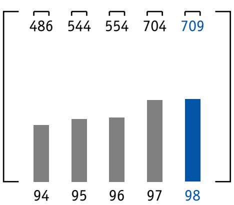
Sales to Customers
(Billion ¥)



Televisions

Televisions includes color TVs, Hi-Vision TVs, projection TVs, flat display panels, personal LCD monitors, professional-use monitors/projectors, and large color video display systems.

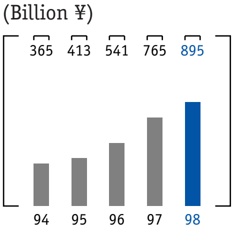
Sales to Customers
(Billion ¥)



Information and communications

Information and communications consists of computer displays, personal computers, computer peripherals, satellite broadcasting reception systems, Internet terminals, telephones, and car navigation systems.

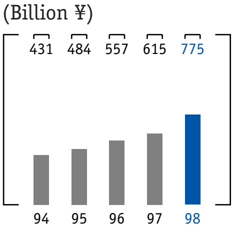
Sales to Customers
(Billion ¥)



Electronic components and other

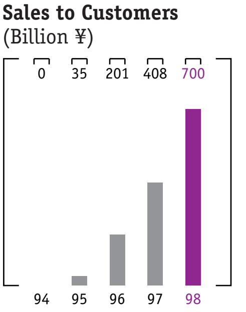
Electronic components and other consists of semiconductors, LCDs, electronic components, cathode ray tubes, batteries, and FA systems.

Sales to Customers
(Billion ¥)



Game

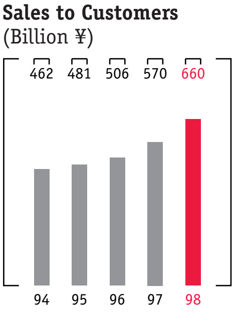
Game consoles and software business is conducted mainly through Sony Computer Entertainment.



Music

Music business is conducted through Sony Music Entertainment Inc. (SMEI) and Sony Music Entertainment (Japan) Inc.

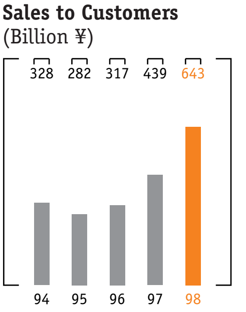
SMEI encompasses Columbia Records Group; Epic Records Group; RED Distribution; Relativity Entertainment Group; Sony/ATV Music Publishing; Sony Classical; Sony Music International; and associated labels.



Pictures

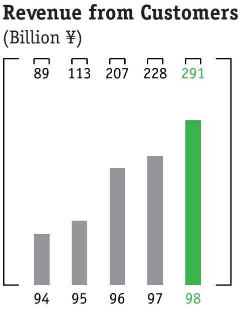
Motion picture and television business is conducted mainly through Sony Pictures Entertainment (SPE); and theatre operations.

SPE includes: the Columbia TriStar Motion Picture Group (Columbia Pictures, Sony Pictures Classics, Sony Pictures Releasing, Columbia TriStar Film Distributors International); the Columbia TriStar Television Group (Columbia TriStar Television, Columbia TriStar Television Distribution, Columbia TriStar International Television); Columbia TriStar Home Video; the Digital Studios Division; and Sony Pictures Studios and The Culver Studios.



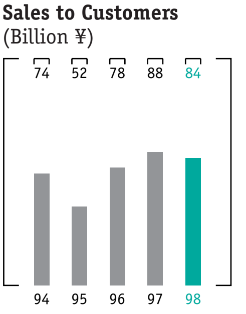
Insurance

Insurance business is conducted mainly through Sony Life Insurance Co., Ltd.



Other

Other businesses include customer financing, leasing, broadcasting, networking, and other businesses.



[Electronics]

During the year under review, sales to customers in the Electronics business accounted for approximately 65% of Sony's consolidated sales. Sony conducts a broad range of businesses within this sector, dividing activities into five categories: Audio, Video, Televisions, Information and communications, and Electronic components and other. In terms of Sony's organization, the Electronics business is divided into ten internal companies. All companies, under the direction of their respective presidents listed below, are working to further improve their ability to respond quickly to changes in customers' needs and market trends.

Suehiro Nakamura
Semiconductor Company

Masayuki Takano
Display Company

Shizuo Takashino
Personal A&V Products Company

Akiyoshi Kawashima
Recording Media & Energy Company

Kunitake Ando
Information Technology Company

Sunobu Horigome
Digital Network Solutions Company

Mitsuru Ohki
Broadcasting & Professional Systems Company

Yutaka Nakagawa
Personal & Mobile Communication Company

Katsumi Ihara
Home A&V Products Company

Yoshihide Nakamura
Computer Peripherals & Components Company

Sony is aggressively expanding its operations outside Japan, developing and manufacturing products and providing customer services in the markets where its products are sold. During the year, Sony further strengthened its manufacturing operations, particularly in North America and Eastern Europe. Additionally, Sony established Sony Marketing (Japan), Inc. in April 1997 to manage sales and marketing activities in Japan for electronics products.

Junichi Kodera
President and Representative Director
Sony Marketing (Japan), Inc.

Teruaki Aoki
President and Chief Operating Officer
Sony Electronics Inc.

Jakob J. Schmuckli
President and Director
Sony Europe GmbH

(As of May 7, 1998)

« Audio »

MiniDisc (MD) Systems

Sony first introduced MD systems in 1992. Since then, compact size, superb sound quality, and digital recording and editing capabilities have fueled solid growth in demand for these systems, primarily in Japan and Europe. During the year, Sony enlarged its entire MD product lineup including MD Walkman models, MD personal component stereo systems, MD decks, and car MD players. These actions reinforced Sony's position at the forefront of the industry.

This MD deck permits editing and the input of song titles on a PC.

One new MD Walkman, introduced in Japan, the United States, and Europe, has a recording capability yet is only 19.7mm thick. Sony also launched a model worldwide that can play continuously for up to 6 hours on a single AA alkaline battery. A new lineup including these models contributed to market expansion.

The MD personal component stereo system with a 3-disc MD changer and 3-disc CD changer, which has been a hit in Japan, offers various recording and editing possibilities. For MD decks, Sony introduced in Japan a model that can be connected to a PC to allow editing and the input of song titles.

Looking ahead, Sony will work toward expanding MD system sales in the United States and other regions where high-growth potential exists. To achieve this objective, Sony plans to introduce models that are even more compact in size, and to continue proposing innovative ideas for using MD systems with PCs.

CD Players

In the portable CD player sector, Sony continued to revitalize the marketplace by introducing models that offer advances in terms of compact size, light weight, and improved specifications. Examples include a unit that is only 20.1mm thick and weighs 175 grams, and units offering an extended continuous playback capability.

Sales also climbed for CD radio-cassette tape recorders and CD players for the home, mainly in the United States, the largest single market for these products.

IC Recorders

Incorporating flash memory, IC recorders combine ultra-compact size and light weight with simple recording and playback operation. These characteristics make IC recorders ideal for use in noting various memos and ideas. During the year, Sony launched worldwide a model with a 4MB(Megabyte) flash memory. This enables 16 minutes of continuous digital recording and playback in the standard mode and 24 minutes in the extended mode. Up to 495 individual entries can be stored in the memory. Furthermore, when the dedicated PC connection kit is used, a huge volume of audio data can be stored and managed on a PC.

Car Audio

With a broad line of car audio products, such as MD players, CD players, and cassette decks, Sony is taking an aggressive stance toward enlarging this business. During the year, units combining CD and MD players posted strong sales in Japan. MD players also performed well, with particularly strong sales growth in the United States and Europe.

« *Video* »

Home-Use Video Equipment

Sony extended its leading position in the home-use camcorder market during the year by posting a strong increase in sales. In this sector, the market for digital camcorders is growing rapidly, mainly in Japan, particularly due to their superior picture quality and compact size. Other merits include their ability to perform editing with virtually no loss of picture quality. Sony's Digital Handycam models were popular, particularly in Japan. Sony plans to continue to build on its solid position in digital camcorders.

Aggressive development of models with extended operating times, backed by the global product theme "stamina," has been an enormous success for Sony. New models distinguish Sony from the competition. One is an analog 8mm Handycam that can record continuously for up to 12 hours. One new Digital Handycam now allows up to 8 hours of recording time.

Furthermore, improvements to Sony's camcorder supply chain, from production through sales, has shortened lead times substantially, made product supplies more stable, and reduced inventories.

In the home-use video deck market, Sony was first in the industry to introduce a model that integrates the DV digital and S-VHS formats in a single deck. This product has been well-received in the market.

In the field of home-use camcorders, Sony is aggressively developing models with extended operating times and compact size. A newly introduced Digital Handycam (left) has an 8-hour continuous recording capability, and another new Digital Handycam is only as long and wide as a passport.

DVD-Video Players

Offering the outstanding functions, picture, and sound that take full advantage of the DVD format, Sony's new DVD-Video players performed well, especially in the United States. Making its debut in Japan during the year was a DVD-Video player with a 5.1-channel Dolby™ digital decoder. This system reproduces extremely realistic sounds.

Digital Still Cameras

Backed by rising use of PCs worldwide, the digital still camera market has been expanding rapidly. By storing photos on 3.5-inch floppy disks, Sony's Digital Mavica allows easy transfer of images to a PC. This feature has led to brisk sales worldwide. In addition to the Digital Mavica, Sony's expanding digital still camera lineup also includes the Cybershot, which employs flash memory to offer compact dimensions and light weight, and the MD Cybershot, which records photos on a MiniDisc.

Broadcast- and Professional-Use Video Equipment

An overwhelming number of broadcasters throughout the world depend on Sony's Betacam format. More than 100 million Betacam-format analog and digital cassette tapes store invaluable video programming. As the world's preeminent name in broadcast- and professional-use video equipment, Sony is firmly committed to introducing digital products and systems that can utilize these video resources.

During the year, Digital Betacam equipment deliveries were brisk to broadcasters and production studios alike. In the news production field, Sony introduced a new field editing system. The system is a new member of the Betacam SX series, which was unveiled in late 1996. The editing system enables rapid editing of news recordings at the scene and allows system separation for added convenience.

In 1998, U.S. terrestrial TV stations plan to begin digital broadcasts. In response, Sony has developed high-definition (HD) format broadcasting systems, which offer superb picture quality. Based on the MPEG world concept, Sony added a new lineup of high-resolution video server systems that use the industry-standard MPEG2 digital video compression technology. Sony displayed these new products and other systems including Betacam SX equipment based on MPEG2 technology at the April 1998 National Association of Broadcasters (NAB) Show in Las Vegas. Sony also displayed DVCAM equipment that offers playback compatibility with the consumer-use DV format. In addition to winning excellent reviews from many broadcasters worldwide, Sony equipment earned many large-scale orders at the NAB Show.

« Televisions »

Color TVs

Sony's Wega home-use color TVs with the industry's first flat-surface cathode ray tube (CRT) have been a huge success in Japan ever since the first model was put on sale in December 1996. The Wega series has contributed to growth in Sony's TV sales and market share in Japan. Sony introduced these TVs in Europe and Asia during the year, generating an extremely favorable response. Sony is promoting these models worldwide, including a model that can receive digital terrestrial broadcasts in the United States, which are scheduled to begin in 1998.

The top-of-the-line Wega model launched in Japan during the year incorporates Sony's new Digital Reality Creation technology. Taking advantage of a unique Sony digital signal processing algorithm, this technology creates an image from standard NTSC TV signals with twice the density of vertical and horizontal lines, thereby yielding an even higher quality picture.

Moving closer to markets is a key strategy of Sony's manufacturing activities. In line with this policy, Sony started production of color TVs in Slovakia in October 1997. In response to expansion of the Wega series, production capacity of FD Trinitron CRTs, which have flat-surfaces, will be expanded in the United States, Europe, and Asia.

Projection TVs and Professional-Use Projectors

Achieving efficient use of space thanks to their slimness, projection TVs are enjoying growing demand for use in home theaters, mainly in the United States. Sony differentiates itself from

During the year, Sony added a 32-inch Hi-Vision model to the lineup of Wega home-use color TVs in Japan. The simulated picture shows a scene from Sony Pictures Entertainment's hit film As Good As It Gets.

competitors by offering higher picture quality and larger screen sizes. This strategy contributed to another year of higher sales in the United States, mainly for large-screen models. In Japan, Sony introduced Wega Screen high-resolution LCD projection TVs. These models incorporate a MUSE decoder for viewing of Hi-Vision broadcasts on 43-inch and 50-inch screens with ease.

The market for professional-use projectors for PC presentations is expanding. During the year, Sony introduced a model in Japan and overseas markets that has an extremely bright image thanks to the use of a device developed by Texas Instruments Incorporated.

« Information and communications »

Personal Computers

Sony has built on the September 1996 introduction of VAIO home-use PCs in the United States by adding original functions and designs. These innovations have offered new ways of enjoying audiovisual equipment and PCs to a wide range of customers. In Japan, the VAIO mini-tower PC and the VAIO notebook PC were launched in July 1997. The mini-tower PC makes it easy to create video CDs and utilize digital photos and still images captured from digital video. A new ultra-slim VAIO notebook PC was an enormous hit when it came on the market in Japan in November 1997. This model features an outer case made of a magnesium alloy that is both light and attractive. This sleek exterior complements the computer's advanced functions, which include automatic collection of e-mail. Sony plans to introduce this series in the United States in the summer of 1998. In March 1998, another member of the VAIO PCs made its debut in Japan: the VAIO Compo PC, which enables music editing from products such as an MD deck that can connect to a PC.

Computer Displays and Peripherals

In the computer display field, Sony is meeting the rising demand for larger screens and higher picture quality. Adding more value to displays is another theme. In May 1998, Sony was first in the world to begin selling a 21-inch computer display with a flat-surface CRT named FD Trinitron.

In computer peripherals, Sony brought to market a succession of new CD-ROM and CD-R drives that can support higher signal processing speeds. In tandem with the growth in hard disk capacity and the spread of servers, demand climbed for tape drives used for data backup. As a next-generation data storage system, Sony and Fuji Photo Film Co., Ltd. jointly developed a high-capacity 200MB floppy disk system called HiFD that is backward-compatible with existing 3.5-inch floppy disks; this product is scheduled to go on sale in the second half of 1998.

Digital Cellular Phones

During the year, sales of Sony's digital cellular phones grew sharply in tandem with enlargement of the market worldwide. In the United States, expansion of the CDMA (Code Division Multiple Access) service area sparked an increase in monthly production of these phones to 400,000 units at the joint venture of Sony and QUALCOMM Incorporated. In Japan, new PDC (Personal Digital Cellular) handsets, which are compact, light and incorporate Jog Dial control, posted strong sales. Good sales results were also recorded in Europe by ultra-compact GSM (Global System for Mobile Communications) handsets, which also feature Jog Dial control.

Digital Broadcast Reception Systems

With an eye on the rapid proliferation of networks, Sony is moving aggressively into the field of household information and communications terminals, including digital satellite broadcast reception systems. During the year, sales were again brisk for reception systems for CANAL+ digital satellite broadcasts in Europe. In Japan, Sony began marketing new products for SKY PerfecTV! digital satellite broadcasts in April 1998. SKY PerfecTV! is expected to launch an official pay service in July 1998. Also, looking toward the digitization of cable TV in the United States, Sony announced a plan in January 1998 to form a strategic alliance with NextLevel Systems Inc. of the United States (now called General Instrument Corp.), to jointly develop digital TV technologies.

The VAIO Compo PC launched in Japan in March 1998 skillfully incorporates a design that is both compact and fitting for audiovisual components. Noise from the main unit is kept down by sound suppression technology.

« Electronic components and other »

Semiconductors

In response to the fast pace of digitization in audiovisual equipment, Sony stepped up development and production of the key devices essential to differentiate its products. During the year, sales grew for LSIs used in video CD, MD products, digital camcorders, and cellular phones due to higher demand for these products. Sales of high-resolution CCDs for digital still cameras also performed well. In the memory business, which was negatively affected by the weakness in the PC market, Sony concentrated on higher value-added products such as ultra-speed SRAM (static random access memory) chips. To meet rising demand for semiconductor lasers, essential elements of CD, DVD and other optical disk equipment, Sony newly constructed a fully integrated production system, which conducts all production operations from wafer processing to final assembly.

To preserve a competitive edge in the semiconductor business while at the same time controlling capital expenditures, Sony entered into strategic alliances during the year. One alliance covers the development, design and production of next-generation system LSIs with Fujitsu Limited. These devices are critical to making electronic equipment smaller while raising performance and cutting power consumption. Preparations are going forward for the start of mass production in the fall of 1999.

Liquid Crystal Display (LCD)

During the year, high-temperature polycrystalline silicon (Poly-Si) thin-film transistor (TFT) LCDs with higher transparency and picture quality, particularly applicable in view-finders of camcorders and projectors, recorded favorable sales. To win out against competition to develop better LCDs, resulting from a trend toward LCD panels with greater resolution and brightness, Sony is continuing its efforts to streamline all processes including shortening the time taken for development, by establishing a comprehensive system which covers design, development, and production. In the low-temperature, Poly-Si TFT LCD field, in which demand is expected to increase for applications such as monitors on camcorders and information-related equipment, Sony has succeeded as one of the first companies to bring such products to market. Sales for these products are steadily expanding. Furthermore, Sony and Toyoda Automatic Loom Works, Ltd. of Japan have created a 50-50 joint manufacturing venture in this field, ST Liquid Crystal Display Corp. The company plans to begin mass production in the spring of 1999.

Electronic Components

Sony develops and produces such key electronic components as optical pickups and spindle motors for CD, MD and DVD applications, as well as magnetic heads for digital VTRs and data storage systems.

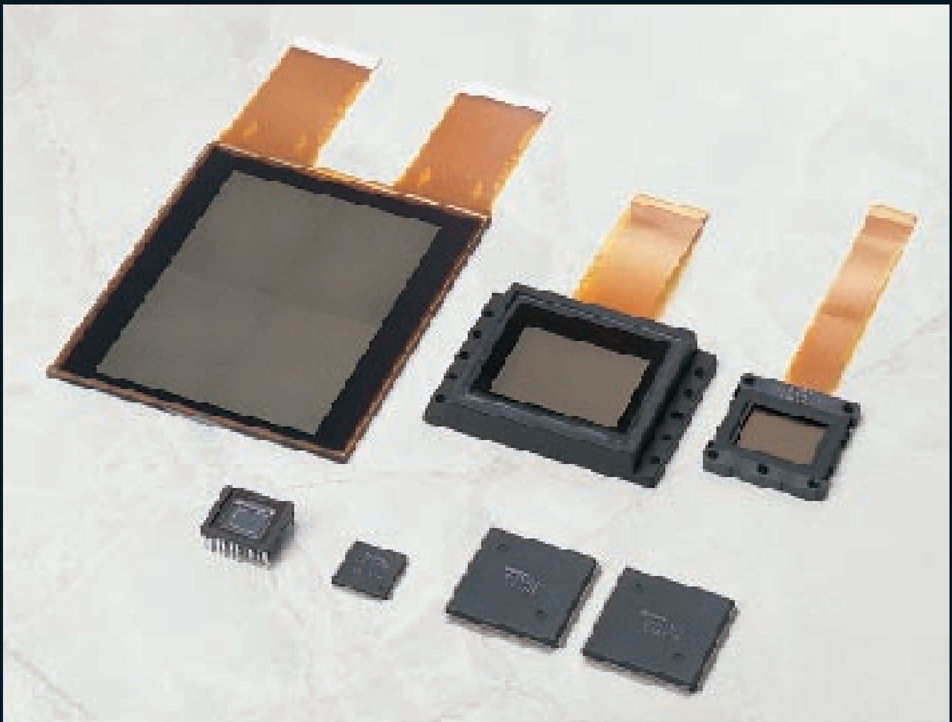
In the optical pickup sector in particular, Sony maintains a worldwide market share exceeding 50%. During the year, output climbed as demand grew for video CD and MD products. In addition, Sony developed an optical pickup that can read CD-ROMs at a maximum 24X speed and perform high-speed writing to CD-R and CD-RW disks.

In the field of spindle motors for CD and DVD equipment, Sony introduced a new product that attenuates the vibrations from a rapidly spinning disk to ensure the stable retrieval of data.

Another newly developed product is a high-density recording head for the HiFD high-capacity floppy disk system, which is planned for release in the near future.

Lithium-Ion Batteries

As a small, lightweight, rechargeable battery, lithium-ion batteries are in increasing demand as the market for portable electronic equipment grows. A pioneer in this field, Sony continued to respond to diversifying customer needs by ensuring a stable supply of batteries and expanding its lineup for cellular phones and other applications. However, sluggishness in the PC market adversely affected the demand for these types of batteries during the year.



[front line from the right]
High-performance single chip MPEG2 AV decoder and video encoder
Interface LSI for connections between digital AV equipment and PCs
High-resolution color CCD for digital still cameras (1/2-inch, 1.45 million pixels)
[back line from the right]
High-transparency LCD for data projectors (0.9-inch, 485,000 dots)
LCD for SVGA AV single-panel projectors (1.6-inch, 1.46 million dots)
Reflective 1/4 VGA color LCD (4-inch, 230,000 dots)—currently under development

[Game]

Since the launch of the PlayStation game console in December 1994, Sony Computer Entertainment (SCE) has actively promoted its business in Japan, North America, and Europe. As of March 31, 1998, cumulative production shipments to markets worldwide have reached 32.82 million consoles and 236 million software units.

Large-Scale and Flexible Production Capabilities

A new model of the PlayStation game console went on sale in Japan in November 1997. The new Dual Shock controller, which is supplied as a standard peripheral, can generate two types of vibrations and allow improved control of the game, adding a new dimension to the realism of video gaming. Further progress was made in reducing costs and raising production efficiency by reducing the number of parts necessary to produce consoles. Backed by these efforts, SCE increased monthly console output to 2 million units during the last three months of 1997 to meet peak-season demand worldwide.

Broadening the Lineup of Game Software

The popularity of PlayStation is due to the breadth and high quality of games that are available to consumers. Software publishers in Japan and overseas are releasing a continuous flow of attractive titles for PlayStation. In Japan, *Bio Hazard 2* by CAPCOM CO., LTD. and *Derby Stallion* by ASCII CORPORATION were both major hits during the year under review. SCE's *Gran Turismo* and *Minnano-Golf* also sold about 2 million units and 1.5 million units, respectively. Following the success in Japan early in 1997, *Final Fantasy VII* from SQUARE CO., LTD. was a smash hit in North America and Europe.

Teruhisa Tokunaka
President and Chief Executive Officer
Sony Computer Entertainment Inc.

Message From Top Management

During the 1997 year-end sales season, PlayStation game consoles posted top sales in Japan, North America and Europe, exceeding past industry records. SCE intends to sustain the momentum and further expand its market. In February 1998, SCE announced the development of a miniature-size PDA (Personal Digital Assistant) for personal entertainment. Preparations are under way with the aim to launch the PDA during the coming winter season in 1998. By bringing new ways of fun and enjoyment to homes and individuals, SCE will attract new customers to further expand the market for computer entertainment.

PlayStation home-use game console

Thomas D. Mottola
President and Chief Executive Officer
Sony Music Entertainment Inc.

Message From Top Management

Sony Music Entertainment Inc. (SMEI) achieved its most successful year in history with record high results. As we begin our new year we are well positioned to build upon this achievement. Our mission, based upon a passionate commitment to long-term artist development, mandates continued investment in new and established talent in order to compete aggressively and establish each of our companies around the world as the market leader. I firmly believe the outlook for SMEI has never been brighter. We are committed to building upon our successes and continuing with the creative spirit that is fundamental to our sustained growth.

Sony Music Entertainment Inc. (SMEI)

Celine Dion's *Let's Talk About Love* and the *Titanic* soundtrack each sold more than 19 million units, and were the top-two selling albums in the world. Mariah Carey's *Butterfly* (8 million units) and Oasis' *Be Here Now* (7 million units) enjoyed global success, followed by Barbra Streisand's *Higher Ground*, Celine Dion's *Falling Into You*, Savage Garden, and the *Men in Black* soundtrack (over 4 million units each). Other multimillion-selling releases included albums by Fiona Apple, Bone Thugs-N-Harmony, Michael Jackson, Jamiroquai, Ricky Martin, Pearl Jam, Will Smith, Wham!, and the soundtrack from *My Best Friend's Wedding*.

Artist and Business Development

Debut and developing artists selling more than 500,000 units during the year under review included Savage Garden (Australia); Meja, Monica Naranjo, Jimmy Ray, Finley Quaye, and Wes (Europe); Alejandro Fernandez (Mexico); and Fiona Apple, Ben Folds Five, Ginuwine, Amanda Marshall, Maxwell, and Uncle Sam (North America). SMEI pioneered new online technologies and forged several relationships with key Internet service providers, and Sony Music Nashville re-established the Monument label.

International Growth

Sony Music International (SMI) increased sales throughout its territories with global bestsellers and local repertoire hit albums by Chang-Jung Im, Nakarin Kingsak, CoCo Lee, AR Rahman (Asia); Amanda Marshall and Our Lady Peace (Canada); Claudio Baglioni, Jean-Jacques Goldman, the Kuschelrock 11 compilation, Monica Naranjo, Meja, Jimmy Ray, Finley Quaye, Magnus Uggla, and Wes (Europe); and ZeZe de Camargo y Luciano, Alejandro Fernandez, and Ricky Martin (Latin America). SMI expanded its roster throughout Asia with a cooperative arrangement in China to develop a Chinese-language repertoire and new signings including Cantopop star Leon Lai and Taiwanese superstar Jeff Chang. SMI also extended its European network of label affiliations with several strategic investments.

Classical Movements

Sony Classical enjoyed phenomenal success with the *Titanic* soundtrack. Other bestsellers included albums by Michael Bolton, Yo-Yo Ma, Itzhak Perlman, and Christmas from Vienna IV. New signings included *Titanic* composer James Horner, tenor Marcelo Alvarez, violinist Eileen Ivers, baritone Jubilant Sykes, and composer/performer Joe Jackson.

Music Publishing

Sony/ATV Music Publishing achieved strong results and earned BMI Publisher of the Year and ASCAP Song of the Year Awards. Agreements were signed with Joni Mitchell, LL Cool J, Miramax Films, October Films and Experience Hendrix.

Sony Music Entertainment (Japan) Inc. (SMEJ)

During the year, SMEJ reviewed its management decision-making processes and reformed its internal organizations primarily in the production and promotion divisions. These steps are aimed at constructing a new system for artist development. In addition, SMEJ took measures to restructure the marketing system. The measures include reinforcing its relationship with leading artists and accepting sales operations on consignment. Furthermore, SMEJ carved out new businesses during the year by establishing a company to operate a broadcast programming business through digital satellite broadcasting, and a concert venue management company. Despite deceleration in growth in the music market in Japan, SMEJ achieved favorable results thanks largely to overall sales expansion from hits in Japan and highly profitable greatest-hits albums. Hit artists who contributed to the sales expansion include L'Arc~en~Ciel, DREAMS COME TRUE, and T.M. Revolution.

Celine Dion's Falling Into You *and* Let's Talk About Love *were the biggest selling albums in the world released in 1996 and 1997.*

John Calley
President and Chief Executive Officer Sony Pictures Entertainment Inc.

Message From Top Management

Last year, we began the transformation of Sony Pictures Entertainment (SPE). During the year under review, we started to hit our stride in becoming a consistent global entertainment leader. Our motion picture companies released a string of hit films that generated the best worldwide box office performance in history. Now we are building on that momentum by reorganizing our motion picture business to further increase production, efficiency and strategic focus, centralizing our motion picture production under the Columbia banner. The Columbia lady, synonymous with nearly 75 years of cinematic excitement, is a strong partner for Sony's global marketing and technological brand name in our commitment to create unique franchise films for audiences worldwide.

Our Television Group also achieved industry leadership by placing more shows on the U.S. networks than any other studio. We intensified our international growth strategies, expanding into local motion picture production as well as creating branded television programming and other new production and distribution platforms worldwide. And we coined a new SPE tag line that summarizes all of these initiatives: "Lighting up screens around the world"—movie screens, television screens and computer screens.

Record-Setting Motion Picture Performance

In the 1997 calendar year, the Columbia TriStar Motion Picture Group set all-time industry records by grossing $1.27 billion at the U.S. box office and more than $2.3 billion worldwide. SPE's success was propelled by blockbuster hits such as *Men in Black*, the year's top-grossing film worldwide and SPE's top-selling video release of all time, *Air Force One*, *My Best Friend's Wedding,* and the critically acclaimed *As Good As It Gets,* which won two major Academy Awards®. SPE's diverse portfolio of hits also included *The Fifth Element*, *Anaconda,* and *I Know What You Did Last Summer*.

Revenue growth was further enhanced by Columbia TriStar Home Video, which achieved four of the five top-selling direct-to-sales video releases in its history. SPE expanded its creative family by forging major relationships with top talent, including producer/filmmakers Roland Emmerich and Dean Devlin, writer Ron Bass and producer Sydney Pollack. SPE also implemented President John Calley's global motion picture production strategy by forming a local German motion picture company as part of a long-term alliance in the German marketplace.

Television Maintains Leadership in Global Content Creation and Distribution

Columbia TriStar opened the 1997/98 television season as the only studio with a series on every network and every night of the week. SPE's television business continued its leadership in two other valuable formats with the most popular game shows in the world, *Wheel of Fortune* and *Jeopardy!*, and the top-rated daytime programs, *The Young & the Restless* and *Days of Our Lives*.

The long-term value of SPE's programming distribution has been underscored by the unprecedented demand for the second syndication sales cycle of the blockbuster comedy *Seinfeld*. SPE also reaffirmed its commitment to global leadership in content creation and distribution by joining with Liberty Media Corporation in acquiring Telemundo Group, Inc., pending regulatory approval, to enter the fast-growing Spanish-language marketplace in the United States and Latin America.

SPE already develops original programming in eight languages and during the year launched the AXN branded channel, devoted to action/adventure programming, in Asia. SPE continued its commitment to capitalizing on growth opportunities throughout the international marketplace for both motion pictures and television, with more than 20 international channel ventures reaching over a billion viewers around the globe. International revenues from licensing films and programming from the studio's library of more than 3,500 motion pictures and 40,000 television episodes have increased 72% during the past two years.

Theatre Operations

Loews Theatres added new locations and expanded existing locations to create a total of 91 new screens. Including Loews Theatres, Sony Theatres, Magic Johnson Theatres, and Star Theatres, the Loews Theatres Exhibition Group operates 1,038 screens in 139 locations.

During the year, Loews Theatres agreed to merge with Cineplex Odeon Corporation forming one of the largest theatrical exhibition companies in the world. The Loews Cineplex Entertainment Corporation will be a stand-alone company with the potential to increase the value of the exhibition assets for Sony, with planned expansion for the theatre circuit throughout the world. The new company will have over 2,700 screens with 425 locations in North America.

The action comedy Men in Black *anchored SPE's record-breaking motion picture slate, generating $581 million in worldwide box office receipts—more than any other SPE film in history.*

[Insurance]

Sony Life Insurance Co., Ltd. is the nucleus of the Sony Group's insurance business. It was in 1979 that Sony and The Prudential Insurance Company of America, the largest life insurer in the United States, formed a joint venture company. This joint venture agreement was dissolved in 1987. Since the commencement of operations in 1981, Sony Life has steadily expanded its business with efficient provision of policies that were tailor-made to match the requirements of each customer. During the year under review, Sony Life's net increase in individual life insurance-in-force was highest among all 44 life insurers operating in Japan.

Sales System

Sony Life's sales system is distinguished most of all by the policy of using highly-qualified Life Planner financial consultants to serve customers. As of March 31, 1998, there were approximately 3,700 such consultants at Sony Life, of whom some 2,300 at least possess the AFP (Affiliated Financial Planner) certification from the Japan Association for Financial Planners. In addition, all Life Planners have participated in Sony Life's own thorough training program. This enhances their ability to offer accurate advice regarding customers' financial assets and household budgets as well as the management of corporate assets. Sony Life maintains an extensive service network including 94 Life Planner branch offices, 23 regional sales offices, and 1,400 independent agencies at the end of March 1998.

Product and Asset Management Policies

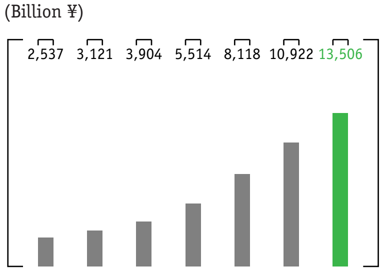
The composition of Sony Life's products reflects the needs of its customers. Rather than endowment and annuity insurance and other savings-type products, the company focuses on protection-type products such as whole life and term insurance. This philosophy is linked to a prudent asset management posture that does not pursue excessive risk to gain higher yields. Assets in the general account are invested mainly in government and corporate bonds in order to maintain a portfolio that ensures stable returns over the medium and long terms. During the year, almost all of the increase in assets was invested in government and corporate bonds. And because loans are extended solely to policyholders, Sony Life maintains a sound management structure free of bad debts. The result is that Sony Life's solvency margin (1,545.5%) is considerably higher than is called for by the administrative guidelines in Japan for life insurers.

Ken Iwaki
President and Chief Operating Officer
Sony Life Insurance Co., Ltd.

Message From Top Management

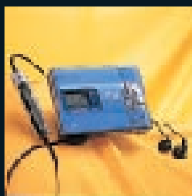
Sony Life places priority on offering services of the highest quality, primarily in the form of effective life insurance and consulting. Our aim is to ensure the financial security and stability of our customers. Our basic mission, therefore, is to help make dreams come true, a concept that we share with the entire Sony Group. During the year, Sony Life increased its capital, realigned the Board of Directors and introduced the position of corporate executive officer. Through these means, we reinforced our financial position and further improved the soundness of Sony Life's operations. Sony Life also obtained an IFS (Insurer Financial Strength) rating from Standard & Poor's for claims paying ability. Looking ahead, we will adhere to our strategy of concentrating on the life insurance business. As we do so, we will make effective use of funds derived from the increase in our capital and pursue plans to enter the life insurance markets in other Asian countries. Above all, we will redouble our efforts to make Sony Life the company of choice for customers.

Individual Life Insurance-in-Force
(Billion ¥)



During the year, Sony Life recorded the largest net increase in individual life insurance-in-force among all life insurance companies operating in Japan.

Life Planners are experienced in management and knowledgeable about taxes, legal matters, economics and other specialties. The planners can accurately evaluate and analyze all aspects of a customer's requirements, present and future. By utilizing this information along with sophisticated computer software, planners conduct studies from many perspectives to formulate a plan for each customer.

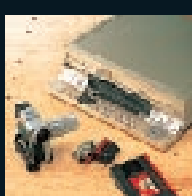


Electronics
This MD Walkman incorporates a recording capability but is only 19.7mm thick.

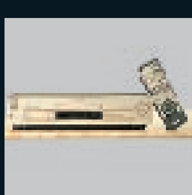
With a 3-disc MD changer and 3-disc CD changer, Sony's MD personal component stereo system offers outstanding versatility in editing audio programming.

The latest addition to Sony's IC recorder lineup.

This new car audio incorporates a 3-disc MD changer and a CD player in a single unit.

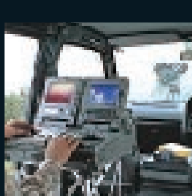


This model has both DV digital and S-VHS formats in a single deck. Editing of recordings from DV format digital camcorders is simple with this new product.

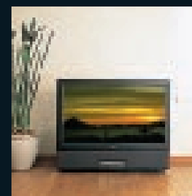


This new DVD-Video player was introduced in Japan and the United States.

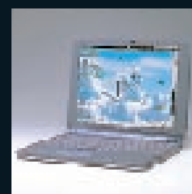
Recording images on 3.5-inch floppy disks, Sony's Digital Mavica still camera can store up to 40 pictures on a single disk.



Introduced during the year, the Betacam SX field editing system incorporates two video decks to offer outstanding versatility for on-site work.



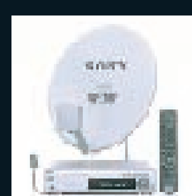
Equipped with Digital Reality Creation technology, this 43-inch LCD projection TV creates better picture quality from any source, including standard TV signals.



The new ultra-slim VAIO notebook PC features an outer case made of a magnesium alloy that is both light and attractive.

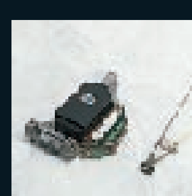
With an FD Trinitron CRT, this 21-inch computer display produces a natural, vivid picture that is free of distortion and reflections over the entire surface.

In March 1998, at the CeBIT 98 information and telecommunications exhibition in Germany, the HiFD high-capacity floppy disk system drew rave reviews.



Sony's digital satellite broadcast reception system for SKY PerfecTV!, launched in Japan, is equipped with a new and original EPG (Electronic Program Guide) to enable easy selection of specific programs.

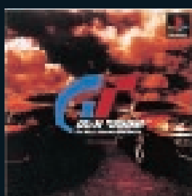
During the year, Sony supplied NTT DoCoMo in Japan with a new PDC digital cellular phone that is easy to handle, lightweight and compact.



(right) Newly developed magnetic head for HiFD drive
(left) Optical pickup for CD-ROM, CD-R, and CD-RW drives

Cylindrical and prismatic lithium-ion batteries

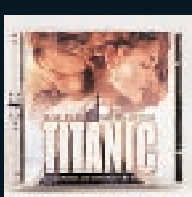
Game
The new Dual Shock controller can generate two types of vibrations, adding a new dimension to the realism of video gaming.



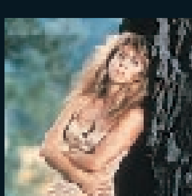
Gran Turismo *from Sony Computer Entertainment (SCE) is a major hit game title in Japan.*

Game characters in hit titles PARAPPA THE RAPPER *and* Crash Bandicoot *from SCE.*

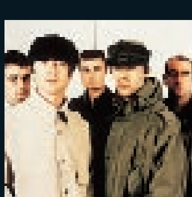
A prototype of a miniature-size PDA will be launched by SCE during the coming winter season in 1998.



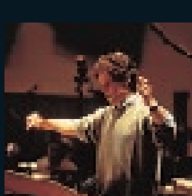
Music
Titanic *has become the biggest selling original score album in history.*



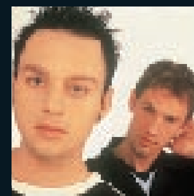
Butterfly's *"Honey" was Mariah Carey's 12th No. 1 single, the most of any solo female artist in the rock era.*



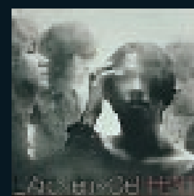
Sales of Oasis' three albums have surpassed 25 million units, with Be Here Now *voted Album of the Year in Rolling Stone magazine.*



The Titanic *score composed by James Horner received twin Golden Globe, Golden Satellite, and Academy Awards® for Best Original Score and Best Original Song.*

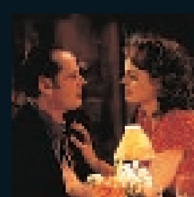


Savage Garden's eponymous debut album received a record-high 10 ARIA Awards (Australia's Grammy) including Best Group, Best Single, and Song of the Year.

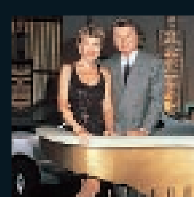


HEART *by L'Arc~en~Ciel achieved strong sales in Japan.*

Pictures
The romantic comedy My Best Friend's Wedding *scored as a major box office success and a hit direct-to-sales video release.*

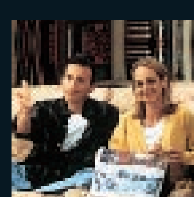


The critically acclaimed blockbuster As Good As It Gets *earned Academy Awards® for Jack Nicholson as Best Actor and Helen Hunt as Best Actress.*



Wheel of Fortune *remains the most popular game show in the world and, underscoring the global appeal of Sony Pictures Entertainment's programming, is shown in 49 countries on six continents.*

Castle Rock's blockbuster comedy Seinfeld *is creating unprecedented demand for its future second syndication sales cycle.*



The hit comedy Mad About You, *starring Paul Reiser and Academy Award-winning Helen Hunt, is a mainstay of Sony Pictures Entertainment's industry-leading roster of prime-time series and has been renewed for its seventh season.*

Other
Scheduled to open in San Francisco, spring 1999, Metreon has drawn increasing local and national attention with the promise of 15 new movie theatres and the SONY•IMAX® Theatre, dining, shopping, and family attractions.

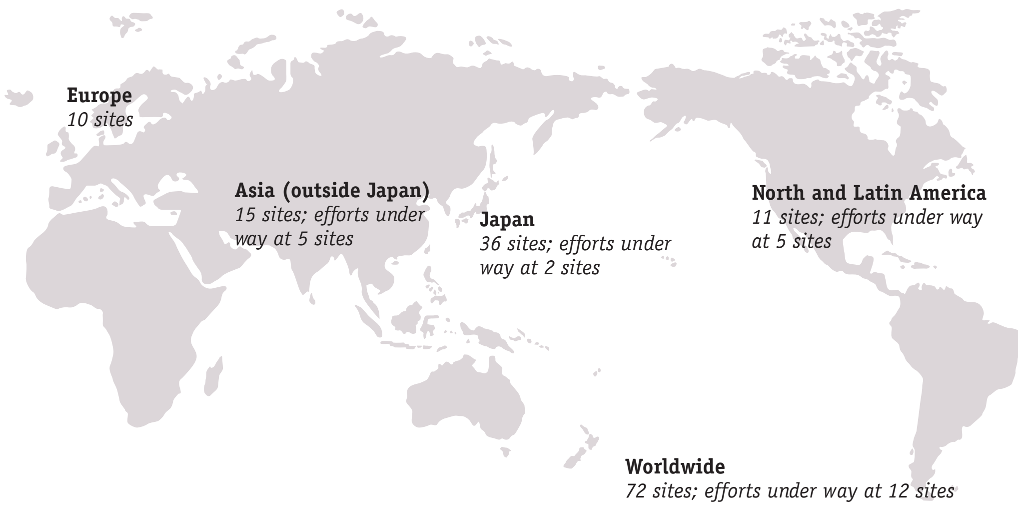
[Environmental Activities at Sony]

Recognizing that environmental protection is one of the most pressing issues facing mankind today, Sony incorporates a sound respect for nature in all of its business activities. Based on this philosophy, Sony conducts numerous environmental programs.

Establishment of Environmental Management Systems

Sony believes that environmental activities are important elements of corporate management. To conduct these activities in a systematic and efficient manner, Sony is making a concerted effort to meet the international ISO-14001 standard for environmental management. As of the end of March 1998, 72 Sony production facilities and 9 operating bases worldwide were ISO-14001 certified. Preparations are proceeding toward obtaining this qualification at all major bases by the end of March 2001.

ISO-14001 Certified Sony Production Facilities



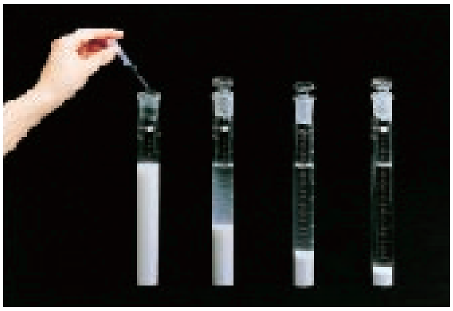
(As of March 31, 1998)

Environmentally Sound Product Development

Sony's Greenplus 2000 project is working toward its goal of incorporating environmental issues as part of the development process for all Sony products from the planning and design stages by the year 2000. The project aims to reduce materials with a high environmental impact and promote ways to conserve energy and resources. Among the Sony products launched since this program began are easily dismantled color TVs and VAIO notebook PCs with easily recycled magnesium alloy outer cases.

New Technologies Addressing Environmental Issues

New technologies for promoting environmental protection are being developed at the Center for Environmental Technologies, which is located at the Sony Research Center. Several key breakthroughs are already being applied. One example is packaging materials like Cellu Mold and used-paper pulp mold that are made from recycled paper. Another is a recycling method for styrene foam. By dissolving the foam in liquid limonene, a substance extracted from citrus rinds, polystyrene resin can be extracted for reuse. Sony also succeeded in creating a method to transform discarded plastic, such as old video cassette shells, into a water-soluble polymer. The polymer can then be used as a condensing agent to treat waste water.



Made from discarded plastic, this water-soluble polymer is used in a condensation process.

Disassembling a television at the DC Recycle Research Center

A Solid Commitment to Reducing Energy Consumption

As interest in the prevention of global warming rises worldwide, Sony is taking a variety of actions to reduce energy consumption. At the product level, the development of products with low power consumption is a central issue. During the year under review, Sony introduced many products such as a personal component stereo that needs less than 3 watts of power in the standby mode.

In the United States, Sony Electronics Inc. became a partner in the Energy Star Buildings Program and the Green Lights Program, both being promoted by the U.S. Environmental Protection Agency. To reduce energy for heating and cooling, the roofs of company buildings are coated with a reflective, heat-resistant paint. Energy-efficient lighting fixtures and other steps further cut power requirements.

Programs to Expand Recycling

In concert with steps to expand product recycling, Sony is pursuing the development of recycling technology. In Europe, The Environmental Product Laboratory has been established at Sony International (Europe) GmbH. This unit studies methods to improve ease of product disassembly and the reuse of resources. Sony also participates in CARE Vision 2000, an important project within the EUREKA (European Research Coordination Action) initiative. In Japan, the DC (Display Company) Recycle Research Center was inaugurated in Aichi Prefecture to develop recycling techniques for color TVs, computer displays and other display products. Activities at this center focus on making recycling more efficient, such as by providing design sections with feedback on the actual benefits of technologies gained from many years of research.

Contribution to Local Environments

Sony's dedication to the environment extends to the community as well. In Japan, Sony Broadcast Products Corporation inaugurated an Environmental Volunteer Registration System in 1997. Volunteers take part in activities to keep communities green and clean. Employees of Sony Corporation also serve as instructors at environmental seminars held at local junior high schools, conduct demonstrations of Sony's liquid limonene styrene foam recycling system, and engage in a variety of other activities. In the United States, volunteers from Sony Pictures Entertainment take part in many programs, including planting vegetation in cooperation with the parents and guardians of local junior high school students.

[Management]

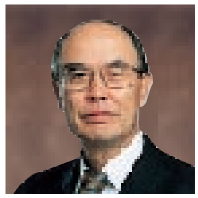
[Founder]

Founder and Honorary Chairman

Akio Morita

[Board of Directors] **Corporate Executive Officer*

Norio Ohga*
Chairman and Representative Director, Chief Executive Officer



Tsunao Hashimoto*
Vice Chairman and Representative Director

Nobuyuki Idei*
President and Representative Director, Co-Chief Executive Officer

Minoru Morio*
Executive Deputy President and Representative Director

Kozo Ohsone*
Executive Deputy President and Representative Director

Yoshiyuki Kaneda*
Executive Deputy President and Representative Director

Tamotsu Iba*
Executive Deputy President and Representative Director

Peter G. Peterson
Director
(Chairman of The Blackstone Group)

Kenichi Suematsu
Director
(Advisor of The Sakura Bank, Limited)

Hideo Ishihara
Director
(Chairman of Goldman Sachs (Japan) Ltd.)

[Corporate Auditors]

Standing Statutory Auditors

Nobuo Kanoi
Akihisa Ohnishi
Yoshisuke Mohri

Statutory Auditor

Kazuaki Morita

[Corporate Executive Officers]

Corporate Executive Vice Presidents

Kiyoshi Yamakawa
Suehiro Nakamura
Kenichi Oyama

Corporate Senior Vice Presidents

Hideo Nakamura
Masayuki Takano
Yasumasa Mizushima
Masayoshi Morimoto
Shizuo Takashino
Akiyoshi Kawashima
Mario Tokoro

Corporate Vice Presidents

Toshitada Doi
Seiichi Watanabe
Kenji Hori
Katsuaki Tsurushima
Kunitake Ando
Takeo Eguchi
Shigeyuki Ochi
Nobuyuki Watanabe
Sunobu Horigome
Tadasu Kawai
Mitsuru Ohki
Yoshio Nishi
Yutaka Nakagawa
Yukio Kubota
Katsumi Ihara

[Group Executive Officers]

Ken Iwaki
Junichi Kodera
Yoshio Ishigaki
Shugo Matsuo
Sumio Sano
Teruaki Aoki
Motoyasu Kanasugi
Shigeo Maruyama
Toshiyuki Yamada
Masahiro Hayashi
Toshiharu Sawada
Masao Morita
Teruhisa Tokunaka
Ken Kutaragi
Jakob J. Schmuckli
Howard Stringer
Thomas D. Mottola
John Calley

(As of May 7, 1998)

[Financial Review]

Effective for the fiscal year ended March 31, 1998, Sony adopted Statement of Financial Accounting Standards No. 131 (FAS 131). This resulted in the reporting of business results based on new operating segments (refer to Note 19 of Notes to Consolidated Financial Statements). Segment information as well as certain items in the consolidated statements of income in prior fiscal years have been reclassified to conform to the presentation for the fiscal year ended March 31, 1998.

Sony also adopted FAS 128 during the fiscal year ended March 31, 1998. FAS 128 requires presentation of basic and diluted net income per share on the face of the statements of income (refer to Notes 2 and 4 of Notes to Consolidated Financial Statements). Net income per share amounts in prior fiscal years have been restated to conform with FAS 128.

RESULTS OF OPERATIONS

During the fiscal year ended March 31, 1998, Sony achieved record consolidated sales and operating revenue (herein referred to as “sales”) and earnings for the second consecutive fiscal year.

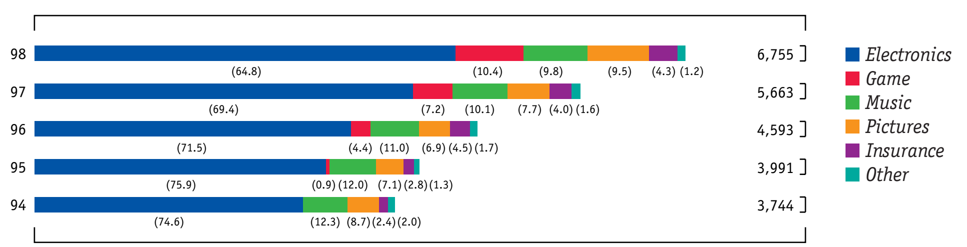
Sales

Consolidated **sales and operating revenue** rose 19.3% compared with the previous fiscal year, to ¥6,755.5 billion ($51,178 million). This performance reflects sales growth across all business segments as well as the yen’s depreciation.

Impact of Foreign Exchange Trends

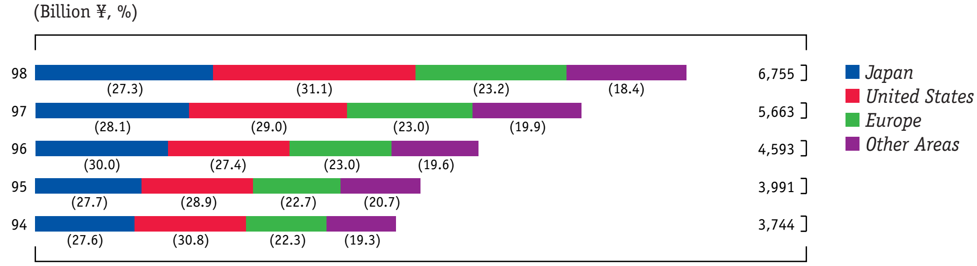
During the year under review, overseas (outside Japan) sales accounted for approximately 73% of Sony’s consolidated sales. During the year, the yen depreciated approximately 8% against the U.S. dollar and 11% against the British pound, but appreciated approximately 5% against the German mark, each in terms of average rates, compared with the previous fiscal year. It is estimated that sales and operating income would have been lower by approximately ¥291 billion ($2,205 million) and ¥110 billion ($833 million), respectively, than the reported figures if the average value of the yen had remained the same as in the previous fiscal year. Note that these estimates are obtained by simply applying the yen’s average exchange rate in the prior fiscal year to foreign currency denominated sales, cost of sales, and selling, general and administrative expenses of the year under review. Therefore, the estimate does not take into account the effect of foreign exchange fluctuations on prices of products and production and sales costs in each region of the world.

Sales and Operating Revenue by Business Segment (Percent of Consolidated Sales)*
(Billion ¥, %)



** Sales and operating revenue to customers*

Sales and Operating Revenue by Geographic Segment (Percent of Consolidated Sales)**
(Billion ¥, %)



*** Sales and operating revenue by location of customers*

To minimize the adverse effects of foreign exchange fluctuations on its financial results and to reduce inventory and cost, Sony promotes the localization of material and parts procurement, design, and manufacturing operations outside Japan. During the year, Sony expanded manufacturing operations mainly in North America and Eastern Europe. Overseas activities represented approximately 50% of total manufacturing output in Sony's Electronics business. Sony employs foreign exchange forward contracts and foreign currency option contracts to hedge against foreign exchange risks that arise from the export and import transactions of Sony Corporation and its consolidated subsidiaries. In addition, interest rate and currency swap agreements are used in connection with certain foreign currency denominated borrowings and debt.

During the second half of 1997, currency and economic turmoil occurred in Asia. However, the overall impact of this situation was positive for Sony's earnings during the year. This is mainly due to a decline in costs in Asia, a major manufacturing base for Sony. In the year under review, Asia accounted for approximately 13% of sales in Sony's Electronics business, while comprising approximately 25% of manufacturing. About 63% of this manufacturing output in Asia was exported for sale outside the region. However, Asian currency and economic turmoil may negatively affect Sony's results over the mid- to long-term.

Cost of Sales and Selling, General and Administrative Expenses

During the year, **cost of sales** rose 17.5% to ¥4,619.0 billion ($34,992 million), mainly due to higher sales. However, the ratio of cost of sales to consolidated sales improved 0.8 percentage point, to 71.5% due to the sales growth and cost reductions. **Research and development expenses** charged to cost of sales increased 12.6% to ¥318.0 billion ($2,409 million), mainly due to increases in the semiconductor business, information and communication business, and Game business, but declined by 0.3 percentage point as a percentage of sales, to 4.9%. Research and development expenses for the fiscal year ending March 31, 1999 are expected to exceed those of the year under review, mainly due to higher expenses in business areas such as broadcast-use equipment and digital network related equipment as well as the semiconductor business.

Selling, general and administrative expenses rose 16.6% to ¥1,345.6 billion ($10,194 million), mainly due to increases in sales, personnel expenses, and advertising costs in the Game business, but improved 0.4 percentage point as a percentage of sales, to 20.8%.

Figures in the above two paragraphs do not include the Insurance segment revenue and expenses.

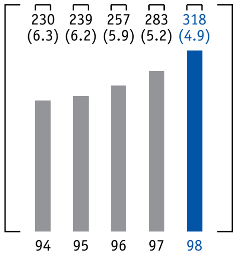
Operating Income

Operating income during the year grew by 40.5% to ¥520.2 billion ($3,941 million). Despite an increased operating loss in the Other segment, higher operating income in the Electronics, Music, Pictures, and Insurance segments, and particularly strong results in the Game segment, contributed to overall growth. Sales and operating income in the Game segment reached approximately 10% and 22%, respectively, of Sony's consolidated sales and operating income before elimination of intersegment transactions. As a percentage of sales, operating income improved by 1.2 percentage points, to 7.7%.

Other Income and Expenses

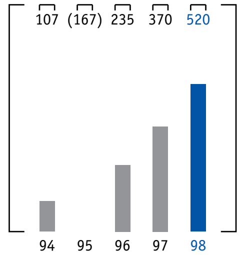
Other income decreased 9.4% to ¥84.0 billion ($636 million), while **other expenses** remained at ¥150.4 billion ($1,140 million) about the same as that in the previous fiscal year. The decline in other income is primarily due to a

R&D Expenses
(Percent of Consolidated Sales*)
(Billion ¥, %)

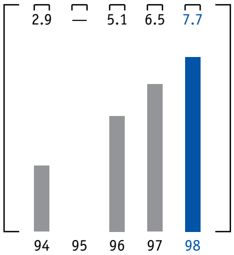


** Excluding Insurance revenue*

Operating Income (Loss)
(Billion ¥)



Ratio of Operating Income to Sales
(%)



decrease in the foreign exchange gain, net, compared with the previous fiscal year. Foreign exchange gains and losses mainly arise from the difference between the value of foreign currency denominated exports and imports when converted into various currencies using prevailing exchange rates and the value at settlement of these exports and imports. The rates used for settlement are primarily based on foreign exchange forward contracts and foreign currency option contracts that Sony employs to hedge risks from exchange rate fluctuations. Among other income and expenses, interest and dividends increased, mainly because of an increase in cash and time deposits and higher investment returns at overseas subsidiaries. Interest expense decreased, mainly due to lower outstanding debt at overseas subsidiaries. As a result, the balance of interest and dividend income less interest expense improved by ¥9.9 billion to net interest expense of ¥41.5 billion ($315 million).

Income Before Income Taxes

Income before income taxes during the year rose 45.2% to ¥453.7 billion ($3,437 million).

Income Taxes

Income taxes as a percentage of income before income taxes (the effective tax rate) declined 5.0 percentage points, to 47.4%. This decline is mainly attributable to improved performance at overseas subsidiaries which incurred operating losses in the previous fiscal year. Due to the reduction of the Japanese statutory income tax rate, effective April 1, 1998, the new statutory tax rate has been used in calculating the future expected tax effects of temporary differences. The effect of the enacted change in tax rate, which resulted in a reduction of income tax expenses, was insignificant (refer to Note 14 of Notes to Consolidated Financial Statements).

Net Income

Net income increased 59.2% to ¥222.1 billion ($1,682 million). **Basic net income per share** rose from ¥367.7 to ¥557.7 ($4.23) and **diluted net income per share** rose from ¥309.2 to ¥483.4 ($3.66).

Net income represented 3.3% of sales, up 0.8 percentage point, and the return on average stockholders' equity increased 3.0 percentage points, to 13.6%.

Results by Business Segment

The following discussion is based on segment information (refer to Note 19 of Notes to Consolidated Financial Statements).

Business Segment Information

Year ended March 31

Sales and operating revenue

(Yen in billions)	1997	**1998**	percent change 1998/1997
Electronics	¥4,132	**¥4,690**	+13.5%
Game	419	**722**	+72.3
Music	592	**695**	+17.3
Pictures	439	**643**	+46.7
Insurance	228	**291**	+27.7
Other	240	**248**	+3.3
Elimination	(387)	**(534)**	–
Consolidated	¥5,663	**¥6,755**	+19.3%

Operating income (loss)

(Yen in billions)	1997	**1998**	percent change 1998/1997
Electronics	¥ 239	**¥ 314**	+31.4%
Game	57	**117**	+105.0
Music	45	**54**	+19.6
Pictures	29	**36**	+22.9
Insurance	19	**20**	+6.4
Other	(1)	**(10)**	–
Corporate and elimination	(18)	**(11)**	–
Consolidated	¥ 370	**¥ 520**	+40.5%

Electronics

During the year, despite weak markets in Brazil and Asia, including China, many hit products and the yen's depreciation helped to increase Electronics sales by 13.5% to ¥4,690.1 billion ($35,531 million). Sales growth, cost reductions, and the yen's depreciation contributed to an increase in operating income of 31.4% to ¥314.5 billion ($2,383 million). As a percentage of sales in the segment, operating income improved by 0.9 percentage point, to 6.7%. However, late in the fiscal year, the business environment in Electronics became more difficult due to a deterioration in the semiconductor business and slowing sales in Southeast Asia. Sales in Japan, where Sony had attained steady growth despite sluggish market conditions, also slowed toward the end of the fiscal year.

Breaking down Electronics sales to customers by product category, "Audio" products sales grew by 9.5% to ¥1,127.8 billion ($8,544 million) due to sales expansion of MiniDisc systems while sales of Walkman headphone stereos decreased. Sales also expanded 6.6% to ¥870.9 billion ($6,597 million) in the "Video" category, as demand grew for home-use digital camcorders and the Digital Mavica still camera. Although the highly successful Wega series of color TVs in Japan, which incorporate flat cathode ray tubes, contributed to sales in "Televisions", the category overall increased only 0.7% to ¥709.0 billion ($5,372 million), due to sluggishness in Brazil and Asia, including China. Despite a slowing of computer display sales caused by weakness in PC markets, sales in the "Information and communications" category increased 17.0% to ¥894.8 billion ($6,779 million), boosted by the popularity of new VAIO notebook PCs in Japan, and expansion of digital cellular phone sales in Japan, the United States, and Europe. In the "Electronic components and other" category, sales grew 26.0% to ¥774.9 billion ($5,870 million) primarily due to higher sales in electronic components such as optical pickups, more than offsetting declining demand for memory chips.

Game

Sales in the Game business jumped by 72.3%, to ¥722.6 billion ($5,474 million), on extremely strong demand for PlayStation game consoles and software worldwide. Operating income in this business segment more than doubled from the previous fiscal year, reaching ¥116.9 billion ($886 million) and rose by 2.6 percentage points, to 16.2% of sales. During the year, worldwide production shipments of PlayStation game consoles increased to 19.37 million units compared with 9.2 million units in the previous fiscal year. As of March 31, 1998, cumulative production shipments to markets worldwide have reached 32.82 million consoles and 236 million software units.

Music

Sony's Music business continued to post strong results as revenue increased 17.3% to ¥694.7 billion ($5,263 million) and operating income increased 19.6% to ¥54.1 billion ($410 million). As a percentage of sales, operating income improved by 0.2 percentage point, to 7.8%. The Music group performed strongly throughout most territories around the world. Global bestsellers, combined with local artist successes worldwide, contributed to the year's results, more than offsetting lower results from direct marketing operations in the United States.

Pictures

Sony's Pictures business recorded strong results. Revenue increased 46.7% to ¥643.2 billion ($4,872 million). Sales increased significantly over the prior year, benefiting from record motion picture box office revenue and strong sell-through video sales, as well as the inclusion of 13 months of activity from March 1, 1997 to March 31, 1998 due to a change in the Pictures group fiscal year. In television operations, the group benefited from continued strong performance from its game shows and soap operas as well as network and syndication revenue. Operating income was up 22.9% to ¥35.5 billion ($269 million), but declined 1.1 percentage points, to 5.5% of sales. This was mainly due to the start-up losses on new international television ventures and losses due to the underutilization of its special effects studio.

Insurance

Insurance revenue increased 27.7% to ¥291.1 billion ($2,205 million), reflecting the expansion of Sony's life insurance business in Japan. In this segment, operating income grew 6.4% to ¥20.3 billion ($154 million) and declined 1.4 percentage points, to 7.0% of sales. The lower operating margin was primarily due to an increase in amortization of deferred insurance acquisition costs and higher expenses such as benefit payments at Sony Life Insurance Co., Ltd.

Other

The Other segment consists of various operating activities including customer financing, leasing, broadcasting, networking, and other businesses. Sales in the Other segment grew 3.3% to ¥248.2 billion ($1,881 million) and operating loss increased to ¥10.3 billion ($78 million) from the prior year's operating loss of ¥1.4 billion. This increase in the operating loss was due to higher costs incurred in the start-up of new businesses including location based entertainment businesses, satellite distribution services, and internet-related businesses.

Outlook

In the fiscal year ending March 31, 1999, Sony will continue its efforts to further improve business results. However, the operating environment has become increasingly challenging. Based on business conditions and management's outlook as of May 7, 1998, Sony estimates flat sales and moderately lower earnings compared to the fiscal year ended March 31, 1998. The major factors contributing to this estimate are as follows.

Based on the assumption that the average yen-dollar exchange rate until the end of the fiscal year ending March 31, 1999 will be around ¥125, a smaller benefit is expected from the yen's depreciation. In the Electronics segment, sales are forecast to continue to be weak in Brazil and Asian countries, and to slow in Japan. Also, conditions in semiconductor markets are not expected to improve in the near-term. The Game business is forecast to experience a decline in profitability due to factors including an increase in R&D expenses. In the Other segment, new business areas such as digital satellite broadcasting remain in start-up stages and are expected to generate a loss.

A depreciation of the yen from the assumption in Sony's forecasts against various currencies in terms of average rates would be anticipated to have a positive impact on Sony's performance.

FINANCIAL POSITION AND LIQUIDITY

Total assets at March 31, 1998 were ¥6,403.0 billion ($48,508 million), 12.7% more than at the previous fiscal year-end. One reason for the increase was the yen's depreciation at the end of the year compared with the previous fiscal year-end. Among current assets, cash and time deposits rose mostly due to the higher earnings, and marketable securities increased as the parent company raised short-term investments. Notes and accounts receivable increased as sales grew. While growth in sales resulted in increases in inventories, the inventory turnover ratio to cost of sales (based on the average of inventories at March 31, 1997 and 1998) improved by 0.22 month to 2.42 months resulting from efforts to shorten product lead-times from manufacture to sale. The increase in investments and advances was due to higher investment assets at Sony Life Insurance Co., Ltd. as insurance premium revenues posted strong growth.

Total current and long-term liabilities increased 8.7% to ¥4,461.7 billion ($33,801 million). Among current liabilities, short-term borrowings and debt declined sharply, mainly due to the redemptions of medium-term notes (MTN) issued by a U.S. subsidiary and maturing during the year. Repayment of MTN was refinanced through commercial paper (CP) issued by the subsidiary. By the end of this fiscal year, most of the outstanding CP was repaid using proceeds from the U.S.$1.5 billion Notes issued in March 1998. Notes and accounts payable, trade and accounts payable, other and accrued expenses increased due to the growth in Sony's businesses. Among long-term liabilities, long-term debt increased only slightly despite the Notes issue because of the conversion of ¥146.5 billion ($1,110 million) of convertible bonds into common stock during the year. As a result, total short- and long-term borrowings and debt amounted to ¥1,303.8 billion ($9,878 million), 8.7% less than the previous fiscal year-end. The increase in accrued pension and severance costs resulted from a reduction in the assumed discount rate used in developing projected benefit obligations for the Japanese plans, due to a decline in long-term interest rates in Japan for the past few years, and from the minimum pension liability recognized at March 31, 1998 (refer to Note 13 of Notes to Consolidated Financial Statements). Future insurance policy benefits were higher because of growth in insurance premium revenues at Sony Life Insurance Co., Ltd.

Stockholders' equity increased 24.4% to ¥1,815.6 billion ($13,754 million), mostly because of higher earnings and the conversion of convertible bonds. The ratio of stockholders' equity to total assets increased by 2.7 percentage points, from 25.7% to 28.4%. Based on the number of shares outstanding at March 31, 1998, **stockholders' equity per share** rose to ¥4,461.39 ($33.80) from ¥3,798.62 at the previous fiscal year-end. In addition, the cumulative translation adjustment at March 31, 1998 decreased in absolute amount to ¥140.7 billion ($1,066 million) from ¥181.2 billion at the previous fiscal year-end mainly due to the yen's depreciation.

Cash Flows

Sony's management aims to maintain a solid financial position with ample liquidity to provide operational flexibility.

There was a net decrease in **cash and cash equivalents at end of year** of ¥5.2 billion ($40 million), including the effect of exchange rate changes of ¥1.1 billion ($8 million), resulting in a balance of ¥423.3 billion ($3,207 million) at year-end.

During the year, **net cash provided by operating activities** decreased to ¥612.4 billion ($4,639 million) from the previous fiscal year, mainly due to an increase in inventories, decreases in accrued income and other taxes and other factors. Depreciation and amortization, including amortization of goodwill and intangibles and deferred insurance acquisition costs, rose 13.2% to ¥301.7 billion ($2,285 million). Depreciation and amortization is projected to be higher in the fiscal year ending March 31, 1999.

During the year, **net cash used in investing activities** increased to ¥598.7 billion ($4,536 million) from the previous fiscal year, mainly due to higher payments for purchases of fixed assets.

During the year, **net cash used in financing activities** decreased significantly to ¥17.8 billion ($135 million) from the previous fiscal year. This was due to a small net repayment of short-term borrowings, reflecting the substantial demand for funds during the year mentioned above, compared to a significant net repayment of short-term borrowings in the previous fiscal year. In addition, proceeds from issuance, mainly of the Notes, increased from the previous fiscal year, while net repayment of long-term debt also increased because of redemptions, mainly of MTN in the United States.

Capital Expenditures

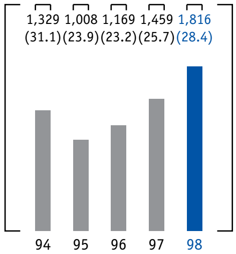
Capital expenditures (additions to fixed assets) were up 30.2% to ¥388.0 billion ($2,939 million). Major components of the capital expenditures were approximately ¥70.0 billion ($530 million) in the semiconductor field, which was the largest amount, and investments in such fields as displays and recording media. In the fiscal year ending March 31, 1999, while Sony plans to maintain a high level of investment in these business areas, total capital expenditures are expected to decrease.

Major Agreements

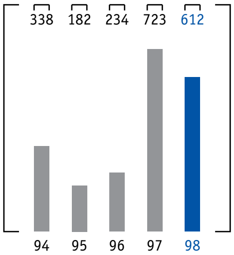
This section details major agreements having an effect on liquidity or earnings during the year and expected in the fiscal years ending March 31, 1999 and thereafter.

During the year, Sony made an equity investment of approximately ¥5.0 billion in Japan Sky Broadcasting Co., Ltd (JSkyB), a digital communications satellite broadcaster. In May 1998, JSkyB and PerfecTV Corporation completed their merger. As a result of this merger, Sony owns 11.375% of shares of the combined company, known as Japan Digital Broadcasting Services Inc. Sony also invested a total of approximately ¥4.2 billion in broadcast programming companies relating to the digital communications satellite broadcasting business during the year. In the fiscal year ending March 31, 1999, Sony plans to make additional investments of approximately ¥3.9 billion in other broadcast programming companies. Such communications satellite related businesses are currently in start-up phases, and Sony is committed to such new business areas, with the required additional investments to be made in accordance with its share of equity. Sony also plans to make an investment of approximately ¥0.8 billion in broadcast programming companies involved in digital satellite broadcasting in the fiscal year ending March 31, 1999.

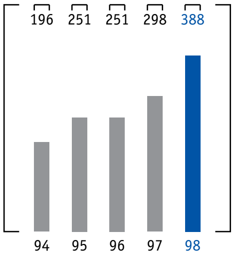
Stockholders' Equity (Percent of Total Assets)
(Billion ¥, %)



Net Cash Provided by Operating Activities
(Billion ¥)



Capital Expenditures
(Billion ¥)



In October 1997, Sony and Toyoda Automatic Loom Works, Ltd. jointly established S.T. Liquid Crystal Display Corp. for the purpose of manufacturing next-generation LCD panels. During the year, Sony made an investment in this firm of approximately ¥4.0 billion. In the fiscal year ending March 31, 1999, Sony expects to make additional investments in this firm in the amount of approximately ¥11.0 billion.

In November 1997, Sony Pictures Entertainment (SPE) reached an agreement to invest in Telemundo Group, Inc. as part of its strategy of producing and distributing programs in local languages around the world. When all necessary procedures have been completed, SPE plans to purchase the equity of Telemundo Group, Inc. at a price of $44 per share, resulting in a total investment of approximately $125 million. Upon this acquisition, Telemundo Group, Inc. will be divided into two groups – the Network and the Station Group. SPE plans to own 50% of the Network Group and 24.95% of the Station Group.

In January 1998, Sony announced a plan to form a strategic alliance with NextLevel Systems Inc. of the United States (now called General Instrument Corp.), to jointly develop digital TV technologies, subject to definitive agreements. When definitive agreements are reached, Sony plans to purchase 7.5 million shares of General Instrument Corp. at a price of $25 per share, resulting in a total investment of approximately $187.5 million.

In May 1998, Loews Theatres Exhibition Group ("Loews Theatres"), a unit of SPE, and Cineplex Odeon Corporation, a Canadian theatre chain, combined and created Loews Cineplex Entertainment Corporation. In conjunction with the combination, SPE received approximately $400 million in cash from the repayment of all of the intercompany debt of Loews Theatres, which was refinanced with third party debt, and receipt of a dividend. Sony plans to use these funds to reduce its U.S. debt and meet internal funding requirements. As a result of the combination, Loews Cineplex Entertainment Corporation is owned 51.1% (representing 49.9% of the voting shares) by SPE. The new company will be deconsolidated and Sony will account for it on the equity basis from the fiscal year ending March 31, 1999. The revenues and operating income of Loews Theatres during the year were approximately $462 million and $20.6 million, respectively. In addition, Sony will record a gain of approximately $36 million on the combination in the fiscal year ending March 31, 1999.

A building complex to house Sony's European headquarters, rental office space, stores, residences, a movie and broadcasting museum with educational facilities, and entertainment space is currently under construction in Berlin, Germany. The structure is located in Potsdam Platz on a site that Sony purchased from the City of Berlin. The developer of the building complex is a partnership controlled by Sony, Tishman Speyer Properties, Inc. of the United States, and Kajima Corporation of Japan. Completion is scheduled for 2000. The budget for this project is approximately 1.5 billion German marks. Of this amount, approximately 1.0 billion German marks will be procured by the partnership in the form of project financing. In addition, Sony is constructing an entertainment complex which includes stores and theatres on a site in San Francisco, U.S.A. Completion is scheduled for 1999. The budget for this project is approximately $85 million. Sony also plans to construct a similar entertainment complex in Tokyo, Japan, with completion scheduled for 2000. Currently, the estimated budget for this project is approximately ¥12.0 billion.

The Year 2000 Issue

Sony has placed top priority on resolving the Year 2000 issue to facilitate the continuity of operations and customer satisfaction. Sony has initiated a comprehensive corporate-wide project to implement an uninterrupted transition into the year 2000 for all internal information systems and Sony products. With plans continuing on schedule, Sony expects to complete the resolution of the Year 2000 issue for internal information systems by December 1998. Sony is also taking the necessary actions so that customers around the world will be able to depend on Sony products on and after the year 2000. In October 1997, Sony completed an identification and assessment of the capability of all Sony products to handle the Year 2000 issue, and established a structure to enable Sony to manage this issue around the world by May 1998. In the broadcast- and professional-use product field, Sony is continuing to deal with each customer in resolving the Year 2000 issue, and expects completion by the end of March 1999.

The external cost to modify all internal information systems for compliance with the Year 2000 issue is estimated to be approximately ¥9.2 billion ($70 million), of which approximately ¥2.1 billion ($16 million) was expensed as incurred by the end of this fiscal year. The external cost associated with the Year 2000 issue for all Sony products is currently expected to be minimal. Sony expects such costs would not have a material adverse effect on consolidated operations and financial results.

Although Sony will make every effort to eliminate any impact of the Year 2000 issues, there can be no assurances that Sony will in fact achieve this goal due to uncertainties that Sony is currently unable to forecast.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The financial instruments including financial assets and liabilities that Sony holds in the normal course of business are continuously exposed to fluctuations in markets, such as currency exchange rates, interest rates, and stock prices of investments. In applying a consistent risk management strategy in order to remove adverse effects caused by market fluctuations in the cash flow value of these financial instruments, Sony hedges the market risk of these financial assets and liabilities by using derivative financial instruments which include foreign exchange forward contracts, foreign currency option contracts, interest rate swap agreements, and interest rate and currency swap agreements. Sony utilizes foreign exchange forward contracts and foreign currency option contracts primarily to fix the cash flow value resulting from accounts receivable and payable and future transactions denominated in foreign currencies in relation to the core currencies (Japanese yen, U.S. dollars, and German marks) of Sony's major operating units. Interest rate swap agreements and interest rate and currency swap agreements are used to diversify funding methods and lower funding costs. Sony's basic policy is to use fixed interest rates when procuring funds for investments having a long-term recovery period and variable interest rates for funding requirements of a short-term nature, such as working capital. The above swaps are utilized to enable Sony to choose between fixed and variable interest rates depending on how the funds are to be used, as well as to hedge foreign exchange risks that result when assets denominated in one currency are funded by liabilities denominated in a different currency. Sony uses these derivative financial instruments solely for risk hedging purposes as described above, and no derivative transactions are held or used for trading purposes. In addition, bond option contracts are used as an integral part of short-term investing activities in order to fix the yields from bonds held by Sony Life Insurance Co., Ltd. on hand to certain ranges. Note that among the market risks described above, no specific hedging activities are taken against the price fluctuations of stocks held by Sony as marketable securities (refer to Notes 2 and 12 of Notes to Consolidated Financial Statements).

Sony measures the effect of market fluctuations on the value of financial instruments and derivatives by using Value-at-Risk (herein referred to as "VaR") analysis. VaR measures a potential maximum amount of loss in fair value resulting from adverse market fluctuations, for a selected period of time and at a selected level of confidence. Sony uses the variance/co-variance model in calculation of VaR. The calculation includes financial instruments such as cash and cash equivalents, time deposits, marketable securities, non-lease short- and long-term borrowings and debt, investments and advances and all derivatives including transactions for risk hedging held by Sony Corporation and consolidated subsidiaries. Sony calculates VaR for one day from the portfolio of financial instruments and derivatives as of March 31, 1998, at a confidence level of 95%.

Based on this assumption, Sony's consolidated VaR at March 31, 1998 is calculated to be ¥6.9 billion ($52 million), which indicates the potential maximum loss in fair value resulting from market fluctuations in one day at a 95% confidence level. By item, the VaR of currency exchange rate risk is calculated to be ¥7.2 billion ($55 million) which mainly consists of risks arising from the volatility of the exchange rates between yen and U.S. dollars in which relatively large amount of financial assets and liabilities and derivative transactions is maintained. VaR of interest rate risk and stock price risk are calculated to be ¥3.4 billion ($26 million) and ¥3.3 billion ($25 million), respectively. The net VaR for Sony's entire portfolio is smaller than the simple aggregate of VaR for each component of market risk. This is due to the fact that market risk factors such as currency exchange rates, interest rates, and stock prices are not completely independent, thus have the effect of offsetting a portion of overall profits and losses.

The calculated VaR does not include the effect of accounts receivable and payable and anticipated transactions denominated in foreign currencies as of March 31, 1998, that are the object of Sony's derivative hedging. Therefore, the above amount of VaR does not reflect the full effect of the hedging activities and Sony expects that the actual risk would be less than the disclosed VaR if those accounts receivable and payable are taken into account in the calculation. The disclosed VaR amount simply represents the calculated potential maximum loss on the following day and by no means indicates an estimate of future loss.

[Quarterly Financial and Stock Information]

Sony Corporation and Consolidated Subsidiaries

(Unaudited)

Year ended March 31

	Yen in billions except per share amounts								Dollars in millions except per share amounts
	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter		4th Quarter
	1997	**1998**	1997	**1998**	1997	**1998**	1997	**1998**	**1998**
Sales and operating revenue	¥1,172.2	**¥1,430.3**	¥1,358.5	**¥1,638.5**	¥1,666.8	**¥2,012.7**	¥1,465.7	**¥1,674.0**	**$12,681.6**
Operating income	55.3	**97.3**	80.6	**140.4**	164.5	**223.7**	69.9	**58.9**	**446.2**
Interest income (expense), net	(12.6)	**(9.8)**	(13.5)	**(10.5)**	(13.9)	**(11.6)**	(11.5)	**(9.6)**	**(72.4)**
Foreign exchange gain (loss), net	(0.6)	**6.4**	7.6	**(6.8)**	5.8	**6.8**	5.3	**3.6**	**27.6**
Income before income taxes	43.8	**91.9**	65.7	**110.2**	147.4	**214.3**	55.6	**37.4**	**283.3**
Income taxes	25.9	**54.6**	28.0	**48.6**	67.8	**96.9**	41.8	**14.8**	**111.8**
Net income	17.1	**34.8**	34.6	**56.1**	75.4	**110.4**	12.3	**20.8**	**157.3**
Net income per share									
Basic	¥ 45.7	**¥ 89.8**	¥ 92.6	**¥ 141.7**	¥ 201.2	**¥ 274.4**	¥ 32.5	**¥ 51.0**	**$ 0.39**
Diluted	38.2	**76.3**	76.1	**122.1**	163.8	**239.0**	27.9	**45.9**	**0.35**
Depreciation and amortization*	¥ 59.7	**¥ 65.6**	¥ 61.8	**¥ 72.9**	¥ 66.9	**¥ 78.3**	¥ 78.2	**¥ 84.8**	**$ 642.2**
Capital expenditures (additions to fixed assets)	67.5	**79.0**	76.6	**88.8**	57.3	**83.3**	96.7	**136.9**	**1,037.2**
R&D expenses	62.8	**69.7**	74.6	**80.5**	67.1	**79.6**	78.0	**88.2**	**668.2**
Tokyo Stock Exchange price per share of Common Stock:									
High	¥ 7,310	**¥ 10,100**	¥ 7,260	**¥ 12,600**	¥ 7,700	**¥ 12,200**	¥ 9,180	**¥ 12,700**	**$ 96.2**
Low	6,350	**8,520**	6,680	**9,550**	6,720	**9,320**	7,250	**10,400**	**78.8**
New York Stock Exchange price per American Depositary Share:									
High	$ 66 5/8	**$ 88 7/8**	$ 66 1/4	**$103 11/16**	$ 67 7/8	**$ 98 7/16**	$ 74 1/4	**$ 97 3/16**	
Low	59	**69 1/2**	61 1/2	**85 1/16**	58 7/8	**74 1/2**	63 3/8	**82 5/16**	

** Including amortization of deferred insurance acquisition costs*

Notes: 1. U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥132=U.S.$1, the approximate Tokyo foreign exchange market rate as of March 31, 1998, as described in Note 3 of Notes to Consolidated Financial Statements.

2. Net income per share amounts were computed based on Statement of Financial Accounting Standards No. 128, "Earnings per Share" (FAS 128). All prior-period net income per share amounts have been restated to conform with FAS 128. FAS 128 requires presentation of basic and diluted net income per share on the face of the income statement. Under FAS 128, basic net income per share is computed based on the average number of shares of common stock outstanding during each period and diluted net income per share assumes the dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock. Refer to Note 4 of Notes to Consolidated Financial Statements.

[Five-Year Summary of Selected Financial Data]

Sony Corporation and Consolidated Subsidiaries · Year ended March 31

	Yen in millions except per share amounts					Dollars in thousands except per share amounts
	1994	1995	1996	1997	**1998**	**1998**
FOR THE YEAR						
Sales and operating revenue	¥3,744,285	¥3,990,583	¥4,592,565	¥5,663,134	**¥6,755,490**	**$51,177,955**
Operating income (loss)	106,962	(166,640)	235,324	370,330	**520,210**	**3,940,985**
Income (loss) before income taxes	102,162	(220,948)	138,159	312,429	**453,749**	**3,437,492**
Income taxes	78,612	65,173	77,158	163,570	**214,868**	**1,627,788**
Net income (loss)	15,298	(293,356)	54,252	139,460	**222,068**	**1,682,333**
Per share data:						
Net income (loss)						
— Basic	¥ 41.0	¥ (784.7)	¥ 145.1	¥ 367.7	**¥ 557.7**	**$ 4.23**
— Diluted	41.0	(784.7)	134.0	309.2	**483.4**	**3.66**
Cash dividends	50.0	50.0	50.0	55.0	**60.0**	**0.45**
Depreciation and amortization*	¥ 242,458	¥ 226,984**	¥ 227,316	¥ 266,532	**¥ 301,665**	**$ 2,285,341**
Capital expenditures (additions to fixed assets)	195,937	250,678	251,197	298,078	**387,955**	**2,939,053**
R&D expenses	229,877	239,164	257,326	282,569	**318,044**	**2,409,424**
AT YEAR-END						
Net working capital	¥ 616,020	¥ 537,733	¥ 816,361	¥ 843,500	**¥1,151,152**	**$ 8,720,849**
Stockholders' equity	1,329,496	1,007,802	1,169,147	1,459,332	**1,815,555**	**13,754,205**
Stockholders' equity per share	¥ 3,557.50	¥ 2,695.31	¥ 3,125.53	¥ 3,798.62	**¥ 4,461.39**	**$ 33.80**
Total assets	¥4,269,816	¥4,223,914	¥5,045,699	¥5,680,246	**¥6,403,043**	**$48,507,902**
Number of shares issued at year-end (thousands of shares)	373,728	373,911	374,068	384,185	**407,195**	

* *Including amortization of deferred insurance acquisition costs*

** *Excluding write-off of goodwill*

Notes:
1. *U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥132=U.S.$1, the approximate Tokyo foreign exchange market rate as of March 31, 1998, as described in Note 3 of Notes to Consolidated Financial Statements.*
2. *Net income (loss) per share amounts were computed based on Statement of Financial Accounting Standards No. 128, "Earnings per Share" (FAS 128). All prior-period net income (loss) per share amounts have been restated to conform with FAS 128. FAS 128 requires presentation of basic and diluted net income per share on the face of the income statement. Under FAS 128, basic net income per share is computed based on the average number of shares of common stock outstanding during each period and diluted net income per share assumes the dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock. Refer to Note 4 of Notes to Consolidated Financial Statements.*
3. *During the fiscal year ended March 31, 1996, the Company changed its method of accounting for assessing the carrying values of intercompany foreign currency commitments to comply with the Emerging Issues Task Force Issue No. 95-2. This did not have a material impact on results of operations for the years ended March 31, 1996, 1997 and 1998.*
4. *The consolidated results for the fiscal year ended March 31, 1995 reflect the write-off of goodwill of ¥265 billion in the Pictures segment and losses in the Pictures segment of approximately ¥50 billion arising from a combination of unusual items, such as abandoning a large number of projects in development and providing for settlement of outstanding lawsuits and contract claims.*
5. *Certain amounts at year-end for the prior years have been reclassified to conform to the 1998 presentation.*

[Composition of Sales and Operating Revenue by Business and Geographic Segment]

Sony Corporation and Consolidated Subsidiaries
Year ended March 31

	Yen in millions					Dollars in thousands**
	1994	1995	1996	1997	**1998**	**1998**
BY BUSINESS SEGMENT*						
Electronics	¥2,791,881	¥3,027,434	¥3,283,234	¥3,930,292	**¥4,377,346**	**$33,161,712**
	74.6%	75.9%	71.5%	69.4%	**64.8%**	
Game	—	35,449	200,894	408,335	**699,574**	**5,299,803**
	—	0.9	4.4	7.2	**10.4**	
Music	461,752	481,021	506,455	570,119	**660,407**	**5,003,083**
	12.3	12.0	11.0	10.1	**9.8**	
Pictures	327,748	281,677	317,382	438,551	**642,714**	**4,869,046**
	8.7	7.1	6.9	7.7	**9.5**	
Insurance	88,680	112,831	206,802	227,920	**291,061**	**2,205,008**
	2.4	2.8	4.5	4.0	**4.3**	
Other	74,224	52,171	77,798	87,917	**84,388**	**639,303**
	2.0	1.3	1.7	1.6	**1.2**	
Sales and operating revenue	¥3,744,285	¥3,990,583	¥4,592,565	¥5,663,134	**¥6,755,490**	**$51,177,955**

** Sales and operating revenue to customers*

Notes: 1. Reporting of business segments has been changed to comply with the Statement of Financial Accounting Standards No. 131 requirements, as described in Note 19 of Notes to Consolidated Financial Statements. Accordingly, results for the prior years have been reclassified to conform to the 1998 presentation.

2. As a result of a change in the accounting period in Pictures, results for the year ended March 31, 1998 in the segment include the thirteen-month period from March 1, 1997 to March 31, 1998.

« Electronics Sales and Operating Revenue to Customers by Product Category »

	1994	1995	1996	1997	**1998**	**1998**
Audio	¥ 840,723	¥ 900,180	¥ 900,400	¥1,029,961	**¥1,127,788**	**$ 8,543,848**
	30.1%	29.7%	27.4%	26.2%	**25.8%**	
Video	668,537	685,802	731,097	816,582	**870,854**	**6,597,379**
	23.9	22.6	22.3	20.8	**19.9**	
Televisions	485,777	544,255	554,023	704,075	**709,043**	**5,371,538**
	17.4	18.0	16.9	17.9	**16.2**	
Information and communications	365,487	413,445	540,719	764,512	**894,810**	**6,778,864**
	13.1	13.7	16.5	19.4	**20.4**	
Electronic components and other	431,357	483,752	556,995	615,162	**774,851**	**5,870,083**
	15.5	16.0	16.9	15.7	**17.7**	
Total	¥2,791,881	¥3,027,434	¥3,283,234	¥3,930,292	**¥4,377,346**	**$33,161,712**

Notes: 1. Sales and operating revenue by product category for the prior years have been reclassified to conform to the 1998 presentation.

2. The above table is a breakdown of Electronics sales and operating revenue to customers by product category. The Electronics business is managed as a single operating segment by the company's management. However, the company believes that the information in this table is useful to investors in understanding the sales contributions of the products in this business segment. Operating income information by product category is not available.

	1994	1995	1996	1997	**1998**	**1998**
BY GEOGRAPHIC SEGMENT						
Japan	¥1,033,273	¥1,105,152	¥1,379,804	¥1,590,820	**¥1,843,149**	**$13,963,250**
	27.6%	27.7%	30.0%	28.1%	**27.3%**	
United States	1,154,454	1,152,081	1,259,926	1,639,334	**2,101,907**	**15,923,538**
	30.8	28.9	27.4	29.0	**31.1**	
Europe	832,751	905,416	1,054,010	1,304,491	**1,567,121**	**11,872,129**
	22.3	22.7	23.0	23.0	**23.2**	
Other Areas	723,807	827,934	898,825	1,128,489	**1,243,313**	**9,419,038**
	19.3	20.7	19.6	19.9	**18.4**	
Sales and operating revenue	¥3,744,285	¥3,990,583	¥4,592,565	¥5,663,134	**¥6,755,490**	**$51,177,955**

Classification by Geographic segment shows sales and operating revenue recognized by location of customers.

*** U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥132=U.S.$1, the approximate Tokyo foreign exchange market rate as of March 31, 1998, as described in Note 3 of Notes to Consolidated Financial Statements.*

[Consolidated Balance Sheets]

Sony Corporation and Consolidated Subsidiaries · March 31

	Yen in millions		Dollars in thousands (Note 3)
	1997	**1998**	**1998**
ASSETS			
Current assets:			
Cash and cash equivalents (Notes 6 and 12)	¥ 428,518	**¥ 423,286**	**$ 3,206,712**
Time deposits (Note 12)	52,518	**107,139**	**811,659**
Marketable securities (Note 9)	120,094	**169,209**	**1,281,887**
Notes and accounts receivable, trade (Notes 8 and 12)	1,066,314	**1,230,799**	**9,324,235**
Allowance for doubtful accounts and sales returns	(93,732)	**(114,911)**	**(870,538)**
Inventories (Note 7)	869,800	**993,927**	**7,529,750**
Deferred income taxes (Note 14)	111,756	**121,189**	**918,098**
Prepaid expenses and other current assets	240,099	**336,839**	**2,551,811**
Total current assets	2,795,367	**3,267,477**	**24,753,614**
Noncurrent inventories—film (Note 7)	242,727	**249,066**	**1,886,864**
Investments and advances:			
Affiliated companies	52,547	**65,912**	**499,333**
Securities investments and other (Note 9)	734,332	**784,550**	**5,943,561**
	786,879	**850,462**	**6,442,894**
Property, plant and equipment (Notes 10 and 17)**:**			
Land	179,011	**184,427**	**1,397,174**
Buildings	818,084	**864,324**	**6,547,909**
Machinery and equipment	1,805,851	**1,947,454**	**14,753,439**
Construction in progress	72,661	**95,799**	**725,750**
	2,875,607	**3,092,004**	**23,424,272**
Less—Accumulated depreciation	1,636,696	**1,744,877**	**13,218,765**
	1,238,911	**1,347,127**	**10,205,507**
Other assets:			
Intangibles (Notes 5 and 13)	112,080	**124,817**	**945,583**
Goodwill (Note 5)	161,840	**160,491**	**1,215,841**
Deferred insurance acquisition costs (Note 11)	148,032	**163,120**	**1,235,758**
Other (Note 14)	194,410	**240,483**	**1,821,841**
	616,362	**688,911**	**5,219,023**
	¥5,680,246	**¥6,403,043**	**$48,507,902**

The accompanying notes are an integral part of these statements.

	Yen in millions		Dollars in thousands (Note 3)
	1997	**1998**	**1998**
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities:			
Short-term borrowings (Notes 10 and 12)	¥ 117,801	**¥ 114,617**	**$ 868,311**
Current portion of long-term debt (Notes 10, 12 and 17)	210,315	**84,794**	**642,378**
Notes and accounts payable, trade (Notes 8 and 12)	653,826	**768,152**	**5,819,333**
Accounts payable, other and accrued expenses (Note 13)	537,726	**676,547**	**5,125,356**
Accrued income and other taxes	169,480	**157,123**	**1,190,326**
Other (Note 14)	262,719	**315,092**	**2,387,061**
Total current liabilities	1,951,867	**2,116,325**	**16,032,765**
Long-term liabilities:			
Long-term debt (Notes 10, 12 and 17)	1,099,765	**1,104,420**	**8,366,818**
Accrued pension and severance costs (Note 13)	146,289	**186,871**	**1,415,690**
Deferred income taxes (Note 14)	173,951	**147,116**	**1,114,515**
Future insurance policy benefits and other (Note 11)	579,263	**713,970**	**5,408,864**
Other	154,912	**193,000**	**1,462,121**
	2,154,180	**2,345,377**	**17,768,008**
Minority interest in consolidated subsidiaries	114,867	**125,786**	**952,924**
Stockholders' equity (Note 15)**:**			
Common stock, ¥50 par value—			
Authorized: 1,350,000,000 shares			
Issued: 1997 —384,185,043 shares	332,037		
1998 —407,195,271 shares		**406,196**	**3,077,242**
Additional paid-in capital	474,033	**548,422**	**4,154,712**
Legal reserve	35,831	**38,885**	**294,583**
Retained earnings	731,470	**926,198**	**7,016,652**
Unrealized gain on securities (Note 9)	67,278	**45,173**	**342,220**
Minimum pension liability adjustment (Note 13)	—	**(5,714)**	**(43,288)**
Cumulative translation adjustment	(181,221)	**(140,725)**	**(1,066,098)**
Treasury stock, at cost			
(1997 — 11,150 shares, 1998 — 246,714 shares)	(96)	**(2,880)**	**(21,818)**
	1,459,332	**1,815,555**	**13,754,205**
Commitments and contingent liabilities (Note 18)			
	¥5,680,246	**¥6,403,043**	**$48,507,902**

[Consolidated Statements of Income and Retained Earnings]

Sony Corporation and Consolidated Subsidiaries · Year ended March 31

	Yen in millions			Dollars in thousands (Note 3)
	1996	1997	**1998**	**1998**
Sales and operating revenue:				
Net sales (Note 8)	¥4,339,411	¥5,383,911	**¥6,424,805**	**$48,672,765**
Insurance revenue	207,691	227,920	**291,061**	**2,205,008**
Other operating revenue	45,463	51,303	**39,624**	**300,182**
	4,592,565	5,663,134	**6,755,490**	**51,177,955**
Costs and expenses:				
Cost of sales (Note 16)	3,216,806	3,930,107	**4,618,961**	**34,992,129**
Selling, general and administrative (Note 16)	937,910	1,153,876	**1,345,584**	**10,193,818**
Insurance expenses	202,525	208,821	**270,735**	**2,051,023**
	4,357,241	5,292,804	**6,235,280**	**47,236,970**
Operating income	235,324	370,330	**520,210**	**3,940,985**
Other income:				
Interest and dividends	18,053	19,406	**20,976**	**158,909**
Foreign exchange gain, net	—	18,085	**10,094**	**76,470**
Other	47,702	55,152	**52,893**	**400,704**
	65,755	92,643	**83,963**	**636,083**
Other expenses:				
Interest	67,095	70,892	**62,524**	**473,667**
Foreign exchange loss, net	25,580	—	**—**	**—**
Other	70,245	79,652	**87,900**	**665,909**
	162,920	150,544	**150,424**	**1,139,576**
Income before income taxes	138,159	312,429	**453,749**	**3,437,492**
Income taxes (Note 14)**:**				
Current	72,088	169,060	**210,113**	**1,591,765**
Deferred	5,070	(5,490)	**4,755**	**36,023**
	77,158	163,570	**214,868**	**1,627,788**
Income before minority interest	61,001	148,859	**238,881**	**1,809,704**
Minority interest in consolidated subsidiaries	6,749	9,399	**16,813**	**127,371**
Net income	54,252	139,460	**222,068**	**1,682,333**
Retained earnings:				
Balance, beginning of year	585,553	617,343	**731,470**	**5,541,439**
Common stock issue costs, net of tax	(2)	—	**—**	**—**
Cash dividends	(18,700)	(20,882)	**(24,286)**	**(183,984)**
Transfer to legal reserve	(3,760)	(4,451)	**(3,054)**	**(23,136)**
Balance, end of year	¥ 617,343	¥ 731,470	**¥ 926,198**	**$ 7,016,652**

	Yen			Dollars (Note 3)
Per share data (Note 4)**:**				
Net income — Basic	¥145.1	¥367.7	**¥557.7**	**$4.23**
— Diluted	134.0	309.2	**483.4**	**3.66**
Cash dividends	50.0	55.0	**60.0**	**0.45**

The accompanying notes are an integral part of these statements.

[Consolidated Statements of Cash Flows]

Sony Corporation and Consolidated Subsidiaries · Year ended March 31

	Yen in millions			Dollars in thousands (Note 3)
	1996	1997	**1998**	**1998**
Cash flows from operating activities:				
Net income	¥ 54,252	¥139,460	**¥222,068**	**$1,682,333**
Adjustments to reconcile net income to net cash provided by operating activities—				
Depreciation and amortization, including amortization of deferred insurance acquisition costs	227,316	266,532	**301,665**	**2,285,341**
Accrual for pension and severance costs, less payments	9,604	19,521	**40,367**	**305,811**
Loss on disposal of fixed assets	9,429	13,411	**22,678**	**171,803**
Deferred income taxes	5,070	(5,490)	**4,755**	**36,023**
Changes in assets and liabilities:				
Increase in notes and accounts receivable	(150,158)	(65,905)	**(113,050)**	**(856,439)**
(Increase) decrease in inventories	(69,157)	41,825	**(96,138)**	**(728,318)**
Increase in other current assets	(32,117)	(2,906)	**(69,198)**	**(524,227)**
Increase (decrease) in notes and accounts payable	(4,169)	66,099	**109,785**	**831,704**
Increase (decrease) in accrued income and other taxes	(6,064)	89,887	**(28,775)**	**(217,992)**
Increase in other current liabilities	54,438	73,786	**155,401**	**1,177,280**
Increase in future insurance policy benefits and other	174,223	131,947	**134,707**	**1,020,507**
Increase in deferred insurance acquisition costs	(42,798)	(51,067)	**(39,553)**	**(299,644)**
Other	4,308	6,035	**(32,362)**	**(245,167)**
Net cash provided by operating activities	234,177	723,135	**612,350**	**4,639,015**
Cash flows from investing activities:				
Payments for purchases of fixed assets	(250,157)	(298,187)	**(378,053)**	**(2,864,038)**
Proceeds from sales of fixed assets	22,823	14,940	**22,413**	**169,795**
Payments for investments and advances	(490,330)	(450,399)	**(463,239)**	**(3,509,386)**
Proceeds from sales of investment securities and collections of advances	313,769	316,787	**323,443**	**2,450,326**
Payments for purchases of marketable securities	(54,964)	(128,929)	**(95,163)**	**(720,932)**
Proceeds from sales of marketable securities	101,913	46,105	**46,730**	**354,015**
Increase in time deposits	(12,359)	(18,361)	**(54,831)**	**(415,386)**
Other	(1,694)	46	**—**	**—**
Net cash used in investing activities	(370,999)	(517,998)	**(598,700)**	**(4,535,606)**
Cash flows from financing activities:				
Proceeds from issuance of long-term debt	381,239	171,698	**342,101**	**2,591,674**
Payments of long-term debt	(87,500)	(209,383)	**(332,154)**	**(2,516,318)**
Decrease in short-term borrowings	(145,527)	(192,034)	**(2,345)**	**(17,765)**
Dividends paid	(18,772)	(18,657)	**(21,582)**	**(163,500)**
Other	1,037	881	**(3,790)**	**(28,712)**
Net cash provided by (used in) financing activities	130,477	(247,495)	**(17,770)**	**(134,621)**
Effect of exchange rate changes on cash and cash equivalents	(9,871)	11,537	**(1,112)**	**(8,424)**
Net decrease in cash and cash equivalents	(16,216)	(30,821)	**(5,232)**	**(39,636)**
Cash and cash equivalents at beginning of year	475,555	459,339	**428,518**	**3,246,348**
Cash and cash equivalents at end of year	¥459,339	¥428,518	**¥423,286**	**$3,206,712**

The accompanying notes are an integral part of these statements.

[Notes to Consolidated Financial Statements]

Sony Corporation and Consolidated Subsidiaries

1. Nature of operations

The company is engaged in the development, design, manufacture, and sale of various kinds of electronic equipment, instruments, and devices for consumer and industrial markets. The company's principal manufacturing facilities are located in Japan, the United States, Europe, and Asia, and its products are marketed by sales subsidiaries and unaffiliated local distributors throughout the world. The company also develops, produces, manufactures, and markets home-use game consoles and software. The company is engaged in the development, production, manufacture, and distribution of recorded music, in all commercial formats and musical genres. The company is also engaged in the development, production, manufacture and marketing of image-based software, including film, video and television. Further, the company conducts insurance operations principally through a Japanese stock life insurance subsidiary. In addition to the above, the company is engaged in customer financing and leasing business and has begun to participate in new business activities including digital broadcasting, information and communications and others.

2. Summary of significant accounting policies

The parent company and its subsidiaries in Japan maintain their records and prepare their financial statements in accordance with accounting principles generally accepted in Japan while its foreign subsidiaries maintain their records and prepare their financial statements in conformity with accounting principles generally accepted in the countries of their domicile. Certain adjustments and reclassifications, including those relating to the tax effects of temporary differences, capitalization of stock purchase warrants, deferral of insurance acquisition costs, the accrual of certain expenses and the accounting for foreign currency translation, have been incorporated in the accompanying consolidated financial statements to conform with accounting principles generally accepted in the United States of America (U.S. GAAP). These adjustments were not recorded in the statutory books of account.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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 those estimates.

Significant accounting policies are as follows:

Basis of consolidation and accounting for investments in affiliated companies

The consolidated financial statements include the accounts of the parent company and those of its majority-owned subsidiary companies. All intercompany transactions and accounts are eliminated. Investments in 20% to 50% owned companies are stated at cost plus equity in undistributed earnings; consolidated net income includes the company's equity in current earnings/losses of such companies, after elimination of unrealized intercompany profits.

On occasion, a subsidiary or affiliated company accounted for by the equity method may issue its shares to third parties as either a public offering or upon conversion of convertible debt to common stock at amounts per share in excess of or less than the company's average per share carrying value. With respect to such transactions, the resulting gains or losses arising from the change in interest are recorded in income for the year the change in interest transaction occurs.

The excess of the cost over the underlying net equity of investments in subsidiaries and affiliated companies accounted for on an equity basis is allocated to identifiable assets based on fair values at the date of acquisition. The unassigned residual value of the excess of the cost over the underlying net equity is recognized as goodwill.

Translation of foreign currencies

All asset and liability accounts of foreign subsidiaries and affiliates are translated into Japanese yen at appropriate year-end current rates and all income and expense accounts are translated at rates that approximate those rates prevailing at the time of the transactions. The resulting translation adjustments are accumulated as a component of stockholders' equity.

Foreign currency receivables and payables are translated at appropriate year-end current rates and the resulting translation gains or losses are taken into income currently.

Revenue recognition

Revenues from electronics, game and music sales are recognized when products are shipped to customers.

Motion picture revenue is recognized beginning on the date of theatrical exhibition. Revenue from television licensing agreements is recognized when the motion picture or television series first becomes available for telecast. Revenue from home videocassette sales is generally recognized on the date of shipment.

Insurance premiums are reported as revenue when due from policyholders. Benefits and expenses are associated with earned insurance premiums so as to result in the recognition of profits over the life of the contracts. This association is accomplished through a provision for liabilities for future benefits and amortization of acquisition costs.

Cash and cash equivalents

Cash and cash equivalents include all highly liquid investments, generally with original maturities of three months or less, that are readily convertible to known amounts of cash and are so near maturity that they present insignificant risk of changes in value because of changes in interest rates.

Marketable securities

Marketable securities consist of debt and equity securities. Debt securities and equity securities designated as available-for-sale, whose fair values are readily determinable, are carried at fair value with unrealized gains or losses included as a component of stockholders' equity, net of applicable taxes. Debt and equity securities classified as trading securities are carried at fair value with unrealized gains or losses included in income. Debt securities that are expected to be held-to-maturity are carried at amortized cost. Individual securities classified as either available-for-sale or held-to-maturity are reduced to net realizable value by a charge to income for other than temporary declines in fair value. Realized gains and losses are determined on the average cost method and are reflected in income.

Inventories

Inventories in electronics, game and music are valued at cost, not in excess of market, cost being determined on the "average cost" basis except for the cost of finished products carried by certain subsidiary companies which is determined on the "first-in, first-out" basis.

Film costs include production, print, certain advertising costs and allocated overhead. Film costs are amortized in the proportion that revenue for a period relates to management's estimate of ultimate revenues.

Unamortized film costs are compared with estimated net realizable value on an individual film basis and write-downs are recorded when indicated. Film costs for motion pictures and television programs that are expected to be amortized against revenues from primary markets are classified as current assets. Primary markets for motion pictures include theatrical, home videocassette and pay television. Primary markets for television programs include network and first-run syndication. All other film costs are classified as noncurrent.

Property, plant and equipment and depreciation

Property, plant and equipment is stated at cost. Depreciation of property, plant and equipment is computed on the declining-balance method for the parent company and Japanese subsidiaries and on the straight-line method for foreign subsidiary companies at rates based on estimated useful lives of the assets according to general class, type of construction and use. Significant renewals and additions are capitalized at cost. Maintenance and repairs, and minor renewals and betterments are charged to income as incurred.

Intangibles and goodwill

Intangibles, which mainly consist of artist contracts and music catalogs, are being amortized on a straight-line basis principally over 16 years and 21 years, respectively.

Goodwill recognized in acquisitions accounted for as purchases is being amortized on a straight-line basis principally over a 40-year period.

Deferred insurance acquisition costs

Costs that vary with and are primarily related to acquiring new insurance policies are deferred and are being amortized mainly over the premium-paying period of the related insurance policies using assumptions consistent with those used in computing policy reserves.

Future insurance policy benefits

Future insurance policy benefits are computed based on actuarial assumptions.

Accounting for the impairment of long-lived assets

The company's long-lived assets, including goodwill and identifiable intangibles, held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. When the sum of expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the asset, an impairment loss is recognized, based on the fair value of the asset. The fair value of goodwill is determined using a discounted cash flows analysis.

Income taxes

The provision for income taxes is computed based on the pretax income included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities.

Derivative financial instruments

Derivative financial instruments, which include foreign exchange forward contracts, foreign currency option contracts, interest rate swap agreements, and interest rate and currency swap agreements, are used in the company's risk management of foreign currency and interest rate risk exposures of its financial assets and liabilities.

Foreign exchange forward contracts

Foreign exchange forward contracts are used to limit exposure to losses, resulting from changes in foreign currency exchange rates, on accounts receivable and payable and anticipated transactions denominated in foreign currencies. Foreign exchange forward contracts which are designated and effective as hedges of such currency exchange rate risk on existing assets and liabilities are marked to market and included as an offset to foreign exchange gains/losses recorded on the existing assets and liabilities. Such contracts on anticipated transactions, including contracts used to hedge intercompany foreign currency commitments which do not qualify as firm commitments, are marked to market with changes in value recognized in foreign exchange gains/losses.

Foreign currency option contracts

The company enters into purchased foreign currency option contracts to limit exposure to losses, resulting from changes in foreign currency exchange rates, on accounts receivable and anticipated transactions denominated in foreign currencies. The company also enters into written foreign currency option contracts, of which the majority are part of range forward contracts corresponding to the purchased foreign currency option contracts. The carrying values of all foreign currency option contracts are marked to market with changes in value recognized in foreign exchange gains/losses.

Interest rate swap agreements and interest rate and currency swap agreements

The company enters into interest rate swap agreements or interest rate and currency swap agreements in order to lower funding costs, to diversify sources of funding and to limit the company's exposure to loss in relation to underlying debt instruments resulting from adverse fluctuations in interest rates or foreign currency exchange rates. The related interest differentials paid or received under the interest rate swap agreements and under the interest rate and currency swap agreements are recognized over the terms of the agreements in interest expense. Currency swap portions of the interest rate and currency swap agreements which are designated and effective as hedges of exposure to losses resulting from changes in foreign currency exchange rates on underlying debt denominated in foreign currency are marked to market and included as an offset to foreign exchange gains/losses on the underlying debt.

After an underlying hedged transaction is settled or ceases to exist, all changes in fair value of related derivatives which have not been settled are recognized in foreign exchange gains/losses.

Net income per share

In February 1997, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No.128 (FAS 128), "Earnings per Share" (EPS), which replaces the presentation of primary earnings per share with a presentation of basic EPS and also requires dual presentation of basic and diluted EPS with an appropriate reconciliation of both computations. Basic EPS is computed based on the average number of shares of common stock outstanding during each period and diluted EPS assumes the dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock. Net income per share is appropriately adjusted for any free distributions of common stock. FAS 128 was effective for both interim and annual periods ending after December 15, 1997. All prior-period EPS data presented have been restated to conform with FAS 128.

Free distribution of common stock

On occasion, the company may make a free distribution of common stock which is accounted for either by a transfer of the applicable par value from additional paid-in capital to the common stock account or with no entry if free shares are distributed from the portion of previously issued shares accounted for as excess of par value in the common stock account. Under the Japanese Commercial Code, a stock dividend can be effected by an appropriation of retained earnings to the common stock account by resolution of the general stockholders' meeting, followed by a free share distribution with respect to the amount appropriated by resolution of the Board of Directors' Meeting.

Common stock issue costs

Common stock issue costs are directly charged to retained earnings, net of tax, in the accompanying consolidated financial statements as the Japanese Commercial Code prohibits charging such stock issue costs to capital accounts which is the prevailing practice in the United States of America.

Recent pronouncements

In June 1997, the FASB issued FAS 130, "Reporting Comprehensive Income". This standard requires additional disclosures in the financial statements for periods beginning after December 15, 1997, and will have no effect on the company's financial position or results of operations.

In March 1998, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use". This SOP, which is effective for financial statements for fiscal years beginning after December 15, 1998, provides guidance on accounting for the costs of computer software developed or obtained solely to meet the company's internal needs. At this stage, it is not possible to estimate the impact of adoption on the company's financial position or results of operations.

Reclassifications

Certain reclassifications of the financial statements and related footnote amounts in the years ended March 31, 1996 and 1997 have been made to conform to the presentation in the year ended March 31, 1998.

3. U.S. dollar amounts

U.S. dollar amounts presented in the financial statements are included solely for the convenience of the reader. These translations should not be construed as representations that the yen amounts actually represent, or have been or could be converted into U.S. dollars. As the amounts shown in U.S. dollars are for convenience only, the rate of ¥132 = U.S. $1, the approximate current rate at March 31, 1998, has been used for the purpose of presentation of the U.S. dollar amounts in the accompanying consolidated financial statements.

4. Reconciliation of the differences between basic and diluted net income per share (EPS)

Reconciliation of the differences between basic and diluted EPS for the years ended March 31, 1996, 1997 and 1998 is as follows:

	Yen in millions	Thousands of shares	Yen
	Income	Weighted-average shares	EPS
For the year ended March 31, 1996			
Basic EPS			
Net income available to common stockholders	¥ 54,252	373,999	¥145.1
Effect of Dilutive Securities			
Warrants		15	
Convertible bonds	2,305	47,976	
Diluted EPS			
Net income for computation	¥ 56,557	421,990	¥134.0
For the year ended March 31, 1997			
Basic EPS			
Net income available to common stockholders	¥139,460	379,230	¥367.7
Effect of Dilutive Securities			
Warrants		69	
Convertible bonds	2,455	79,729	
Diluted EPS			
Net income for computation	¥141,915	459,028	¥309.2

	Yen in millions	Thousands of shares	Yen	Dollars
	Income	Weighted-average shares	EPS	
For the year ended March 31, 1998				
Basic EPS				
Net income available to common stockholders	**¥222,068**	**398,181**	**¥557.7**	**$4.23**
Effect of Dilutive Securities				
Warrants		**51**		
Convertible bonds	**2,271**	**65,890**		
Diluted EPS				
Net income for computation	**¥224,339**	**464,122**	**¥483.4**	**$3.66**

5. Accumulated amortization of intangibles and goodwill

Accumulated amortization of intangibles and goodwill amounted to ¥188,943 million and ¥218,225 million ($1,653,220 thousand) at March 31, 1997 and 1998, respectively.

6. Cash flow information

Cash payments during the year

Cash payments for income taxes were ¥88,565 million, ¥87,723 million and ¥239,054 million ($1,811,015 thousand) for the years ended March 31, 1996, 1997 and 1998, respectively; in these respective years, cash payments for interest were ¥69,882 million, ¥68,004 million and ¥64,102 million ($485,621 thousand).

Noncash investing and financing activities

Capital lease obligations of ¥9,563 million, ¥4,824 million and ¥4,406 million ($33,379 thousand) were incurred during the years ended March 31, 1996, 1997 and 1998, respectively.

Conversions of convertible debt into common stock and additional paid-in capital were ¥680 million, ¥63,578 million and ¥146,512 million ($1,109,939 thousand) for the years ended March 31, 1996, 1997 and 1998, respectively.

7. Inventories

Inventories comprise the following:

	Yen in millions		Dollars in thousands
	March 31		**March 31,**
	1997	**1998**	**1998**
Current:			
Finished products	¥527,418	**¥630,613**	**$4,777,371**
Work in process	119,406	**110,035**	**833,598**
Raw materials, purchased components and supplies	127,366	**134,392**	**1,018,121**
Film — released	73,767	**104,585**	**792,311**
— in process	21,843	**14,302**	**108,349**
	¥869,800	**¥993,927**	**$7,529,750**
Noncurrent:			
Film — released	¥143,003	**¥172,515**	**$1,306,932**
— in process	99,724	**76,551**	**579,932**
	¥242,727	**¥249,066**	**$1,886,864**

8. Account balances and transactions with affiliated companies

Account balances and transactions with affiliated companies are presented below:

	Yen in millions		Dollars in thousands
	March 31		**March 31,**
	1997	**1998**	**1998**
Accounts receivable, trade	¥13,232	**¥9,425**	**$71,402**
Accounts payable, trade	89	**945**	**7,159**

	Yen in millions			Dollars in thousands
	Year ended March 31			**Year ended**
	1996	1997	**1998**	**March 31, 1998**
Sales	¥123,623	¥96,183	**¥27,419**	**$207,720**
Purchases	2,647	733	**3,199**	**24,235**

9. Marketable securities and securities investments

Marketable securities and securities investments and other include debt and equity securities of which the aggregate fair value, gross unrealized gains and losses and cost pertaining to available-for-sale securities are as follows:

	Yen in millions							
	March 31, 1997				**March 31, 1998**			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Available-for-sale:								
Debt securities . .	¥531,968	¥ 22,001	¥1,338	¥552,631	**¥613,905**	**¥27,146**	**¥2,135**	**¥638,916**
Equity securities . .	49,512	124,682	2,364	171,830	**60,049**	**65,486**	**4,220**	**121,315**
Total.	¥581,480	¥146,683	¥3,702	¥724,461	**¥673,954**	**¥92,632**	**¥6,355**	**¥760,231**

	Dollars in thousands			
	March 31, 1998			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Available-for-sale:				
Debt securities	**$4,650,795**	**$205,652**	**$16,174**	**$4,840,273**
Equity securities	**454,917**	**496,106**	**31,970**	**919,053**
Total.	**$5,105,712**	**$701,758**	**$48,144**	**$5,759,326**

Marketable securities and securities investments and other as of March 31, 1997 and 1998 include short-term investments in money market funds and long-term advances to third parties of ¥65,776 million and ¥131,662 million ($997,439 thousand), respectively.

At March 31, 1998, debt securities mainly consist of Japanese government and municipal bonds and corporate debt securities due within 1 to 15 years.

During the years ended March 31, 1996, 1997 and 1998, the net unrealized gains on available-for-sale securities included in the separate component of stockholders' equity, net of applicable taxes, increased by ¥16,361 million, decreased by ¥14,055 million and decreased by ¥22,105 million ($167,462 thousand), respectively.

Proceeds from sales of available-for-sale securities were ¥397,774 million, ¥347,790 million and ¥359,815 million ($2,725,871 thousand) for the years ended March 31, 1996, 1997 and 1998, respectively. On those sales, gross realized gains computed on the average cost basis were ¥14,605 million, ¥19,174 million and ¥18,028 million ($136,576 thousand) and gross realized losses were ¥7,734 million, ¥9,877 million and ¥13,793 million ($104,492 thousand), respectively.

The net change in unrealized gain or loss on trading securities that has been included in earnings during the years ended March 31, 1996, 1997 and 1998 was insignificant.

In the ordinary course of business, the company maintains long-term investment securities, included in securities investments and other, issued by a number of nonpublic companies. The aggregate carrying amounts of the investments in nonpublic companies were ¥62,346 million and ¥60,527 million ($458,538 thousand) at March 31, 1997 and 1998, respectively. The corresponding fair values at those dates were not computed as such estimation was not readily determinable.

10. Short-term borrowings and long-term debt

Short-term borrowings at March 31, 1998 comprise the following:

	Yen in millions	Dollars in thousands
Loans, principally from banks, with interest ranging from 0.77% to 12.00% per annum	¥112,636	$853,303
Commercial paper with interest of 6.15% per annum	1,981	15,008
	¥114,617	$868,311

Long-term debt at March 31, 1998 comprises the following:

	Yen in millions	Dollars in thousands
Unsecured loans, representing obligations principally to banks, due 1998 to 2017 with interest ranging from 1.0% to 9.25% per annum	¥ 83,158	$ 629,985
Secured loans, representing obligations principally to banks, due 1999 to 2003 with interest ranging from 3.0% to 10.13% per annum	4,148	31,424
Medium-term notes of consolidated subsidiaries due 1998 to 2006 with interest ranging from 3.41% to 8.04% per annum	231,419	1,753,174
Unsecured 2.0% convertible bonds due 2000, convertible currently at ¥4,159.9 ($31.51) for one common share, redeemable before due date	342	2,591
Unsecured 0.15% convertible bonds due 2001, convertible currently at ¥6,519 ($49.39) for one common share, redeemable before due date	105,882	802,136
Unsecured 1.5% convertible bonds due 2002, convertible currently at ¥4,387.9 ($33.24) for one common share, redeemable before due date	772	5,848
Unsecured 1.4% convertible bonds due 2003, convertible currently at ¥5,415.5 ($41.03) for one common share, redeemable before due date	17,428	132,030
Unsecured 1.4% convertible bonds due 2005, convertible currently at ¥7,990.9 ($60.54) for one common share, redeemable before due date	297,772	2,255,848
Unsecured 0.1% bonds, due 1999 with detachable warrants	1,000	7,576
Unsecured 0.1% bonds, due 2000 with detachable warrants	2,000	15,152
Unsecured 0.1% bonds, due 2001 with detachable warrants	3,500	26,515
Unsecured 6.875% bonds due 2000, net of unamortized premium	50,149	379,917
Unsecured 4.4% bonds due 2001	80,000	606,061
Unsecured 6.125% notes due 2003, net of unamortized discount	193,022	1,462,288
Unsecured 1.95% bonds of a consolidated subsidiary, due 1998	15,000	113,636
Unsecured 2.55% notes of a consolidated subsidiary, due 2000	5,000	37,879
Unsecured 5.01% notes of a consolidated subsidiary, due 2000	25,362	192,136
Unsecured 2.0% bonds of a consolidated subsidiary, due 2001	15,000	113,636
Unsecured 2.5% bonds of a consolidated subsidiary, due 2003	15,000	113,636
Unsecured fixed coupon notes linked to the Yen/U.S. dollar rate of a consolidated subsidiary, due 2001	859	6,508
Secured 3.8% bonds of a consolidated subsidiary, due 2001, redeemable before due date	3,000	22,727
Long-term capital lease obligations, 1.15% to 16.28% per annum, due 1998 to 2006	26,863	203,508
Guarantee deposits received	12,538	94,985
	1,189,214	9,009,196
Less — Portion due within one year	84,794	642,378
	¥1,104,420	$8,366,818

On September 1, 1995, the company issued ¥1 billion ($7,576 thousand) of 0.1% bonds, with detachable 500 warrants. One warrant, which became exercisable from October 1, 1995, entitles the holder to subscribe ¥2 million ($15 thousand) for shares of common stock of the company at ¥5,330 ($40) per share (subject to adjustment in certain circumstances). Upon issuance of the bonds, the company bought all of these warrants and distributed such instruments at fair market value to the directors of the company as a part of their directors' remuneration. At March 31, 1998, 41 warrants were outstanding and will expire on August 31, 1999.

On August 16, 1996, the company issued ¥2 billion ($15,152 thousand) of 0.1% bonds, with detachable 1,000 warrants. One warrant, which became exercisable from October 1, 1996, entitles the holder to subscribe ¥2 million ($15 thousand) for shares of common stock of the company at ¥7,022 ($53) per share (subject to adjustment in certain circumstances). Upon issuance of the bonds, the company bought all of these warrants and distributed such instruments at fair market value to the directors and selected employees of the company as a part of their remuneration or salary. At March 31, 1998, 262 warrants were outstanding and will expire on August 15, 2000.

On October 13, 1997, the company issued ¥3.5 billion ($26,515 thousand) of 0.1% bonds, with detachable 1,750 warrants. One warrant, which will be exercisable from November 2, 1998, entitles the holder to subscribe ¥2 million ($15 thousand) for shares of common stock of the company at ¥11,788 ($89) per share (subject to adjustment in certain circumstances). Upon issuance of the bonds, the company bought all of these warrants and distributed such instruments at fair market value to the directors and selected employees of the company as a part of their remuneration or salary. At March 31, 1998, all warrants were outstanding and will expire on October 12, 2001.

On March 4, 1998, the company issued unsecured U.S. $1.5 billion Notes due 2003 denominated in U.S. dollars with an interest rate of 6.125%. The Notes are redeemable before the due date.

At March 31, 1998, 57,369 thousand shares of common stock would be issued upon conversion or exercise of all convertible debentures and warrants outstanding.

At March 31, 1998, property, plant and equipment with a book value of ¥5,191 million ($39,326 thousand) is mortgaged as security for loans and bonds issued by consolidated subsidiaries.

Aggregate amounts of annual maturities of long-term debt during the next five years are as follows:

Year ending March 31	Yen in millions	Dollars in thousands
1999	¥ 84,794	$ 642,378
2000	101,053	765,553
2001	245,517	1,859,977
2002	154,486	1,170,348
2003	224,114	1,697,833

The basic agreements with certain banks in Japan include provisions that collateral (including sums on deposit with such banks) or guarantors will be furnished upon the banks' request and that any collateral furnished, pursuant to such agreements or otherwise, will be applicable to all present or future indebtedness to such banks.

11. Insurance-related operations

The company's stock life insurance subsidiary maintains accounting records as noted in Note 2 in accordance with the accounting principles and practices prescribed by the Japanese Ministry of Finance (the "MOF"), which vary in some respects from U.S. GAAP. Those differences are mainly: that insurance acquisition costs are deferred and amortized generally over the premium-paying period of the insurance policies, that future policy benefits calculated locally under the authorization of the MOF are comprehensively adjusted to a net level premium method with certain adjustments of actuarial assumptions and that deferred income taxes are not recognized under local accounting practices. For purposes of preparing the consolidated financial statements, appropriate adjustments have been made to reflect such items in accordance with U.S. GAAP.

The amounts of statutory net equity of the subsidiary as of March 31, 1997 and 1998 were ¥12,625 million and ¥40,625 million ($307,765 thousand), respectively.

Deferred insurance acquisition costs

Insurance acquisition costs to be deferred, such as commission expenses, medical examination and inspection report fees, etc., vary with and are primarily related to acquiring new insurance policies and are amortized mainly over the premium-paying period of the related insurance policies using assumptions consistent with those used in computing policy reserves. Amortization charged to income for the years ended March 31, 1996, 1997 and 1998 amounted to ¥9,694 million, ¥15,855 million and ¥21,838 million ($165,439 thousand), respectively.

Future insurance policy benefits

Liabilities for future policy benefits are established in amounts adequate to meet the estimated future obligations of policies in force. These liabilities are computed by the net level premium method based upon estimates as to future investment yield, mortality and withdrawals. Future policy benefits are computed using interest rates ranging from approximately 2.75% to 6.25%, generally graded down after 10 to 20 years. Mortality, morbidity and withdrawal assumptions for all policies are based on either the life insurance subsidiary's own experience or various actuarial tables. At March 31, 1997 and 1998, future insurance policy benefits amounted to ¥528,204 million and ¥673,473 million ($5,102,068 thousand), respectively.

12. Financial instruments

The company has certain financial instruments including financial assets and liabilities and off-balance-sheet financial instruments incurred in the normal course of business. In applying a consistent risk management strategy, the company manages the exposure to market rate movements of its financial assets and liabilities through the use of derivative financial instruments which include foreign exchange forward contracts, foreign currency option contracts, interest rate swap agreements and interest rate and currency swap agreements designated as hedges. These instruments are executed with creditworthy financial institutions, and virtually all foreign currency contracts are denominated in U.S. dollars, German marks and other currencies of major countries. Although the company may be exposed to losses in the event of nonperformance by counterparties or interest and currency rate movements, it does not anticipate significant losses due to the nature of its counterparties or the hedging arrangements.

Following are explanatory notes regarding the financial assets and liabilities and off-balance-sheet financial instruments.

Cash and cash equivalents, time deposits and notes and accounts receivable, trade

In the normal course of business, substantially all cash and cash equivalents, time deposits and notes and accounts receivable, trade, are highly liquid and are carried at amounts which approximate fair value.

Notes and accounts payable, trade

In the normal course of business, substantially all notes and accounts payable, trade, are to be paid currently and their carrying amounts approximate fair value.

Short-term borrowings and long-term debt

The fair values of short-term borrowings and total long-term debt, including the current portion, were estimated based on the discounted amounts of future cash flows using the company's current incremental borrowing rates for similar liabilities.

Derivative financial instruments

The company utilizes foreign exchange forward contracts and foreign currency option contracts primarily to fix the cash flow value resulting from accounts receivable and payable and future transactions denominated in foreign currencies in relation to the core currencies (Japanese yen, U.S. dollars, and German marks) of the company's major operating units. Foreign exchange forward contracts, the majority of which mature within three months, are used to hedge this risk which is substantially associated with accounts receivable and payable and anticipated transactions denominated in foreign currencies. The contracted amounts outstanding at March 31, 1997 and 1998 were ¥756,294 million and ¥733,020 million ($5,553,182 thousand), respectively. The fair values of these contracts were estimated based on market quotations.

The company has entered into interest rate swap agreements and interest rate and currency swap agreements which mature from 1998 to 2006 to reduce its exposure to losses resulting from adverse fluctuations in interest rates or foreign currency exchange rates on underlying debt instruments. At March 31, 1997 and 1998, the aggregate notional principal amounts of the interest rate swap agreements were ¥176,705 million and ¥91,235 million ($691,174 thousand), respectively, and those of the interest rate and currency swap agreements were ¥300,269 million and ¥430,297 million ($3,259,826 thousand), respectively. The fair values of such agreements were estimated based on the discounted amounts of net future cash flows.

The company has entered into purchased foreign currency option contracts in the notional amounts of ¥196,990 million and ¥233,184 million ($1,766,545 thousand) at March 31, 1997 and 1998, respectively. The majority of these contracts expire within three months of the balance sheet dates. The company has also entered into written foreign currency option contracts in the notional amounts of ¥185,621 million and ¥279,406 million ($2,116,712 thousand) at March 31, 1997 and 1998, respectively. The majority of these contracts are part of range forward contract arrangements and expire in the same month with the corresponding purchased foreign currency option contracts described above. The fair values of such foreign currency options were estimated based on values quoted by brokers.

A consolidated insurance subsidiary has entered into written government bond option contracts as an integral part of short-term investing activities in order to fix the yields from bonds on hand to certain ranges. All of these contracts expire within two months of the balance sheet date and their notional principal amounts were ¥204,945 million and ¥181,509 million ($1,375,068 thousand) at March 31, 1997 and 1998, respectively. For accounting purposes, those transactions do not qualify for hedge accounting. Accordingly, those written bond option contracts were marked to market. The fair values of such written bond option contracts were estimated based on market quotations.

The estimated fair values of the company's financial instruments excluding debt and equity securities, both on and off the balance sheets, are summarized as follows:

	Yen in millions	
	Carrying amount	Estimated fair value
At March 31, 1997		
Cash and cash equivalents	¥ 428,518	¥ 428,518
Time deposits	52,518	52,518
Notes and accounts receivable, trade	1,066,314	1,066,314
Short-term borrowings	(117,801)	(117,801)
Notes and accounts payable, trade	(653,826)	(653,826)
Long-term debt including the current portion	(1,310,080)	(1,248,046)
Forward exchange contracts	997	2,464
Interest rate and currency swap agreements	—	(27,740)
Option contracts purchased	724	724
Option contracts written	(1,035)	(1,035)
Bond option contracts written	(1,026)	(1,026)
At March 31, 1998		
Cash and cash equivalents	**¥ 423,286**	**¥ 423,286**
Time deposits	**107,139**	**107,139**
Notes and accounts receivable, trade	**1,230,799**	**1,230,799**
Short-term borrowings	**(114,617)**	**(114,617)**
Notes and accounts payable, trade	**(768,152)**	**(768,152)**
Long-term debt including the current portion	**(1,189,214)**	**(1,191,367)**
Forward exchange contracts	**(471)**	**(1,682)**
Interest rate and currency swap agreements	**—**	**(24,757)**
Option contracts purchased	**2,461**	**2,461**
Option contracts written	**(2,548)**	**(2,548)**
Bond option contracts written	**(909)**	**(909)**

	Dollars in thousands	
	Carrying amount	Estimated fair value
At March 31, 1998		
Cash and cash equivalents	**$3,206,712**	**$3,206,712**
Time deposits	**811,659**	**811,659**
Notes and accounts receivable, trade	**9,324,235**	**9,324,235**
Short-term borrowings	**(868,311)**	**(868,311)**
Notes and accounts payable, trade	**(5,819,333)**	**(5,819,333)**
Long-term debt including the current portion	**(9,009,196)**	**(9,025,508)**
Forward exchange contracts	**(3,568)**	**(12,742)**
Interest rate and currency swap agreements	**—**	**(187,553)**
Option contracts purchased	**18,644**	**18,644**
Option contracts written	**(19,303)**	**(19,303)**
Bond option contracts written	**(6,886)**	**(6,886)**

13. Pension and severance plans

Upon terminating employment, employees of the parent company and subsidiaries in Japan are entitled, under most circumstances, to lump-sum indemnities or pension payments as described below. For employees voluntarily retiring, under normal circumstances, minimum payment is an amount based on current rates of pay and lengths of service. In calculating the minimum payment for employees involuntarily retiring, including employees retiring due to meeting mandatory retirement age requirements, the company may grant additional benefits. With respect to directors' resignations, lump-sum severance indemnities are calculated using a similar formula and are normally paid subject to the approval of the company's stockholders.

The parent company and most subsidiaries in Japan have contributory funded defined benefit pension plans, which are pursuant to the Japanese Welfare Pension Insurance Law. The contributory pension plans cover a portion of the governmental welfare pension program, under which the contributions are made by the companies and their employees, and an additional portion representing the substituted noncontributory pension plans. Under the contributory pension plans, the defined benefits representing the noncontributory portion of the plans, in general, cover 60% of the indemnities under the existing regulations to employees. The remaining indemnities are covered by severance payments by the companies. The pension benefits are determined based on years of service and the compensation amounts, as stipulated in the aforementioned regulations, are payable at the option of the retiring employee in a lump-sum amount or on a monthly pension. Contributions to the plans are funded through several financial institutions in accordance with the applicable laws and regulations.

Most foreign subsidiaries have defined benefit pension plans or severance indemnity plans which substantially cover all of their employees, under which the cost of benefits is currently funded or accrued. Benefits awarded under these plans are based primarily on current rate of pay and lengths of service.

Net pension and severance costs and the related pension plans' funded status including the employees' contributory portion and rate assumptions are shown below:

Japanese plans:

	Yen in millions			Dollars in thousands
	Year ended March 31			**Year ended**
	1996	1997	**1998**	**March 31, 1998**
Net pension and severance cost (credit):				
Service cost — benefits earned during the year	¥29,276	¥32,772	**¥39,436**	**$298,758**
Interest cost on projected benefit obligation	11,090	11,959	**13,303**	**100,780**
Actual return on plan assets	(9,545)	(14,373)	**(7,843)**	**(59,417)**
Net amortization and deferral	7,245	14,053	**7,037**	**53,311**
Actuarial net pension and severance cost for the year	38,066	44,411	**51,933**	**393,432**
Employee contributions	(4,098)	(4,073)	**(4,118)**	**(31,197)**
Net pension and severance cost for the year	¥33,968	¥40,338	**¥47,815**	**$362,235**

Foreign plans:

	Yen in millions			Dollars in thousands
	Year ended March 31			**Year ended**
	1996	1997	**1998**	**March 31, 1998**
Net pension and severance cost (credit):				
Service cost — benefits earned during the year	¥10,790	¥15,988	**¥15,625**	**$118,371**
Interest cost on projected benefit obligation	3,197	4,108	**4,911**	**37,204**
Actual return on plan assets	(4,122)	(3,897)	**(6,149)**	**(46,583)**
Net amortization and deferral	1,860	870	**2,365**	**17,917**
Net pension and severance cost for the year	¥11,725	¥17,069	**¥16,752**	**$126,909**

Pension plans' funded status:

	Japanese plans			Foreign plans		
	Yen in millions		Dollars in thousands	Yen in millions		Dollars in thousands
	March 31		**March 31,**	March 31		**March 31,**
	1997	**1998**	**1998**	1997	**1998**	**1998**
Actuarial present value of obligations—						
Vested benefit	¥268,719	**¥327,802**	**$2,483,348**	¥50,325	**¥57,119**	**$432,720**
Nonvested benefit	53,311	**61,508**	**465,970**	4,060	**5,850**	**44,318**
Accumulated benefit obligation	322,030	**389,310**	**2,949,318**	54,385	**62,969**	**477,038**
Additional benefits related to projected salary increase	71,418	**86,758**	**657,258**	20,288	**22,190**	**168,106**
Projected benefit obligation	393,448	**476,068**	**3,606,576**	74,673	**85,159**	**645,144**
Plan assets at fair value	204,491	**236,966**	**1,795,197**	43,837	**54,597**	**413,614**
Excess of projected benefit obligation over plan assets	188,957	**239,102**	**1,811,379**	30,836	**30,562**	**231,530**
Unrecognized net loss	(59,740)	**(91,343)**	**(691,992)**	(4,805)	**(4,617)**	**(34,977)**
Unrecognized net transition asset	3,104	**2,729**	**20,674**	1,453	**492**	**3,727**
Unrecognized prior service cost	(12,807)	**(12,496)**	**(94,667)**	—	**2,651**	**20,084**
Adjustment required to recognize minimum pension liability	—	**20,692**	**156,758**	—	**—**	**—**
Net pension liability recognized in the balance sheet	¥119,514	**¥158,684**	**$1,202,152**	¥27,484	**¥29,088**	**$220,364**
Assumptions used in developing the pension obligation as of March 31:						
Discount rate	3.5%	**3.0%**		6.5 - 9.0%	**6.5-8.0%**	
Long-term rate of salary increase	3.0%	**3.0%**		2.5 - 8.5%	**2.5-8.5%**	
Long-term rate of return on funded assets	3.7%	**4.0%**		7.0-10.0%	**6.5-9.8%**	

As required under FAS 87 "Employers' Accounting for Pensions", the assumptions are reviewed in accordance with changes in circumstances. Such changes in assumptions are the primary reason for the fluctuation in the projected benefit obligation and unrecognized net gains and losses.

Under FAS 87, the company has recorded a pension liability to cover the amount of the projected benefit obligation in excess of plan assets, considering unrealized items and the minimum pension liability. The minimum pension liability which the company has recognized represents the excess of accumulated benefits over plan assets and accrued pension cost. A corresponding amount was recognized as an intangible asset to the extent of unrecognized prior service cost, and the balance was recorded as a separate reduction of stockholders' equity, net of tax.

The plan assets are invested primarily in interest bearing securities and listed equity securities.

14. Income taxes

The company is subject to a number of different income taxes which, in the aggregate, indicate a statutory rate in Japan of approximately 51%. Due to a change in Japanese income tax regulations, effective April 1, 1998, the statutory rate was reduced to approximately 48% and such amount has been used in calculating the future expected tax effects of temporary differences. The effect of the enacted change in the tax rate was insignificant.

Reconciliation of the differences between the statutory tax rate and the effective income tax rate is as follows:

	Year ended March 31		
	1996	1997	**1998**
Statutory tax rate	51.0%	51.0%	**51.0%**
Increase (reduction) in taxes resulting from:			
Income tax credit	(2.8)	(2.8)	**(2.4)**
Current operating losses of subsidiaries	7.9	5.2	**1.9**
Other	(0.2)	(1.0)	**(3.1)**
Effective income tax rate	55.9%	52.4%	**47.4%**

The significant components of deferred tax assets and liabilities are as follows:

	Yen in millions		Dollars in thousands
	March 31		**March 31,**
	1997	**1998**	**1998**
Deferred tax assets:			
Operating loss carryforwards for tax purposes	¥ 75,536	**¥ 79,761**	**$ 604,250**
Accrued pension and severance costs	45,418	**54,487**	**412,780**
Warranty reserve and accrued expenses	46,187	**52,445**	**397,311**
Inventory – intercompany profits and write-down	44,416	**38,915**	**294,811**
Future insurance policy benefits	34,580	**38,686**	**293,076**
Accrued enterprise taxes	12,952	**18,276**	**138,454**
Other accrued employees' compensation	14,465	**12,336**	**93,454**
Other	74,173	**77,232**	**585,091**
Gross deferred tax assets	347,727	**372,138**	**2,819,227**
Less: Valuation allowance	(122,258)	**(125,908)**	**(953,848)**
Total deferred tax assets	225,469	**246,230**	**1,865,379**
Deferred tax liabilities:			
Undistributed earnings of foreign subsidiaries	(68,928)	**(77,833)**	**(589,644)**
Insurance acquisition costs	(67,004)	**(67,858)**	**(514,076)**
Unrealized gain on securities	(72,741)	**(41,185)**	**(312,007)**
Depreciation	(17,041)	**(13,264)**	**(100,485)**
Other	(39,133)	**(45,773)**	**(346,765)**
Gross deferred tax liabilities	(264,847)	**(245,913)**	**(1,862,977)**
Net deferred tax assets (liabilities)	¥(39,378)	**¥ 317**	**$ 2,402**

The valuation allowance mainly relates to deferred tax assets of consolidated subsidiaries with operating loss carryforwards for tax purposes that are not expected to be realized. The net changes in the total valuation allowance for the years ended March 31, 1996, 1997 and 1998 were increases of ¥28,174 million, ¥3,902 million and ¥3,650 million ($27,652 thousand), respectively.

Net deferred tax assets (liabilities) are included in the consolidated balance sheets as follows:

	Yen in millions		Dollars in thousands
	March 31		**March 31,**
	1997	**1998**	**1998**
Current assets — Deferred income taxes	¥111,756	**¥121,189**	**$ 918,098**
Other assets — Other	27,158	**30,523**	**231,235**
Current liabilities — Other	(4,341)	**(4,279)**	**(32,416)**
Long-term liabilities — Deferred income taxes	(173,951)	**(147,116)**	**(1,114,515)**
Net deferred tax assets (liabilities)	¥(39,378)	**¥ 317**	**$ 2,402**

At March 31, 1998, no deferred income taxes have been provided on undistributed earnings of foreign subsidiaries not expected to be remitted in the foreseeable future totaling ¥295,778 million ($2,240,742 thousand), and on the gain on a subsidiary's sale of stock of ¥61,544 million arising from the issuance of common stock of Sony Music Entertainment (Japan) Inc. in a public offering to third parties in November 1991, as the company does not anticipate any significant tax consequences on possible future disposition of its remaining investment based on its tax planning strategies. The unrecognized deferred tax liabilities as of March 31, 1998 for such temporary differences amounted to ¥109,827 million ($832,023 thousand).

Operating loss carryforwards for tax purposes of consolidated subsidiaries at March 31, 1998 amounted to approximately ¥235,319 million ($1,782,720 thousand) and are available as an offset against future taxable income of such subsidiaries. These carryforwards expire at various dates primarily up to 15 years. Realization is dependent on such subsidiaries generating sufficient taxable income prior to expiration of the loss carryforwards. Although realization is not assured, management believes it is more likely than not that all of the deferred tax assets, less valuation allowance, will be realized. The amount of such net deferred tax assets considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

15. Stockholders' equity

Changes in common stock, additional paid-in capital and treasury stock have resulted from the following:

	Number of shares	Yen in millions		
	Common stock		Additional paid-in capital	Treasury stock, at cost
Balance at March 31, 1995	373,911,490	¥ 299,589	¥ 441,241	¥ (6)
Conversion of convertible debt	156,216	296	384	—
Common stock warrants	—	—	110	—
Purchase of treasury stock	—	—	—	(955)
Reissuance of treasury stock	—	—	—	935
Balance at March 31, 1996	374,067,706	299,885	441,735	(26)
Exercise of stock purchase warrants	117,838	336	336	—
Conversion of convertible debt	9,999,499	31,816	31,762	—
Common stock warrants	—	—	200	—
Purchase of treasury stock	—	—	—	(3,156)
Reissuance of treasury stock	—	—	—	3,086
Balance at March 31, 1997	384,185,043	332,037	474,033	(96)
Exercise of stock purchase warrants	**264,562**	**861**	**860**	**—**
Conversion of convertible debt	**22,745,666**	**73,298**	**73,214**	**—**
Common stock warrants	**—**	**—**	**315**	**—**
Purchase of treasury stock	**—**	**—**	**—**	**(7,948)**
Reissuance of treasury stock	**—**	**—**	**—**	**5,164**
Balance at March 31, 1998	**407,195,271**	**¥406,196**	**¥548,422**	**¥(2,880)**

	Dollars in thousands		
	Common stock	Additional paid-in capital	Treasury stock, at cost
Balance at March 31, 1997	$2,515,432	$3,591,159	$ (727)
Exercise of stock purchase warrants	**6,522**	**6,515**	**—**
Conversion of convertible debt	**555,288**	**554,652**	**—**
Common stock warrants	**—**	**2,386**	**—**
Purchase of treasury stock	**—**	**—**	**(60,212)**
Reissuance of treasury stock	**—**	**—**	**39,121**
Balance at March 31, 1998	**$3,077,242**	**$4,154,712**	**$(21,818)**

On November 20, 1991, the company made a free share distribution of 33,908,621 shares for which no accounting entry is required in Japan. Had the distribution been accounted for in the manner adopted by companies in the United States of America, ¥201,078 million ($1,523,318 thousand) would have been transferred from retained earnings to the appropriate capital accounts.

Conversions of convertible debt into common stock are accounted for in accordance with the provisions of the Japanese Commercial Code by crediting approximately one-half of the conversion proceeds to the common stock account and the remainder to the additional paid-in capital account.

The Japanese Commercial Code provides that an amount equal to at least 10% of cash dividends and other distributions from retained earnings paid by the parent company and its Japanese subsidiaries be appropriated as a legal reserve. The amounts of statutory retained earnings of the parent company available for the payments of dividends to stockholders as of March 31, 1997 and 1998 were ¥507,253 million and ¥555,643 million ($4,209,417 thousand), respectively. These amounts include cash dividends for the six-month periods ended March 31, 1997 and 1998, respectively, which have been incorporated in the accompanying consolidated financial statements.

The appropriations of retained earnings for the year ended March 31, 1998, which have been incorporated in the accompanying consolidated financial statements, will be proposed for approval at the general stockholders' meeting to be held on June 26, 1998 and will be recorded in the statutory books of account, in accordance with the Japanese Commercial Code, after stockholders' approval.

The ordinary general meeting of stockholders held on June 27, 1997 authorized the company, pursuant to the Japanese regulations, to acquire and retire up to a total not exceeding 30 million outstanding shares of its common stock with its profit, on and after June 28, 1997, whenever deemed necessary by the Board of Directors in view of general economic conditions, the company's business performance and financial condition and other factors. At March 31, 1998, no common stock had been acquired under this authorization.

On May 7, 1998, the company's Board of Directors resolved the following proposals to be approved by the general stockholders' meeting to be held on June 26, 1998. The proposals resolve that (a) in addition to the shares discussed in the preceding paragraph, on and after June 27, 1998, the company may, by a resolution of the Board of Directors, acquire and retire up to a total not exceeding 30 million outstanding shares of its common stock with its additional paid-in capital at prices in total not exceeding ¥400 billion ($3,030,303 thousand) and (b) the company may grant share subscription rights to directors and/or employees pursuant to the Japanese regulations.

In February 1998, the company adopted a cash stock appreciation rights plan (the "SARs") as an incentive plan for selected employees. Under the terms of the plan, the SARs may be exercised during the period from 1999 until 2004. No compensation expense was recognized for the SARs in the year ended March 31, 1998 as the company's stock price did not exceed the strike price of the SARs.

An analysis of the changes in the minimum pension liability adjustment and the cumulative translation adjustment are presented below:

	Yen in millions			Dollars in thousands
	Year ended March 31			**Year ended**
	1996	1997	**1998**	**March 31, 1998**
Minimum pension liability adjustment:				
Balance, beginning of year	—	—	**—**	**—**
Valuation adjustment, net of related income taxes	—	—	**¥(5,714)**	**$(43,288)**
Balance, end of year	—	—	**¥(5,714)**	**$(43,288)**
Cumulative translation adjustment:				
Balance, beginning of year	¥(411,167)	¥(302,503)	**¥(181,221)**	**$(1,372,886)**
Aggregate translation adjustment for the year	114,461	127,705	**35,985**	**272,614**
Income taxes for the year allocated to translation adjustment	(5,797)	(6,423)	**4,511**	**34,174**
Balance, end of year	¥(302,503)	¥(181,221)	**¥(140,725)**	**$(1,066,098)**

16. Research and development expenses and advertising costs

Research and development expenses

Research and development expenses charged to cost of sales for the years ended March 31, 1996, 1997 and 1998 were ¥257,326 million, ¥282,569 million and ¥318,044 million ($2,409,424 thousand), respectively.

Advertising costs

Advertising costs included in selling, general and administrative expenses for the years ended March 31, 1996, 1997 and 1998 were ¥159,821 million, ¥216,579 million and ¥268,985 million ($2,037,765 thousand), respectively.

17. Leased assets

The company leases certain plant facilities, office space, warehouses, employees' residential facilities and other assets.
An analysis of leased assets under capital leases is as follows:

	Yen in millions		Dollars in thousands
	March 31		**March 31,**
Class of property	1997	**1998**	**1998**
Land	¥ 2,538	**¥ 2,501**	**$ 18,947**
Buildings	24,623	**21,682**	**164,257**
Machinery and equipment	9,682	**10,103**	**76,538**
Accumulated amortization	(13,022)	**(12,243)**	**(92,750)**
	¥23,821	**¥22,043**	**$166,992**

The following is a schedule by year of the future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of March 31, 1998:

Year ending March 31	Yen in millions	Dollars in thousands
1999	¥ 6,675	$ 50,568
2000	5,449	41,280
2001	4,459	33,780
2002	4,431	33,568
2003	4,198	31,803
Later years	9,378	71,046
Total minimum lease payments	34,590	262,045
Less — Amount representing interest	7,727	58,537
Present value of net minimum lease payments	26,863	203,508
Less — Current obligations	5,135	38,902
Long-term capital lease obligations	¥21,728	$164,606

Rental expenses under operating leases for the years ended March 31, 1996, 1997 and 1998 were ¥81,385 million, ¥86,570 million and ¥87,564 million ($663,364 thousand), respectively. The minimum rental payments required under operating leases that have initial or remaining noncancelable lease terms in excess of one year at March 31, 1998 are as follows:

Year ending March 31	Yen in millions	Dollars in thousands
1999	¥ 44,269	$ 335,371
2000	42,416	321,334
2001	35,119	266,053
2002	28,575	216,477
2003	24,000	181,818
Later years	158,396	1,199,970
Total minimum future rentals	¥332,775	$2,521,023

18. Commitments and contingent liabilities

Commitments outstanding at March 31, 1998 for the purchase of property, plant and equipment and other assets approximated ¥54,474 million ($412,682 thousand).

Contingent liabilities for guarantees given in the ordinary course of business and for employee loans amounted to ¥123,065 million ($932,311 thousand) at March 31, 1998.

The company has entered into agreements with financial institutions whereby the company can sell specifically identified accounts receivable and future receivables with limited recourse. For the years ended March 31, 1996, 1997 and 1998, the company did not sell any specifically identified accounts receivable or future receivables. As of March 31, 1997 and 1998, the outstanding balance of all receivables sold with limited recourse amounted to ¥868 million and ¥0 million ($0 thousand), respectively.

The company has also entered into agreements with financial institutions whereby the company can sell up to ¥125,400 million ($950,000 thousand) of undivided interests in a pool of eligible receivables with limited recourse. The maximum pool of eligible receivables sold outstanding at any one time during the years ended March 31, 1996, 1997 and 1998 amounted to ¥71,868 million, ¥0 million and ¥0 million ($0 thousand), respectively. As of March 31, 1997 and 1998, there were no outstanding balances of receivables sold.

Under the terms of each of the receivable sale agreements, the company has retained substantially the same risk of credit loss as if the receivables had not been sold. The company has fully reserved for these potential credit losses. The company pays fees which approximate the purchasers' costs of issuing commercial paper and are included in other expense.

Certain subsidiaries in the music business entered into long-term contracts with recording artists and companies for the production and/or distribution of prerecorded music and videos. These contracts cover various periods mainly through March 31, 2001. As of March 31, 1998, these subsidiaries were committed to make payments under such long-term contracts of ¥24,211 million ($183,417 thousand).

The parent company and certain of its subsidiaries are defendants in several pending lawsuits. However, based upon the information currently available to both the company and its legal counsel, management of the company believes that damages from such lawsuits, if any, would not have a material effect on the company's consolidated financial statements.

19. Business segment information

Effective for the year ended March 31, 1998, the company adopted FAS 131, "Disclosures about Segments of an Enterprise and Related Information" which requires disclosure of financial and descriptive information about the company's reportable operating segments. The operating segments reported below are the segments of the company for which separate financial information is available and for which operating profit/loss amounts are evaluated regularly by executive management in deciding how to allocate resources and in assessing performance.

The operating segment information reported below differs from the industry segment information previously disclosed under FAS 14, "Financial Reporting for Segments of a Business Enterprise" in that the Game business was previously included in the Electronics segment, the Music and Pictures businesses were previously combined in the Entertainment segment, and the company's financing operations, which were previously in the Insurance and financing segment, are now included as part of the Other segment below. The operating segment information, as well as geographic data, for previous years have been reclassified to conform to the segment presentation for the year ended March 31, 1998.

The Electronics segment develops, designs, manufactures and distributes audiovisual equipment, instruments and devices throughout the world. The Game segment develops, designs and sells PlayStation game consoles and related software mainly in Japan, the United States and Europe, and licenses to the third party software developers. The Music segment is mainly engaged worldwide in the development, production, manufacture, and distribution of recorded music, in all commercial formats and musical genres. The Pictures segment develops, produces, and manufactures image-based software, including film, video, and television mainly in the United States, and in their marketing worldwide. The Insurance segment represents insurance-related underwriting business, primarily individual life insurance business in the Japanese market. The Other segment consists of other various operating activities primarily including customer financing and leasing business, and media-communication network businesses relating to broadcasting and information technology. The company's products and services are generally unique to a single operating segment.

Business segments

Sales and operating revenue:

	Yen in millions			Dollars in thousands
	Year ended March 31			Year ended
	1996	1997	**1998**	**March 31, 1998**
Sales and operating revenue:				
Electronics —				
Customers	¥3,283,234	¥3,930,292	**¥4,377,346**	**$33,161,712**
Intersegment	182,222	201,339	**312,764**	**2,369,424**
Total	3,465,456	4,131,631	**4,690,110**	**35,531,136**
Game —				
Customers	200,894	408,335	**699,574**	**5,299,803**
Intersegment	3,017	10,943	**22,977**	**174,068**
Total	203,911	419,278	**722,551**	**5,473,871**
Music —				
Customers	506,455	570,119	**660,407**	**5,003,083**
Intersegment	11,380	21,961	**34,307**	**259,902**
Total	517,835	592,080	**694,714**	**5,262,985**
Pictures —				
Customers	317,382	438,551	**642,714**	**4,869,046**
Intersegment	198	3	**450**	**3,409**
Total	317,580	438,554	**643,164**	**4,872,455**
Insurance —				
Customers	206,802	227,920	**291,061**	**2,205,008**
Intersegment	101	14	**7**	**53**
Total	206,903	227,934	**291,068**	**2,205,061**
Other —				
Customers	77,798	87,917	**84,388**	**639,303**
Intersegment	196,177	152,457	**163,841**	**1,241,220**
Total	273,975	240,374	**248,229**	**1,880,523**
Elimination	(393,095)	(386,717)	**(534,346)**	**(4,048,076)**
Consolidated total	¥4,592,565	¥5,663,134	**¥6,755,490**	**$51,177,955**

Segment profit or loss:

	Yen in millions			Dollars in thousands
	Year ended March 31			Year ended
	1996	1997	**1998**	**March 31, 1998**
Operating income (loss):				
Electronics	¥193,331	¥239,312	**¥314,538**	**$2,382,864**
Game	(8,938)	57,045	**116,936**	**885,879**
Music	40,129	45,216	**54,084**	**409,727**
Pictures	23,862	28,925	**35,544**	**269,273**
Insurance	7,116	19,099	**20,326**	**153,985**
Other	(6,078)	(1,422)	**(10,292)**	**(77,970)**
Total	249,422	388,175	**531,136**	**4,023,758**
Elimination	5,188	3,390	**10,749**	**81,432**
Unallocated amounts: Corporate expenses	(19,286)	(21,235)	**(21,675)**	**(164,205)**
Consolidated operating income	235,324	370,330	**520,210**	**3,940,985**
Other income	65,755	92,643	**83,963**	**636,083**
Other expenses	(162,920)	(150,544)	**(150,424)**	**(1,139,576)**
Consolidated income before income taxes	¥138,159	¥312,429	**¥453,749**	**$3,437,492**

Assets:

	Yen in millions			Dollars in thousands
	March 31			March 31,
	1996	1997	1998	1998
Total assets:				
Electronics	¥2,798,818	¥3,014,756	**¥3,253,990**	**$24,651,439**
Game	75,964	128,056	**197,605**	**1,497,008**
Music	594,949	714,792	**835,939**	**6,332,871**
Pictures	635,284	796,942	**915,545**	**6,935,947**
Insurance	563,784	716,843	**899,016**	**6,810,727**
Other	318,128	275,824	**309,150**	**2,342,046**
Total	4,986,927	5,647,213	**6,411,245**	**48,570,038**
Elimination	(227,635)	(204,006)	**(221,112)**	**(1,675,091)**
Corporate assets	286,407	237,039	**212,910**	**1,612,955**
Consolidated total	¥5,045,699	¥5,680,246	**¥6,403,043**	**$48,507,902**

Other significant items:

	Yen in millions			Dollars in thousands
	Year ended March 31			Year ended
	1996	1997	1998	March 31, 1998
Depreciation and amortization:				
Electronics	¥162,592	¥187,960	**¥197,449**	**$1,495,826**
Game	2,198	3,738	**12,536**	**94,969**
Music	22,323	28,707	**30,933**	**234,341**
Pictures	10,613	13,286	**16,668**	**126,273**
Insurance, including deferred insurance acquisition costs	9,880	15,870	**22,410**	**169,773**
Other	16,683	14,141	**17,539**	**132,871**
Total	224,289	263,702	**297,535**	**2,254,053**
Corporate	3,027	2,830	**4,130**	**31,288**
Consolidated total	¥227,316	¥266,532	**¥301,665**	**$2,285,341**
Capital expenditures for segment assets:				
Electronics	¥185,638	¥226,696	**¥301,197**	**$2,281,796**
Game	4,776	5,757	**17,114**	**129,652**
Music	25,842	31,807	**28,361**	**214,856**
Pictures	15,658	15,194	**13,477**	**102,098**
Insurance	1,484	176	**633**	**4,795**
Other	15,645	16,502	**24,102**	**182,591**
Total	249,043	296,132	**384,884**	**2,915,788**
Corporate	2,154	1,946	**3,071**	**23,265**
Consolidated total	¥251,197	¥298,078	**¥387,955**	**$2,939,053**

Equity earnings for the years ended March 31, 1996, 1997 and 1998, which were included in sales and operating revenue for the years then ended, were not material.

Geographic information

Sales and operating revenue which are attributed to countries based on location of customers and long-lived assets for the years ended March 31, 1996, 1997 and 1998 are as follows:

	Yen in millions			Dollars in thousands
	Year ended March 31			**Year ended**
	1996	1997	**1998**	**March 31, 1998**
Sales and operating revenue:				
Japan	¥1,379,804	¥1,590,820	**¥1,843,149**	**$13,963,250**
U.S.A.	1,259,926	1,639,334	**2,101,907**	**15,923,538**
Europe	1,054,010	1,304,491	**1,567,121**	**11,872,129**
Other	898,825	1,128,489	**1,243,313**	**9,419,038**
Total	¥4,592,565	¥5,663,134	**¥6,755,490**	**$51,177,955**

	Yen in millions			Dollars in thousands
	March 31			**March 31,**
	1996	1997	**1998**	**1998**
Long-lived assets:				
Japan	¥ 701,413	¥ 730,075	**¥ 843,800**	**$ 6,392,424**
U.S.A.	694,733	824,439	**845,887**	**6,408,235**
Europe	147,339	174,524	**192,695**	**1,459,811**
Other	166,842	194,683	**209,984**	**1,590,788**
Total	¥1,710,327	¥1,923,721	**¥2,092,366**	**$15,851,258**

There are not any individually material countries with respect to the sales and operating revenue and long-lived assets included in the Europe and Other areas.

Transfers between reportable business or geographic segments are made at arms-length prices. Operating income is sales and operating revenue less costs and operating expenses. Unallocated corporate assets consist primarily of cash and cash equivalents and marketable securities maintained for general corporate purposes.

There has been no sales and operating revenue with a single major external customer for the years ended March 31, 1996, 1997 and 1998.

The following information is sales and operating revenue and operating income which show those recognized by geographic origin for the years ended March 31, 1996, 1997 and 1998. In addition to the disclosure requirements under FAS 131, the company discloses this information as the supplemental information in light of the disclosure requirement of the Japanese Securities and Exchange Law, which a Japanese public company is subject to.

	Yen in millions			Dollars in thousands
	Year ended March 31			**Year ended**
	1996	1997	**1998**	**March 31, 1998**
Sales and operating revenue:				
Japan —				
Customers	¥1,768,132	¥2,048,406	**¥2,361,734**	**$17,891,924**
Intersegment	1,275,251	1,386,422	**1,697,655**	**12,861,023**
Total	3,043,383	3,434,828	**4,059,389**	**30,752,947**
U.S.A. —				
Customers	1,250,712	1,672,173	**2,156,173**	**16,334,644**
Intersegment	113,121	126,637	**153,603**	**1,163,659**
Total	1,363,833	1,798,810	**2,309,776**	**17,498,303**
Europe —				
Customers	886,468	1,100,958	**1,338,232**	**10,138,122**
Intersegment	30,299	42,381	**62,506**	**473,530**
Total	916,767	1,143,339	**1,400,738**	**10,611,652**
Other —				
Customers	687,253	841,597	**899,351**	**6,813,265**
Intersegment	509,120	603,518	**715,156**	**5,417,849**
Total	1,196,373	1,445,115	**1,614,507**	**12,231,114**
Elimination	(1,927,791)	(2,158,958)	**(2,628,920)**	**(19,916,061)**
Consolidated	¥4,592,565	¥5,663,134	**¥6,755,490**	**$51,177,955**
Operating income:				
Japan	¥147,582	¥259,376	**¥348,458**	**$2,639,833**
U.S.A.	32,372	30,928	**75,820**	**574,394**
Europe	48,621	70,597	**74,064**	**561,091**
Other	55,772	69,858	**69,490**	**526,440**
Corporate and elimination	(49,023)	(60,429)	**(47,622)**	**(360,773)**
Consolidated	¥235,324	¥370,330	**¥520,210**	**$3,940,985**

[Report of Independent Accountants]

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Shibuya-ku, Tokyo 150-6013

Telephone 03-5424-8100

Price Waterhouse

May 7, 1998

To the Stockholders and Board of Directors of
Sony Corporation (Sony Kabushiki Kaisha)

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and retained earnings and of cash flows present fairly, in all material respects, the financial position of Sony Corporation and its consolidated subsidiaries at March 31, 1997 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 1998, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

Price Waterhouse

[Investor Information]

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Sony on the Internet
Sony's Home Pages on the World Wide Web offer a wealth of corporate and product information, including the latest annual report and financial results.
'Sony online World' http://www.world.sony.com/
'Sony online USA' http://www.sony.com/

Environmental Report
If you would like a copy of the above report, please direct your request to:
Sony Corporation
Corporate Environmental Affairs
Phone: (03) 5448-3533
Facsimile: (03) 5448-7838
This report is also available on the World Wide Web.
http://www.sony.co.jp/soj/CorporateInfo/

Ordinary General Meeting of Shareholders
The Ordinary General Meeting of Shareholders will be held at the end of June in Tokyo.

Independent Accountants
Price Waterhouse
Tokyo, Japan

Depositary, Transfer Agent, and Registrar for American Depositary Receipts
Morgan Guaranty Trust Company of New York
Shareholder Relations
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CIBC Mellon Trust Company
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Overseas Stock Exchange Listings
New York, Pacific, Chicago, Toronto, London, Paris, Frankfurt, Düsseldorf, Brussels, Vienna, and Swiss stock exchanges

Japanese Stock Exchange Listings
Tokyo, Osaka, Nagoya, Fukuoka, and Sapporo stock exchanges

Number of Shareholders
(As of March 31, 1998)
183,720

Sony Corporation

Printed in Japan