New Management Benchmark – Promoting Risk Capital Management –

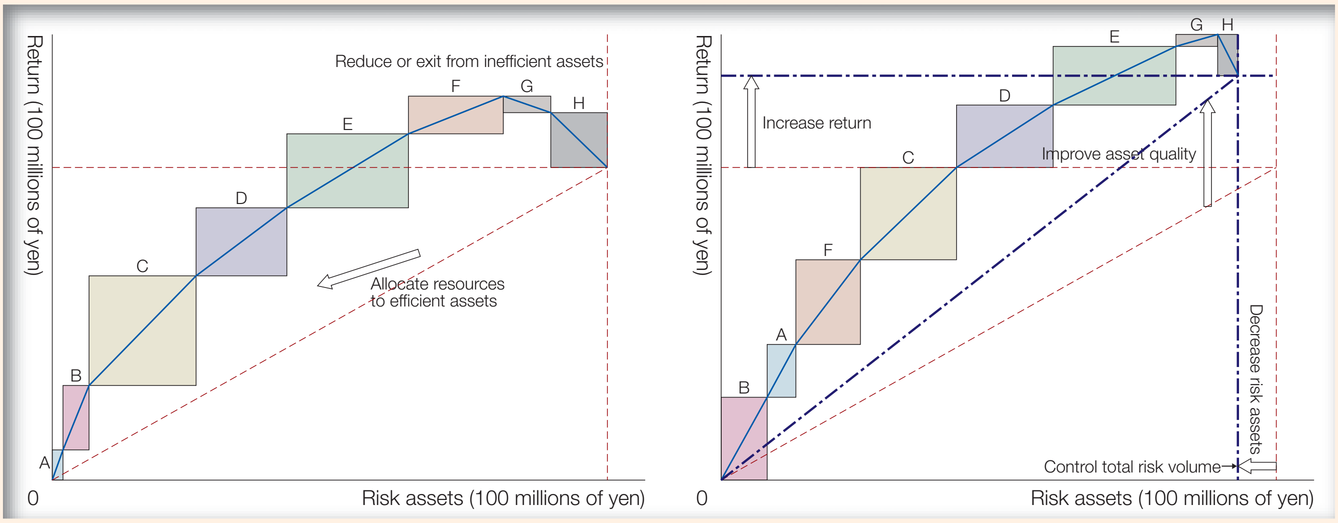
By introducing Risk Capital Management (RCM), a management tool focusing on risk as its key concept, ITOCHU is exiting from inefficient assets and allocating resources to efficient assets to enhance corporate value. RCM is designed to control total risk volume by quantifying risks as risk assets (note 1), and to measure asset efficiency in Risk Return Index (RRI) (note 2), which is return on risk assets.

By segmenting the business areas of Division Companies into business units according to the each business's attributes, we measure and analyze the asset efficiency of each business by using the RCM method. In addition to estimated market growth potential, RRI is used as a criterion for optimizing resource allocation.

Specifically, for each Division Company, we create a graph (note 3), whose example is shown in Graph 1. This graph arranges segments in descending order of efficiency from the left, showing risk asset volume, return (net income), and asset efficiency (RRI = diagonal line) for both each business unit and the Division Company as a whole. In this example, inefficient businesses (ex. G, H) on the right of the graph will basically be subject to a strategy of downsizing or withdrawal, unless growth is expected. Eventually we will reduce assets or exit from inefficient businesses. The resources that are recovered through this process will then be reallocated to new strategic projects to increase the efficient assets (ex. A, B) on the left. By shifting assets in unprofitable business areas to new strategic business areas, we aim to improve overall profitability and enhance corporate value. At the same time, setting a risk asset limit as a covenant, or item to be monitored, for each Division Company, we control total risk volume (risk asset amount), for new investments as well as for existing businesses.

By doing the above activities, we are promoting the Super A&P strategy, in which we accelerate reallocation of assets to shift management resources selectively to more efficient business areas.

Graph1: Example of a Division Company



Note 1: Risk Assets

Risk assets represent the maximum amount of the possible loss caused by the held assets. Statistical methods are used to measure risk weight of each asset according to its attributes and risk assets are then calculated by multiplying asset amount by risk weight. Not only assets on the balance sheet, but guarantees, foreign exchange balances and other off-balance sheet items are subject to this risk asset evaluation and included in the total risk assets.

(Examples)

- Trade receivables: Each customer is assigned a credit rating based on its financial data, and a risk weight is assigned to each customer based on the credit rating, which is linked with its default rate. Risk assets are then calculated in consideration of collateral and other security. The same method is applied to loans and guarantees.
- Listed stocks/Land: Risk weight is calculated based on the volatility of stock prices or land prices.
- Associated company investment: Risk assets are calculated by multiplying risk asset volume of the associated company, which is calculated by each asset account, by ITOCHU's share.
- Inventories: Risk assets are calculated for the book balance of the item by assigning risk weight based on market price volatility. Risk assets for inventories with sales contracts are calculated by assigning risk weight that considers the probability of cancellation, as well as market price volatility.

Note 2: Risk Return Index (RRI)

Risk Return Index (RRI) = Net income ÷ Risk assets

RRI is used to measure efficiency in comparison with cost of equity. Cost of equity is currently set at 8%. Units with RRI over 8% and ROA over 2% are considered efficient segments.

Note 3: Graph

This graph plots returns (net income) on the vertical axis and risk assets on the horizontal axis. The diagonal line shows RRI.

Please see page 66 of Financial Section for the overall Company's risk management system and methods for managing market, credit, country, and investment risk.