Management's Discussion and Analysis

Changes in the Scope of Consolidation

During the fiscal year ended March 31, 2007, the Anritsu Group established two companies, Anritsu EMEA Ltd. in the United Kingdom and Anritsu Company S.A. de C.V. in Mexico, and added them to the scope of consolidation. The Anritsu Group also liquidated two companies, NetTest (Pty) Ltd. and NetTest (China) Co., Ltd. As a result, the Anritsu Group comprised 45 consolidated subsidiaries at the end of the fiscal year, unchanged from a year earlier.

Sales and Income

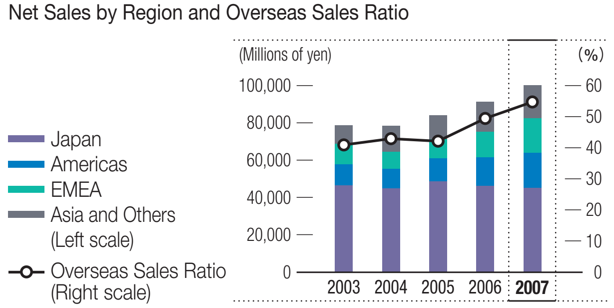
In the telecommunications and electronic equipment industries, competition in the market is increasing in terms of both function and price, but due to factors including an increase in exports and the effect of a weaker yen, sales were generally strong. In the Anritsu Group's core business field of measuring instruments for telecommunications, business opportunities are increasing overall, with a continuing trend toward worldwide expansion in mobile phone handset sales, base station installation and optical broadband access. In these conditions, the Anritsu Group formulated and is working aggressively to achieve its Mid-term Business Plan, Anritsu Global LP 2008, which ends on March 31, 2009.

As a result, net sales increased 9.0 percent compared with the previous fiscal year to ¥99,446 million. Sales increased substantially in the core Test and Measurement segment, centered on overseas operations. Sales also increased in the Services and Others segment. Operating income increased 39.8 percent compared with the previous fiscal year to ¥6,359 million. The Information and Communications segment returned to profitability after several years of operating losses, and operating income increased in the Services and Others segment. Net income increased a substantial 144.4 percent compared with the previous fiscal year to ¥1,376 million.

Net Sales

For the fiscal year ended March 31, 2007, net sales increased 9.0 percent, or ¥8,184 million, year-on-year to ¥99,446 million. Factors included a substantial increase of 11.9 percent in sales in the core Test and Measurement segment, centered on overseas sales, and the full-year contribution of consolidated subsidiary Anritsu A/S, which the Anritsu Group acquired in the previous fiscal year.

Net Sales by Region and Overseas Sales Ratio



Note: The former Europe segment has been changed to EMEA from the year ended March 31, 2007. In addition, Middle East and Africa, which had been part of the Asia and Others segment, are now included in the EMEA segment.

Overseas sales increased 20.6 percent compared with the previous fiscal year to ¥54,392 million. By region, sales in the Americas increased 23.4 percent compared with the previous fiscal year. Factors included substantial growth in orders in the Test and Measurement segment in the North American market for handheld measuring instruments for mobile base station installation and maintenance. In Europe, the Middle East and Africa (EMEA), sales increased 29.3 percent compared with the previous fiscal year due to factors including the inclusion of sales of Anritsu A/S. The ratio of overseas sales to net sales increased 5.3 percentage points year-on-year to 54.7 percent from 49.4 percent. Domestic sales decreased 2.4 percent compared with the previous fiscal year to ¥45,054 million due to factors including lower sales of measuring instruments for mobile communications as the third-generation investment cycle is coming to an end.

Cost of Sales and Gross Profit

Cost of sales increased 1.1 percent, or ¥582 million, compared with the previous fiscal year to ¥55,787 million. However, cost of sales decreased to 56.1 percent of net sales from 60.5 percent in the previous fiscal year as a result of the Anritsu Group's efforts to assiduously implement supply chain management (SCM) that continued from the previous fiscal year and programs to reduce expenses such as material costs and fixed costs. Gross profit increased 21.1 percent compared with the previous fiscal year to ¥43,659 million, and the ratio of gross profit to net sales increased 4.4 percentage points to 43.9 percent.

Selling, General and Administrative (SG&A) Expenses and Operating Income

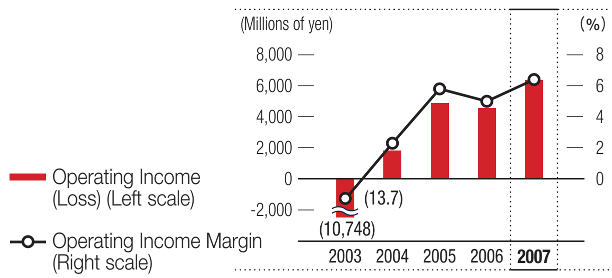
SG&A expenses increased 18.4 percent compared to the previous fiscal year to ¥37,300 million. Factors included increased expenses to enhance the Anritsu Group's overseas sales organization and expand sales, as well as the inclusion of full-year personnel and research and development expenses at subsidiary Anritsu A/S. Research and development expenses, which are included in cost of sales and SG&A expenses, increased 12.5 percent compared with the previous fiscal year to ¥14,072 million. The ratio of research and development expenses to net sales increased 0.5 percentage points to 14.2 percent.

Operating income increased 39.8 percent, or ¥1,810 million, year-on-year to ¥6,359 million. Factors included the return to profitability in the Information and Communications segment after several years of operating losses, and increased operating income in the Services and Others segment. The ratio of operating income to net sales increased 1.4 percentage points to 6.4 percent.

SG&A Expenses (Millions of yen)

	2007	2006	Change (%)
Salaries and Bonuses	**¥13,216**	¥11,441	**15.5%**
Advertising	**1,800**	1,844	**(2.4)**
Pensions	**775**	782	**(1.1)**
Travel and Transportation	**2,038**	1,752	**16.3**
Depreciation	**863**	626	**37.9**
Testing Research	**7,277**	5,603	**29.9**

Operating Income and Operating Income Margin



Other Income (Expenses), Income before Income Taxes, and Net Income

Other expenses, net totaled ¥3,258 million, compared to ¥2,521 million for the previous fiscal year. Factors included foreign exchange loss totaling ¥465 million, compared to a foreign exchange gain of ¥551 million for the previous fiscal year. Loss on devaluation of inventories, however, decreased ¥454 million compared with the previous fiscal year. Gain on sales of investment securities totaled ¥1 million, compared to ¥1,648 million for the previous fiscal year. The Anritsu Group also incurred a special allowance for retirement totaling ¥332 million as a result of integrating U.S. production operations into facilities in Japan and restructuring at Anritsu A/S. Moreover, loss on disposal of inventories totaled ¥542 million, compared to ¥55 million for the previous fiscal year. Restructuring expense totaling ¥1,032 million in the previous fiscal year for restructuring the Information and Communications segment did not recur.

As a result of the above, income before income taxes increased 53.0 percent, or ¥1,073 million, year-on-year to ¥3,101 million. Net income increased 144.4 percent, or ¥813 million, year-on-year to ¥1,376 million. Basic net income per share increased to ¥10.79 from ¥3.76 for the previous fiscal year.

Costs, Expenses and Income as a Percentage of Net Sales (%)

	2007	2006	2005
Net Sales	**100.0%**	100.0%	100.0%
Cost of Sales	**56.1**	60.5	63.9
Gross Profit	**43.9**	39.5	36.1
SG&A Expenses	**37.5**	34.5	30.4
Operating Income	**6.4**	5.0	5.8
R&D Expenses	**14.2**	13.7	12.5
Net Income	**1.4**	0.6	1.5

Shareholder Return Policies

Dividend Policy

Distributing returns to shareholders is one of Anritsu's management priorities. Based on consolidated net income, Anritsu distributes profits taking into account various factors, including the operating environment, the outlook for the coming fiscal year and the ratio of dividends to consolidated net assets.

Cash Dividends per Share

Based on the above policy, Anritsu maintained cash dividends at ¥7.00 per share for the fiscal year ended March 31, 2007, unchanged from the previous fiscal year. The Anritsu Group will use internal capital resources to make capital investments and conduct research and development to respond to rapid advances in technology and changes in market structure.

Business Segments

The Anritsu Group classifies operations into the segments of Test and Measurement, Information and Communications, Industrial Automation, and Services and Others.

Test and Measurement

During the year ended March 31, 2007, sales grew significantly in all regions due to factors including large-scale orders in the U.S. market for handheld measuring instruments for use in the installation and maintenance of base stations for mobile communications. Overseas, demand remained firm for measuring instruments for use in third-generation mobile communications services (3G) and 3.5G development, while in Japan demand began to show a recovery in the latter half of the fourth quarter.

Orders for newly launched measuring instruments for ultra-high-speed communications also expanded steadily. Moreover, making Anritsu A/S (formerly NetTest) a subsidiary upon its purchase in August 2005 increased revenue on a year-on-year basis with its inclusion in the scope of consolidation. As a result of these and other factors, segment sales increased 11.9 percent compared with the previous fiscal year to ¥72,883 million. Despite increased income from growth in sales of handheld measuring instruments and other products, a decrease in profits due to a delay in orders of the Service Assurance sub-segment resulted in a 10.8 percent decrease in operating income compared with the previous fiscal year to ¥4,718 million.

The Test and Measurement segment, which accounts for approximately 70 percent of the Anritsu Group's net sales, is divided into the following four sub-segments.

1) Wireless Test and Measurement

Wireless Test and Measurement includes measuring instruments for design, production, testing, and maintenance applications for telecom operators that provide mobile communications services and manufacturers of mobile phones, IC chipsets and other related electronic components and base stations.

Demand in this field tends to be influenced by technological innovations in mobile phone services, the degree of diffusion, and the number of new subscribers, new mobile phone models and mobile phones shipped, as well as network improvement plans including the installation of base stations. Among communications protocols, requirements for measuring instruments used to develop 3.5G mobile phones is expected to continue increasing. In Japan, 3G service development and investments in production have already peaked, but demand for a wide variety of wireless devices including Bluetooth® and WLAN is expected to rise. In Europe, the number of 3G service subscribers has begun to increase, and demand expanded for conformance testing, which is required to certify interconnection capability. In China, home of the largest number of subscribers in the world and the largest global production source for mobile phones, full-scale trials for commercialization have begun for the original TD-SCDMA standard, but price competition is intensifying. Throughout the world, demand expanded significantly for compact measuring instruments for base station installation and maintenance, a strong product area for Anritsu. However, investment trends for operators in the next fiscal year are uncertain.

Faced with these regional differences in investment trends and service development, Anritsu will continue making efficient investments in development to offer a broader lineup of products that accurately reflect changes in market and customer demands.

2) Optical, Digital and IP Test and Measurement

Optical, Digital and IP Test and Measurement includes measuring instruments for design, production, testing, maintenance and service quality assurance for applications of wireline network service providers and communications equipment manufacturers.

With the start of full-scale trials of next-generation networks (NGN) by major telecom operators in Japan, the United States and Europe, Anritsu was able to secure orders from large communications equipment vendors for measuring instruments for 40Gbit/s and other ultra-high-speed communications. In the future, Anritsu anticipates the production of devices for installing commercial networks and the establishment of a market for network maintenance.

Around the world, installation of fiber-optic cable is progressing for the shift to broadband by subscriber networks. The Anritsu Group's lineup of measuring instruments for construction and maintenance of optical digital network holds the top share of the global market, and plans to further expand this business in the future include launching new products developed jointly by business divisions in Japan and a team in the United States (from the former NetTest A/S Group).

3) General Purpose Test and Measurement

General Purpose Test and Measurement includes measuring instruments widely used in the electronics industry, particularly for design, production and evaluation of electronic devices used in telecommunications network-related communications equipment and other electronic equipment.

Sales in this sub-segment are strong in Japan as a result of expansion of electronic component production due to the spread of OneSeg broadcasting and advances in intelligent home appliances. Sales of handheld measuring instruments incorporating compact, high-density packaging and energy-saving technologies, an Anritsu strength, are also growing steadily around the world, including the United States.

The market for general purpose measuring instruments is expected to grow steadily in the future due to the increasing use of electronic components in automobiles as well as communications and advances in intelligent home appliances. Accordingly, Anritsu will work to further expand the business in this sub-segment by enhancing its lineup of network analyzers and spectrum analyzers.

4) Service Assurance

Based on a core of protocol analysis technologies for VoIP and mobile communications, the Service Assurance sub-segment provides major telecom operators and other customers in Europe and North America with solutions that improve network performance and service and enhance management and operating cost efficiency.

In the telecommunications service market, subscriber services such as triple play are becoming more diverse. At the same time, networks that formerly offered separate services are converging at an escalating rate. With the IP-based integration of wireline and wireless communication networks for the NGN era, service assurance to maintain and manage service quality has become a key issue for all telecom operators.

This sub-segment was added to the Anritsu Group as a result of the August 2005 acquisition and addition of the former NetTest A/S (now Anritsu A/S). In the year ended March 31, 2007, Anritsu worked to reinforce functions that satisfy customer demands and improve project management, based on a Tier 1 strategy targeting major telecom operators in each region. However, development and orders have been slower than expected, and the Anritsu Group is working to generate earnings from its initial investment.

In the year ending March 31, 2008, Anritsu intends to work for early achievement of operating profitability in this sub-segment by promoting its Tier 1 strategy, enhancing the competitiveness of MasterClaw network monitoring solutions, a core product line, and implementing management structure reforms including business process revisions and streamlining.

Information and Communications

In the year ended March 31, 2007, sales of the former business segment declined as a result of its divesture as a separate company and progress in selecting and concentrating businesses, including liquidation of unprofitable businesses. However, sales of new network bandwidth control equipment grew steadily as cooperation with system integrators and other factors increased market penetration. As a result, overall segment sales declined 17.0 percent to ¥6,011 million. Operating income was ¥146 million, compared to an operating loss of ¥1,972 million for the previous fiscal year. This return to profitability was the result of factors including reduction of fixed costs and other expenses due to streamlining.

The Information and Communications segment accounts for 6 percent of the Anritsu Group's net sales. It is easily influenced by the budgets of the national and local governments because a high proportion of its sales are for delivery to the government market. In addition, because they occur in synch with budget implementation periods, approximately 50 percent of sales tend to be concentrated in the fourth quarter.

In the government market, although overall spending for public works is declining, the amount spent for disaster prevention and IP infrastructure development is increasing and demand for public information systems is rising. In the video distribution market, demand has increased for bandwidth control equipment for maintaining Quality of Service (QoS). In the year ended March 31, 2007, the Information and Communications segment accurately responded to these business opportunities. Anritsu has successfully rebuilt the business, which had been unprofitable for many years. It achieved operating profitability as planned at the start of the fiscal year through divestiture and reestablishment as a separate company and the implementation of business selection and concentration.

Looking forward, the Anritsu Group will fortify its profit structure by providing high-quality solutions based on its IP network technologies, an area of strength, while promoting its model of business cooperation with system integrators.

The Information and Communication business is conducted as Anritsu Networks Co., Ltd., a wholly owned subsidiary of the Company.

Industrial Automation

Orders were weak in the first half as a result of constraints on capital investment in inspection equipment in the food products industry due to increased packaging and distribution costs caused by the rise in crude oil prices. However, due to the effect of subsequent investment in X-ray inspection equipment with significantly enhanced functions compared with existing systems, increased inclination among food manufacturers to make capital investments, growth in imports and other factors, sales were ¥12,295 million, a slight increase of 0.8 percent compared with the previous fiscal year. However, as a result of a worsening product cost ratio caused by the high price of metals used as raw materials, operating income decreased 22.7 percent compared with the previous fiscal year to ¥608 million.

The Industrial Automation business accounts for 12 percent of the Anritsu Group's net sales. Since more than 80 percent of segment sales are made to food manufacturers, this segment is influenced by the effect that the economic growth rate and changes in consumer spending levels have on food manufacturers. Its core products, metal detectors and X-ray inspection systems, have achieved the leading share in the market for inspection systems due to their high speed and high precision in detecting metal fragments and other alien materials in the food processing process. Promoting investment aimed at expanding market share in Asia, the United States and Europe resulted in an increase in the overseas sales ratio to about 25 percent.

Inquiries about the Anritsu Group's quality control inspection systems have been increasing because of food safety and security incidents in Japan and overseas. At the same time, Anritsu is working to strengthen the price competitiveness of this business segment by sharing and standardizing basic units and reducing costs to deal with intensifying competition caused by rising metal raw material costs, new market entrants and other factors.

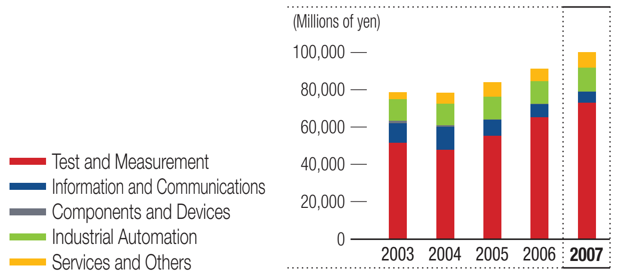
The Industrial Automation business is conducted as Anritsu Industrial Solutions Co., Ltd., a wholly owned subsidiary of the Company.

Services and Others

This segment comprises devices, precision measurement, environmental, logistics, welfare services, real estate leasing and other businesses.

In the year ended March 31, 2007, sales increased 23.0 percent compared with the previous fiscal year to ¥8,257 million and operating income increased 47.3 percent year-on-year to ¥2,634 million, due to stronger year-on-year performance of the devices business, including devices for optical communications equipment, as well as the solid performance of sensors used in manufacturing devices for flat panel displays and 3D solder paste inspectors in the precision measuring instruments business, supported by increased capital investment in the intelligent home appliance industry.

Sales by Business Segment



Note: From the year ended March 31, 2005, "Components and Devices" is included as part of "Services and Others."

Geographical Segments

Japan

In the domestic test and measurement business, base station installation and maintenance resulting from the implementation of phone number portability generated demand for measuring instruments for mobile communications. However, overall sales were flat because investment in 3G neared the end of its cycle and investment in 3.5G was not as strong as expected. Overseas demand was robust, centered on measuring instruments used for development of 3.5 G (HSDPA and HSUPA). Moreover, construction of the infrastructure for NGN has begun, which supported a steady increase in sales of measuring instruments for core networks and fiber-optic networks, including measuring instruments for testing devices and equipment and for use in the field. In the information and communications business, competition continued to intensify in the government market for public information systems. However, the Anritsu Group has improved earnings in the government market by restructuring this business, which along with strong product sales to the private sector has resulted in a return to profitability in this business. In the services and others business, the other devices and precision measurement businesses essentially performed according to plan.

As a result, sales in Japan decreased 0.9 percent year-on-year to ¥49,903 million, and operating income increased 39.4 percent year-on-year to ¥5,163 million.

Americas

Sales in the Test and Measurement segment increased significantly due to factors including large orders in the North American market for handheld measuring instruments for installation and maintenance of base stations for mobile communications. Demand in Asia and other regions supported steady growth in sales of handheld measuring instruments used for installation and maintenance of wireless infrastructure such as base stations. Moreover, government demand for general purpose measuring instruments was strong in North America, and sales of measuring instruments for wireless applications such as Bluetooth® and wireless local area networks (LAN) were solid.

As a result, sales in the Americas increased 19.4 percent year-on-year to ¥20,646 million, and operating income increased 86.2 percent year-on-year to ¥4,073 million.

Europe

In the Test and Measurement segment, demand was firm for measuring instruments used for conformance test systems for 3G handsets and for 3.5G development. The Anritsu Group entered the service assurance business in the second half of the previous fiscal year, but is not yet generating earnings because of proactive investments to further strengthen the operating foundation of this business in addition to delays in process integration and in orders from the target customer group of major telecom operators. As a result, while sales in Europe increased 26.7 percent year-on-year to ¥17,839 million, operating loss increased substantially to ¥3,005 million from ¥2,001 million for the previous fiscal year.

Asia and Others

In the Test and Measurement segment, demand recovered for measuring instruments for mobile communications used in mass-production of second-generation (2G) handsets and of 3G handsets for the European and North American markets. Demand remained solid for handheld measuring instruments for construction and maintenance of wireless infrastructure such as base stations. Moreover, demand was firm for measuring instruments used in the construction and maintenance of fiber-optic networks. In the industrial automation business, demand was strong in Southeast Asia for specialized checkweighers.

As a result, sales increased 16.1 percent year-on-year to ¥11,058 million, and operating income increased 32.3 percent year-on-year to ¥574 million.

Liquidity and Financial Condition

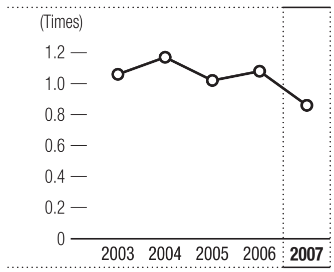
Fund Procurement and Liquidity Management

The Anritsu Group's capital requirements consist primarily of working capital for purchases of materials and other operating expenses incurred in manufacturing and selling products, and funds for capital investment and research and development expenditures. Anritsu supplements internal capital resources by directly and indirectly procuring funds from external sources to secure sufficient liquidity. Moreover, in March 2005 the Anritsu Group secured stable financing by establishing a committed ¥15,000 million line of credit effective until March 2008. Looking forward, while preparing for unforeseeable financial conditions in a dramatically changing market environment in Japan and overseas, the Anritsu Group will swiftly and flexibly meet its capital requirements for working capital, regular repayment of long-term borrowings and business growth.

In the year ended March 31, 2007, Anritsu proactively reduced interest-bearing debt amid rising market rates in Japan and overseas. As a result, the balance of interest-bearing debt decreased ¥12,556 million from a year earlier to ¥53,033 million. The net debt-to-equity ratio[7] was 0.54 times, compared with 0.57 times at the previous fiscal year-end. The debt-to-equity ratio[8] was 0.86 times, compared with 1.08 times at the previous fiscal year-end. The Company will use increased cash flow generated by improvements in Anritsu Capital-cost Evaluation (ACE)[9] and asset turnover as well as enhanced capital efficiency resulting from measures including an internal Group cash management system to make further reductions in interest-bearing debt, improve the net debt-to-equity ratio, enhance net assets and fortify its financial structure. At the end of March 2007, Rating and Investment Information, Inc. rated Anritsu's short-term debt a-2, and its long-term debt BBB. The Company's long-term rating was lowered from A- to BBB in December 2002, but this has not had any material effect on fund procurement. To restore its A- rating, Anritsu will continue taking measures to improve its financial stability.

(Note 7): Net debt-to-equity ratio: (Interest-bearing debt – Cash and cash equivalents)/Net assets
(Note 8): Debt-to-equity ratio: Interest-bearing debt/Net assets
(Note 9): Anritsu Capital-cost Evaluation (ACE): Net operating income after tax less a charge for the cost of capital

Debt-to-Equity Ratio



Cash Flow

Cash and cash equivalents as of March 31, 2007 decreased ¥10,923 million from the end of the previous fiscal year to ¥19,947 million. Main factors included a decrease in interest-bearing debt due to the redemption at maturity of convertible bonds.

Free cash flow, the sum of cash flows from operating activities and cash flows from investing activities, was positive ¥2,908 million, compared with negative ¥5,016 million in the previous fiscal year.

Net cash provided by operating activities totaled ¥2,488 million, compared with ¥5,929 million in the previous fiscal year. Main factors were increases in orders and sales and an increase in inventories associated with the launch of new products. In addition, income taxes payable increased as a result of the strong performance of U.S. subsidiaries. Depreciation and amortization was ¥3,670 million, an increase of ¥40 million compared with the previous fiscal year.

Net cash provided by investing activities was ¥420 million. In the previous fiscal year, investing activities used net cash of ¥10,945 million. This year-on-year change primarily reflected the absence of payments for acquisition of newly consolidated subsidiaries in the previous fiscal year in connection with the acquisition of Anritsu A/S. Acquisition of property, plant and equipment totaled ¥2,219 million, a decrease of ¥229 million compared with the previous fiscal year.

Net cash used in financing activities was ¥13,975 million. In the previous fiscal year, financing activities provided net cash of ¥1,761 million. This was mainly the result of the redemption at maturity of the fourth series of unsecured convertible bonds totaling ¥14,793 million and progress by overseas subsidiaries in repaying borrowings from local banks. Factors providing cash included the procurement of ¥7,000 million through long-term borrowings to prepare for the repayment of a syndicated loan that matured in April 2007.

Assets, Liabilities and Net Assets

As of March 31, 2007, total assets decreased 7.9 percent, or ¥11,964 million, from a year earlier to ¥140,395 million. Current assets decreased 11.1 percent, or ¥10,666 million, from a year earlier to ¥85,392 million. Primary factors included a decrease of ¥5,224 million in cash and a decrease of ¥6,604 million in marketable securities.

The inventory turnover ratio improved to 3.9 times from 3.7 times for the previous fiscal year. One of the Anritsu Group's objectives is to increase the inventory turnover ratio to 5.0 times.

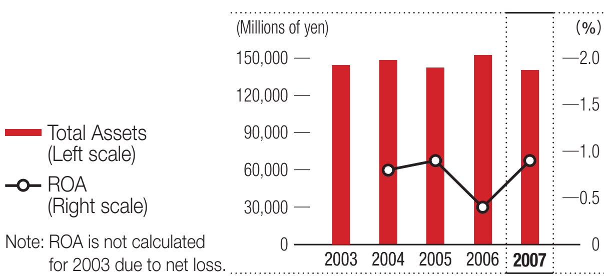
Property, plant and equipment net of accumulated depreciation decreased 4.1 percent, or ¥1,008 million, from a year earlier to ¥23,459 million. Investments and other assets were essentially unchanged.

As of March 31, 2007, total liabilities decreased 13.8 percent, or ¥12,643 million, from a year earlier to ¥78,776 million. Current liabilities increased ¥3,110 million from a year earlier to ¥51,086 million. Short-term borrowings decreased 17.6 percent from a year earlier to ¥6,582 million, and long-term debt due within one year decreased 59.8 percent from a year earlier to ¥7,000 million. The current portion of bonds totaled ¥15,000 million, and was the primary factor in the increase in current liabilities from a year earlier. The current ratio was 167.2 percent, compared to 200.2 percent a year earlier.

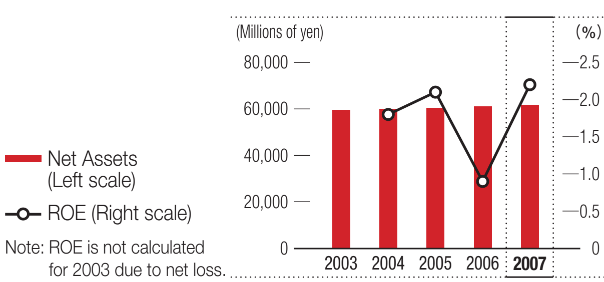
Long-term debt decreased ¥15,756 million from a year earlier to ¥24,451 million as ¥15,000 million in bonds pending repayment shifted from long-term debt to long-term debt due within one year. Total interest-bearing debt decreased ¥12,556 million from a year earlier to ¥53,033 million. Working capital totaled ¥34,306 million as of March 31, 2007, compared to ¥48,082 million a year earlier.

Net assets increased ¥679 million from a year earlier to ¥61,619 million. The ratio of net assets to total assets was 43.9 percent, compared to 40.0 percent a year earlier.

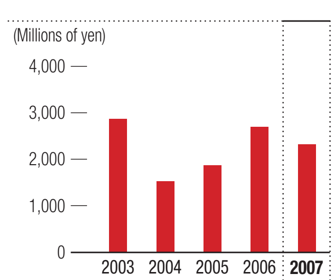
Total Assets and ROA



Net Assets and ROE



Capital Expenditures



Capital Expenditures

For the fiscal year ended March 31, 2007, capital expenditures decreased 14.1 percent compared with the previous fiscal year to ¥2,319 million. The Anritsu Group is concentrating resources in fields related to the ongoing evolution of communication network quality and high performance, including expansion of triple play services, the integration of wireline and wireless communication networks, and the development of next-generation networks. During the year ended March 31, 2007, the Anritsu Group concentrated capital expenditures in the core Test and Measurement segment with the primary objectives of enhancing its research and development environment and improving its business processes to support its strategies for profitable growth.

Overview of Capital Expenditures (Millions of yen)

	2007	Change (%)
Test and Measurement	¥1,700	(10.0)%
Information and Communications	118	(51.0)
Industrial Automation	167	16.0
Services and Others	279	(28.1)
Sub-total	2,264	(15.0)
Eliminations or corporate	55	48.6
Total	¥2,319	(14.1)%

Research and Development

The Anritsu Group conducts research and development under the Group corporate philosophy of developing “Original & High Level” products that contribute to the realization of an affluent ubiquitous network society. The Anritsu Group is promoting new product research and development with a focus on leading-edge technology fields including IP networks and mobile communication systems.

An overview of research and development expenditures in the year ended March 31, 2007 follows below.

(Millions of yen)

	2007	Ratio to Segment Sales (%)
Test and Measurement	¥10,574	14.5%
Information and Communications	204	3.4
Industrial Automation	1,057	8.6
Services and Others	398	4.8
Basic Research	1,839	—
Total	¥14,072	14.2%

Note: The “Total” line shows the ratio to net sales.

The results of research and development in each business segment are outlined below.

1. Test and Measurement

1) Enhanced Functions for the MD1230B Data Quality Analyzer: Development of the MU120131A & MU120132A

The volume of data that networks handle has increased dramatically with the spread of high-speed Internet and rich content encompassing video and voice data. Communication infrastructure systems such as fiber-to-the-home (FTTH) are changing from broadband passive optical network (B-PON) systems that employ 10/100Mbit/s Ethernet to Ethernet passive optical network (E-PON) systems for 1Gbit/s Ethernet. Anritsu has developed new modules for the MD1230B data quality analyzer and is delivering more efficient E-PON evaluation solutions and low-cost multiport equipment test solutions.

2) Development of the MT9082A & MT9083A Access Master

Anritsu has been providing compact, multifunctional Access Master products to handle fiber-optic-cable installation and maintenance needs brought on by the full-scale advent of FTTH. Anritsu has developed and launched the MT9082A to meet market needs for enhanced functionality, and the MT9083A, which meets North American operability requirements.

3) Development of the Mobile WiMAX IQproducer Software for the MG3700A Vector Signal Generator

Anritsu has developed MX370105A Mobile WiMAX IQproducer PC software for use with the MG3700A vector signal generator. It allows parameters to be set to generate wave form patterns that conform with the specifications for Mobile WiMAX, a next-generation communication protocol now gaining attention. This software offers superb flexibility in allocating Mobile WiMAX resources and is easy to operate. Moreover, it contributes to improved development efficiency because it also enables multiple input, multiple output (MIMO) wave form pattern generation for evaluating MIMO downlink signal reception (base station to handset signal transmission).

2. Information and Communications
Development of Monitoring Manager and Config Manager for PureFlow® GS1

The PureFlow® GS1 series of traffic shapers is an original Anritsu lineup of bandwidth controllers featuring a high-precision bandwidth control engine and a flexible packet grouping function. The demand for the PureFlow® GS1 series has increased primarily in the enterprise market among companies in businesses including finance, manufacturing and logistics, driven by the recent shift to broadband and more sophisticated network use. Amid this rising demand, the use of PureFlow® GS1 to control bandwidth at a single center is evolving into its use as a bandwidth controller at all bases throughout the network. Anritsu has responded by developing Monitoring Manager and Config Manager for PureFlow® GS1 as integrated trend analysis and management solutions.

3. Industrial Automation
Development of Large-scale Metal Detector

Concern about food safety has increased, and quality control is becoming even more stringent in food production processes. The scope of application of alien material inspection has therefore expanded from post-packaging shipping processes to encompass raw material processing. The of large-scale metal detectors offers a significantly higher level of metal detection sensitivity by using Anritsu's original simultaneous dual-frequency magnetic field detection method and. Offering easy on-site operation and a full lineup of enhanced support functions, the Super Mepoli III DUW series contributes to improved quality inspection during raw material processing.

Management Objectives and Indicators

Anritsu aims to maximize corporate value by managing its operations with a focus on consolidated cash flow. In addition, Anritsu uses an original metric, ACE (Anritsu Capital-cost Evaluation), to evaluate the results of each business to analyze the added value generated by capital invested.

During the year ended March 31, 2007, Anritsu deployed capital in areas such as new product development related to NGN, including service assurance. Consolidated ACE was negative ¥1,397 million, compared to negative ¥3,121 million for the previous fiscal year. Consolidated ROE was 2.2 percent, compared to 0.9 percent for the previous fiscal year. Consolidated free cash flow was ¥2,908 million, compared to negative ¥5,016 million for the previous fiscal year.

By the year ending March 31, 2009, Anritsu aims to be a high earnings-oriented company, with consolidated ACE of ¥5 billion and a consolidated operating margin of 10 percent or higher.

Outlook and Management Issues for the Year Ending March 31, 2008

In the fiscal year ending March 31, 2008, the global economy is expected to remain firm, but matters such as the instability indicated by the interlinked worldwide drop in stock prices, slowing growth of corporate profits in the United States and worsening business confidence in Japan will require attention. While dealing with these conditions, the Anritsu Group will deploy its next set of measures toward achieving the Mid-Term Business Plan.

In the Test and Measurement segment, Anritsu will actively invest in research and development and reorganize businesses in anticipation of the integration of wireline and wireless networks with the advent of the NGN era. Toward that end, Anritsu will work to generate synergy between the Service Assurance sub-segment and other sub-segments in the Test and Measurement segment while reforming the management structure to improve profitability. In sales, Anritsu will continue its efforts from the previous fiscal year to expand sales channels and introduce a new system for back-office functions. In addition, Anritsu will work to get closer to customers by sharing development road maps with key customers in order to promote the launch of new products that match market needs.

In the Information and Communications segment, Anritsu will aggressively cultivate private-sector markets by boosting the competitiveness of its IP network solutions and strengthening relationships with system integrators. In addition, it will work to fortify its management foundation.

In the Industrial Automation segment, Anritsu aims to expand by promoting a product strategy of higher added value and differentiation while aggressively expanding into overseas markets.

Steady implementation of these strategies requires appropriately managing and reducing risks and transforming them from impediments into a source of competitive advantage. For this reason, Anritsu will strive to achieve its management targets by making ongoing improvements to the risk management system that incorporate upgrades to the internal control system, which the Anritsu Group is currently devoted to promoting.

The Anritsu Group believes that honest business practices enhance corporate value, and will continue to actively conduct corporate social responsibility (CSR) activities. Anritsu intends to go beyond what it considers to be its primary CSR activity – contributing to the realization of a safe, secure, and comfortable society through its products and services – to review the activities of the entire Group in all areas of corporate social responsibility, including compliance, corporate governance, the environment, human rights and risk management. Doing so will lead to further improvement of the Group's management infrastructure.

Based on the above, as of April 25, 2007, for the year ending March 31, 2008 Anritsu projects that net sales will increase 4.1 percent year-on-year to ¥103,500 million, operating income will increase 10.1 percent year-on-year to ¥7,000 million, and net income will increase 81.7 percent year-on-year to ¥2,500 million.

Risk Information

The following are among the operational and management issues presented in this annual report that have the potential to materially affect investor decisions. Forward-looking statements reflect the Anritsu Group's judgment as of March 31, 2007.

Risk Associated with the Anritsu Group's Technology and Marketing Strategy

The Anritsu Group works to deploy its well-developed technological capabilities to provide products and services that offer value to customers. However, the rapid pace of technological innovation in the Anritsu Group's core information and communication markets and the Anritsu Group's ability to deliver products and services in a timely manner to meet the needs and wants of customers are factors that have the potential to exert a material impact on the Anritsu Group's results.

Amid advances in mobile phone and internet protocol (IP) technologies, an especially important point is the ability to provide customers with timely solutions based on an accurate understanding of trends in service and research and development investment for triple play services incorporating voice, video and Internet, as well as Fixed Mobile Convergence (FMC) and NGN.

Market Fluctuation Risk

External factors including changes in economic and market conditions and technological innovation have the potential to exert a material impact on the Anritsu Group's product lines and performance.

In the Test and Measurement segment, economic conditions and consumption trends in countries worldwide influence changes in capital investment among telecom operators, telecommunications equipment manufacturers and electronic component manufacturers. In addition, the increasing sophistication and complexity of telecommunications services represented by triple play services, FMC and NGN are accelerating integration and reorganization in the telecommunications industry, which is lending uncertainty to investment trends. Moreover, demand for mobile communications measuring instruments, the cornerstone of earnings for the Anritsu Group, is affected by such factors as the number of subscribers, rate of adoption of and technological innovation in mobile phone services, and earnings are also affected by the Company's response to factors such as changes in the food chain, as seen in areas such as System on Chip for mobile phones, and intensified price competition for measuring instruments for commercial scale production of mobile phones.

The Information and Communications segment has a high proportion of sales to government entities, and the scale and status of implementation of government and municipal budgets for disaster prevention and IP networks may exert a material impact on its performance.

In the Industrial Automation business, sales to food manufacturers constitute 80 percent of sales. Economic growth rates, consumer spending and raw material price trends have the potential to impact performance, capital investment and other issues among food manufacturers and materially influence Anritsu's results.

Global Business Development Risks

The Anritsu Group markets its products globally, and conducts business in the Americas, Europe, Asia and elsewhere. In particular, the overseas sales ratio for the Test and Measurement segment is 68 percent, and many customers likewise operate on a global scale. As a result, economic trends in countries worldwide, international conditions and progress in the Anritsu Group's global strategy have the potential to exert a material impact on earnings. Of particular importance is the expected increase in mergers and acquisitions among operators and telecommunications equipment manufacturers doing business globally amid the worldwide acceleration of the integration of information and communications and of FMC. Significant changes in capital investment resulting from this trend have the potential to exert a material impact on the Anritsu Group's operating results.

Foreign Exchange Risk

The Anritsu Group's sales outside Japan account for 54.7 percent of consolidated net sales. The Anritsu Group hedges foreign exchange risk using instruments including forward foreign exchange contracts for foreign currency transactions that occur upon collection of accounts receivable and other events. However, rapid changes in foreign exchange rates have the potential to exert a material impact on the Anritsu Group's performance.

Long-term Inventory Obsolescence Risk

The Anritsu Group works to provide products and services that precisely meet customer needs and wants. However, particularly in the test and measuring instruments market, product lines are subject to rapid change in technology, which can easily render products and parts obsolete, and cause inventory held for long periods to lose its value. These factors have the potential to exert a material impact on the Anritsu Group's financial condition.

Risk of Loss from Goodwill

As of March 31, 2007, the Anritsu Group recorded ¥14,651 million in goodwill resulting from the acquisition of an overseas company for the purpose of expanding the territory of the Test and Measurement segment. The impact on earnings of the Test and Measurement segment from changes in the global economy and markets, intensifying competition and other factors has the potential to cause the Group to recognize a loss from goodwill.