Management's Discussion and Analysis

Changes in the Scope of Consolidation

During the fiscal year ended March 31, 2008, the Anritsu Group liquidated two subsidiaries, NetTest do Mexico C.V. de SA and NetTest Co., Ltd. As a result, the Anritsu Group comprised 43 consolidated subsidiaries at the end of the fiscal year, down from 45 a year earlier.

Sales and Income

During the fiscal year ended March 31, 2008, in the information and communications network industry, both wireline and mobile communications moved toward broadband. Along with the development of a wide array of services that use broadband, various efforts to construct next-generation networks (NGN) accelerated worldwide. On the other hand, competition has intensified in this sector, resulting in business restructurings and mergers that have made customer trends harder to identify. Amid these conditions, the Anritsu Group worked to introduce new solutions and enhance its product lineup, as well as to strengthen its sales and customer support networks in each region. In addition, amid a marked trend among customers to restrain capital investments at the start of 2008, the Anritsu Group restructured its strategy for profitable growth and announced Management Innovation 2008, its plan to increase competitiveness and profitability in the fiscal year ending March 31, 2009 and beyond. The Anritsu Group decided to begin undertaking this plan by March 31, 2008, and has been shaping and executing concrete measures, including eliminating unprofitable products and reforming inefficient divisions.

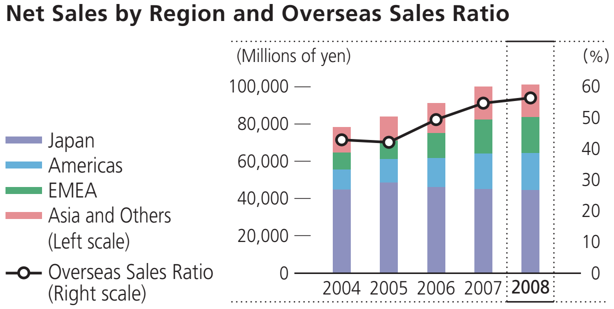
As a result, for the fiscal year ended March 31, 2008, net sales increased 1.0 percent year on year to ¥100,486 million. Operating income decreased 15.8 percent year on year to ¥5,356 million because of reduced profitability in every business segment except Industrial Automation. Moreover, as one result of Management Innovation 2008, loss on valuation of inventories and loss on disposal of inventories in other expenses increased substantially, and Anritsu also incurred restructuring expense in other expenses. Consequently, net loss for the year ended March 31, 2008 totaled ¥3,900 million.

Net Sales

For the fiscal year ended March 31, 2008, net sales increased 1.0 percent, or ¥1,040 million, year on year to ¥100,486 million. The Industrial Automation business segment performed strongly against a backdrop of increasing needs for food safety and security. Sales weakened in the core Test and Measurement business segment. Sales were brisk in the Service Assurance business in Europe, the Middle East and Africa (EMEA). However, in other Test and Measurement businesses, sales of new products were below forecast, particularly with the sharp appreciation of the yen in the second half of the fiscal year and rapidly increasing restraint in capital investment.

On a regional basis, sales increased 2.8 percent year on year in the Americas because of solid performance in the Test and Measurement business segment. In EMEA, Anritsu continued to execute the Tier I strategy initiated in the previous fiscal year, and sales increased 4.6 percent year on year. Overall, overseas sales increased 3.3 percent year on year to ¥56,205 million, and the ratio of overseas sales to net sales increased 1.2 percentage points to 55.9 percent from 54.7 percent. This ratio also increased in part because sales in Japan decreased 1.7 percent year on year to ¥44,281 million. Among various factors, while sales were firm in the Industrial Automation business segment centered on X-ray inspection systems, the demand cycle for highly profitable measuring instruments for use in developing mobile phones came to an end.

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.

Cost of Sales and Gross Profit

Cost of sales increased 1.2 percent, or ¥687 million, compared with the previous fiscal year to ¥56,474 million, and cost of sales increased to 56.2 percent of net sales from 56.1 percent in the previous fiscal year. Customer restraint in capital investment and the sharp appreciation of the yen in the second half of the fiscal year strongly impacted cost of sales. However, Anritsu continued to reduce material costs and also reduced the research and development expenses that are included in cost of sales, with the result that cost reductions exceeded projections. Gross profit increased 0.8 percent, or ¥353 million, compared with the previous fiscal year to ¥44,012 million, and the ratio of gross profit to net sales decreased 0.1 percentage points to 43.8 percent.

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

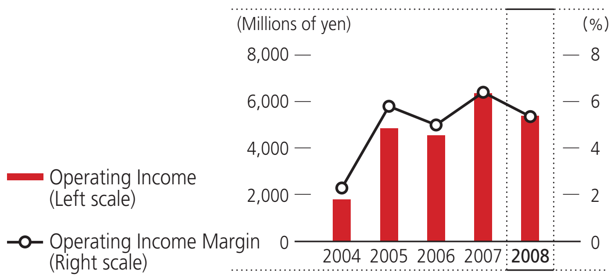
SG&A expenses increased 3.6 percent year on year to ¥38,656 million. Factors included increased personnel expenses due to expansion of the Anritsu Group's overseas sales network, and an increase in pension expenses. Research and development expenses, which are included in cost of sales and SG&A expenses, increased 0.3 percent compared with the previous fiscal year to ¥14,115 million. The ratio of research and development expenses to net sales decreased 0.2 percentage points to 14.0 percent.

As a result of the above, operating income decreased 15.8 percent, or ¥1,003 million, year on year to ¥5,356 million. The ratio of operating income to net sales decreased 1.1 percentage points to 5.3 percent.

SG&A Expenses (Millions of yen)

	2008	2007	Change (%)
Salaries and Bonuses	¥14,277	¥13,216	8.0%
Pensions	1,083	775	39.8
Advertising	2,003	1,800	11.2
Travel and Transportation	2,135	2,038	4.7
Depreciation	1,002	863	16.1
Testing Research	7,444	7,277	2.3

Operating Income and Operating Income Margin



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

Other expenses, net totaled ¥8,513 million, compared to ¥3,258 million for the previous fiscal year. Factors included efforts under Management Innovation 2008 to improve profitability and inventory turnover by eliminating low-profit products. As a result, loss on devaluation of inventories totaled ¥3,221 million, an increase of ¥2,109 million compared with the previous fiscal year. Moreover, loss on disposal of inventories totaled ¥2,247 million, compared to ¥542 million for the previous fiscal year. The Anritsu Group also incurred restructuring expense totaling ¥1,156 million.

As a result of the above, loss before income taxes totaled ¥3,157 million, compared with income before income taxes of ¥3,101 million for the previous fiscal year. Net loss totaled ¥3,901 million, compared with net income of ¥1,376 million for the previous fiscal year. Net loss per share totaled ¥30.60, compared with basic net income per share of ¥10.79 for the previous fiscal year.

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

	2008	2007	2006
Net Sales	100.0%	100.0%	100.0%
Cost of Sales	56.2	56.1	60.5
Gross Profit	43.8	43.9	39.5
SG&A Expenses	38.5	37.5	34.5
R&D Expenses	14.0	14.2	13.7
Net Income	—	1.4	0.6

Shareholder Return Policies

Dividend Policy

Anritsu considers the return of profits to shareholders a management priority. Its basic policy for paying dividends from surplus funds is to increase the ratio of dividends on consolidated equity (DOE) to reflect the level of income during the consolidated period while taking into general account factors such as the operating environment and the outlook for results in the current fiscal year and beyond.

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, 2008, unchanged from the previous fiscal year despite the net loss, to reward shareholders for their continuing support. 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, 2008, segment sales increased substantially as the Anritsu Group continued to execute the Tier 1 strategy initiated in the previous fiscal year in the Service Assurance business, and received orders from leading telecom operators.

In the category of measuring instruments for third generation mobile communications (3G) and 3.5G services, demand was firm for use in mobile handset manufacturing, centered on Japan and Asia, and for handheld products for use in base station installation and maintenance primarily in the United States. However, sales declined overall as demand for use in research and development in Japan and Europe subsided. In addition, NGN-related business and general purpose measuring instruments did not contribute to sales as expected due to the time needed to launch new products and customer restraint in capital investment.

As a result, segment sales decreased 0.2 percent year on year to ¥72,718 million. Operating income decreased 12.5 percent to ¥4,126 million. While income in the Service Assurance business improved, segment operating income was impacted by delays in sales from new products expected to cover decreased profitability from measuring instruments for mobile handsets and the sharp appreciation of the yen.

The Test and Measurement segment, which accounts for approximately 70 percent of the Anritsu Group's net sales, was divided into four sub-segments through the year ended March 31, 2007: Wireless Test and Measurement; Optical, Digital and IP Test and Measurement; General Purpose Test and Measurement; and Service Assurance. Under Management Innovation 2008, however, the Anritsu Group now divides the Test and Measurement segment into three sub-segments: NGN and Infrastructure; Mobile Handset; and General Purpose.

1. NGN and Infrastructure

The NGN and Infrastructure sub-segment includes network construction, maintenance, monitoring and service quality assurance solutions for wireline and wireless service providers, and solutions for communication equipment manufacturers in areas including design, production and testing.

With the proliferation of broadband network services, new services are appearing not only for consumers, such as music and video downloading, IPTV, and social networking services (SNS), but also for enterprise applications. New markets are expanding due to the integration of wireline and wireless communications, as demand for high-speed data transfer rises with increasing data traffic. In addition, with the start of full-scale construction of 40Gbps ultra-high-speed networks and research and development for 100Gbps backbone network equipment, demand for related measuring equipment is expected to increase. Establishment of IP-based NGN is progressing worldwide, and Anritsu anticipates demand for related measuring equipment due to the growth of this market.

On the other hand, technological innovations such as these are prompting mergers and acquisitions between telecom operators, and lending uncertainty to investment trends, including scale and timing. In this environment, Anritsu will work to enhance its lineup of solutions to match the changing needs of major customers while carrying out efficient investment in development.

2. Mobile Handset

The Mobile Handset sub-segment includes measuring instruments for mobile phone acceptance testing by mobile phone service operators, and for design, production, function and performance verification, and maintenance of mobile handsets by manufacturers of mobile phones, IC chipsets and relevant components.

Demand in this sub-segment tends to be influenced by factors including technological innovations in mobile phone services, the degree of diffusion, and the number of new subscribers, new mobile phone models and mobile phones shipped. The number of mobile phone subscriber contracts in Japan was over 100 million at the end of December 2007. With a nearly 100 percent penetration rate, the market is essentially saturated. Moreover, a longer mobile phone replacement cycle is forecast for the Japanese market because service providers have been phasing out the use of mobile phones as a promotional incentive in revising rate plans since fall 2007. On the other hand, demand for mobile handsets is expected to continue growing worldwide as the number of subscribers in China, India and other markets continues to expand strongly.

Full-scale development is expected to begin for handsets supporting Long-Term Evolution (LTE), the 3.9 generation (3.9G) technology, as the current 3.5G technology has almost completely matured. A decrease in the number of customers due to mergers and acquisitions among handset manufacturers has intensified competition and increased pressure on prices. Based on these factors, Anritsu will focus development investment on measuring instruments for LTE handset development in order to meet cutting-edge needs in this area, and develop competitive products to serve the demand for measuring equipment used in LTE handset production that is expected to follow.

3. General Purpose

The General Purpose sub-segment 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.

Demand in this sub-segment is expected to grow steadily due to the increasing use of electronic components in automobiles as well as communications 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 in the United States and other parts of the world. Anritsu will offer a wider range of applications for these markets, and work to further expand business in this sub-segment by enhancing its lineup of network analyzers, spectrum analyzers, signal generators and products that incorporate several of these functions.

Information and Communications

During the fiscal year ended March 31, 2008, customers made conspicuous revisions to their capital investment plans, centered on public information systems. Private-sector sales of bandwidth control equipment weakened despite cooperation with system integrators and other approaches, and segment sales decreased 4.4 percent year on year to ¥5,749 million. Segment operating income decreased 47.5 percent year on year to ¥76 million. The Anritsu Group reduced costs for existing products, but made proactive investments to develop disaster mitigation solutions and build other new businesses.

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 of the connection with customers’ budget implementation periods, approximately 50 percent of sales tend to be concentrated in the fourth quarter.

In the government market, although investment related to disaster prevention and IP infrastructure development is increasing, overall spending for public works projects continues to decline. In the private-sector market, demand is increasing for bandwidth control equipment for maintaining quality of service (QoS) of growing traffic resulting from expansion of video distribution and other services.

Looking forward, the Anritsu Group will expand revenues in the private-sector market and improve profitability 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

During the year ended March 31, 2008, heightened concerns about food safety and security resulted in a sharp increase in demand for food inspection equipment, and domestic and overseas sales of X-ray inspection systems were strong. Overseas, sales of automatic checkweighers were robust. As a result, segment sales increased 10.6 percent year on year to ¥13,596 million. Segment operating income increased 34.0 percent year on year to ¥815 million because of increased sales and efforts to counter the sharp rise in the price of metal raw materials.

The Industrial Automation segment accounts for 14 percent of the Anritsu Group’s net sales. Since approximately 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 precision in detecting metal fragments and other alien materials in the food processing process. Investment to expand market share in Asia, the United States and Europe resulted in an overseas sales ratio of approximately 30 percent.

Inquiries about the Anritsu Group’s quality control inspection solutions, especially from the Americas and Europe, are on the increase following food safety and security incidents in Japan and other countries. At the same time, in addition to the rise in the procurement cost of metals used as raw materials, the Group must deal with new concerns including restrained capital investment by domestic food manufacturers due to the rising cost of flour and other food raw materials and packaging materials. To address these factors, Anritsu will begin overseas production aimed at lowering production and distribution costs, and continue working to strengthen the price competitiveness of this business segment by commoditizing and standardizing basic units and reducing costs. 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, 2008, segment sales increased 2.0 percent compared with the previous fiscal year to ¥8,423 million and segment operating income decreased 26.9 percent year on year to ¥1,926 million. Demand for optical communications devices waned in the video distribution market, but sales of low-cost existing products for metro networks increased. Other factors included expenses associated with efforts to improve quality control in the precision measuring instruments business.

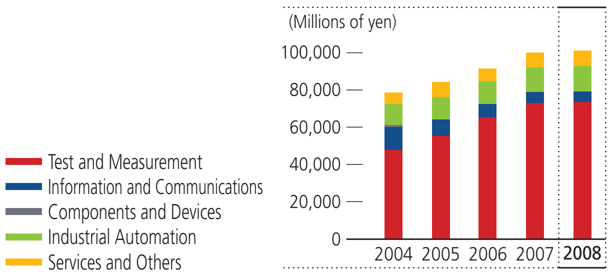
Geographical Segments

Japan

In the domestic test and measurement business, sales were firm of 3G and 3.5G measuring equipment to domestic mobile handset manufacturers for new handset models that can be used internationally. However, demand waned for highly profitable measuring instruments for use in research and development, and sales and operating income decreased. In addition, NGN development and general purpose measuring instruments did not contribute to sales as planned because of factors including the time needed to launch new products aimed at increasing profitability and restrained capital investment among customers.

The information and communications business was profitable even though customers made conspicuous adjustments to their capital investment plans, centered on public information systems, and private-sector sales of bandwidth control equipment weakened despite cooperation with system integrators and other approaches. In the industrial automation business, heightened concern about food safety and security resulted in higher sales, centered on X-ray inspection systems. In other businesses, in the device business waning demand for optical devices for the video distribution market caused sales to decline, but sales of low-cost existing products for metro networks increased. The Anritsu Group also incurred expenses associated with efforts to improve quality control in the precision measuring instruments business. Operating income in Japan decreased due to these and other factors.

Sales by Business Segment



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

As a result, sales in Japan increased 0.5 percent year on year to ¥50,167 million, and operating income decreased 51.6 percent to ¥2,497 million.

Americas

In the Test and Measurement segment, sales of handheld measuring instruments for installation and maintenance of base stations for mobile communications were solid. However, operating income decreased in the absence of the large-scale orders of the previous fiscal year. Sales of general purpose handheld measuring instruments for applications such as measuring radio waves were strong, but sales of other general purpose measuring instruments decreased.

As a result, sales in the Americas decreased 1.0 percent year on year to ¥20,438 million, and operating income decreased 14.8 percent to ¥3,471 million.

Europe

In the Test and Measurement segment, sales of 3G and 3.5G measuring equipment decreased due to waning demand for use in R&D. However, in the Service Assurance business, the Anritsu Group continued to execute the Tier 1 strategy initiated in the previous fiscal year, and received orders from major telecom operators. As a result, sales increased substantially and the operating loss narrowed.

As a result, sales in Europe increased 8.0 percent year on year to ¥19,267 million, and the operating loss decreased substantially to ¥1,925 million from ¥3,005 million for the previous fiscal year.

Asia and Others

In the Test and Measurement segment, demand for measuring instruments was impacted because full-scale demand for TD-SCDMA handsets in China has not yet developed and demand for measuring instruments for mass production of universal mobile telecommunication system (UMTS) handsets (3G for Europe and the Americas) has not reached expected levels. Demand for handheld measuring instruments for installation and maintenance of base stations and for measuring instruments for construction and maintenance of optical networks was stagnant. In the industrial automation business, demand remained solid in Southeast Asia for products such as specialized checkweighers.

As a result, sales decreased 4.0 percent year on year to ¥10,614 million, and operating income decreased 23.7 percent to ¥438 million.

Liquidity and Financial Condition

Fund Procurement and Liquidity Management

The Anritsu Group's funding requirements consist primarily of working capital such as material purchase costs and operating expenses incurred in product manufacturing, sales and marketing, as well as capital investment funds and research and development expenses. Anritsu supplements internal capital resources by directly and indirectly procuring funds from external sources to secure sufficient liquidity. In addition, despite a worldwide contraction in credit resulting from turbulence in financial markets triggered by the subprime mortgage problem in the United States, the Anritsu Group established a committed ¥15,000 million line of credit in April 2008 that will be available until March 2011, thus securing stable financing. Looking forward, while preparing for unforeseen financial risks, both domestic and overseas, in a dramatically changing market environment, the Anritsu Group will swiftly and flexibly meet its capital requirements for working capital, repayment of long-term borrowings and business growth.

In the year ended March 31, 2008, Anritsu continued to make progress in reducing interest-bearing debt. As a result, the balance of interest-bearing debt was ¥47,010 million, compared to ¥53,033 million at the end of the previous fiscal year. The net debt-to-equity ratio[1] was 0.57 times, compared with 0.54 times at the previous fiscal year-end. The debt-to-equity ratio[2] was 0.89 times, compared with 0.86 times at the previous fiscal year-end.

The Company will use increased cash flow generated by improvements in Anritsu Capital-cost Evaluation[3] 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 shareholders' equity and fortify its financial structure. At the end of March 2008, Rating and Investment Information, Inc. (R&I) rated Anritsu's short-term debt a-2, and its long-term debt BBB. Anritsu will continue working to enhance its financial stability in order to improve its debt rating.

Note 1: Net debt-to-equity ratio: (Interest-bearing debt - Cash and cash equivalents)/Net assets

Note 2: Debt-to-equity ratio: Interest-bearing debt/Net assets

Note 3: Anritsu Capital-cost Evaluation (ACE): Net operating profit after tax - Invested capital cost

Cash Flow

Cash and cash equivalents as of March 31, 2008 decreased ¥3,262 million from the end of the previous fiscal year to ¥16,685 million. The main factor was the reduction of interest-bearing debt.

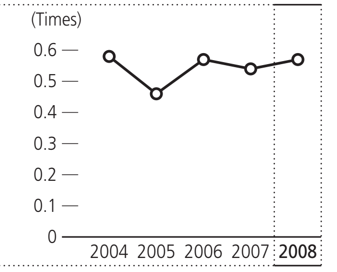
Free cash flow, defined as the sum of net cash provided by operating activities and net cash provided by or used in investing activities, increased to ¥3,878 million from ¥2,908 million for the previous fiscal year.

Net cash provided by operating activities totaled ¥6,251 million, compared with ¥2,488 million in the previous fiscal year. Main factors included more efficient deployment of working capital through means including reduction in inventories. Moreover, income taxes payable at U.S. subsidiaries decreased. Depreciation and amortization was ¥3,348 million, a decrease of ¥322 million compared with the previous fiscal year.

Net cash used in investing activities was ¥2,373 million. In the previous fiscal year, investing activities provided net cash of ¥420 million. This year-on-year change primarily reflected the absence of the proceeds from sale of marketable and investment securities of the previous fiscal year. Acquisition of property, plant and equipment totaled ¥2,438 million, an increase of ¥219 million compared with the previous fiscal year.

Net cash used in financing activities was ¥6,625 million, compared with ¥13,975 million in the previous fiscal year. One factor in the year-on-year change was the April 2007 repayment of a syndicated loan totaling ¥7,000 million. The Anritsu Group prepared for the January 2008 redemption of the third series of unsecured bonds totaling ¥15,000 million by issuing the fourth series of unsecured bonds totaling ¥10,000 million in September 2007, and by procuring a syndicated loan totaling ¥7,000 million in January 2008.

Net Debt-to-Equity Ratio



Assets, Liabilities and Net Assets

As of March 31, 2008, total assets decreased 11.0 percent, or ¥15,478 million, from a year earlier to ¥124,917 million. Current assets decreased 11.4 percent, or ¥9,733 million, from a year earlier to ¥75,659 million. Primary factors included a decrease in inventories reflecting the loss on devaluation of inventories and the loss on disposal of inventories incurred for the fiscal year.

The inventory turnover ratio improved to 4.9 times from 3.7 times for the previous fiscal year. One of the Anritsu Group's near-term objectives is to increase the inventory turnover ratio to 6.0 times.

Property, plant and equipment net of accumulated depreciation decreased 6.4 percent, or ¥1,513 million, from a year earlier to ¥21,946 million. Factors included a reduction in assets resulting from the restructuring of R&D divisions in connection with the discontinuation of certain products in the former Optical, Digital and IP Test and Measurement sub-segment. Investments and other assets decreased 13.4 percent, or ¥4,232 million, from a year earlier to ¥27,312 million. Factors included a reduction in goodwill based on international accounting standards through the one-time amortization of testing research expenses associated with the discontinuation of certain products in the network monitoring business.

As of March 31, 2008, total liabilities decreased 8.5 percent, or ¥6,704 million, from a year earlier to ¥72,072 million. Current liabilities decreased 46.3 percent, or ¥23,651 million, from a year earlier to ¥27,435 million. The decrease was the result of the redemption of the third series of unsecured bonds totaling ¥15,000 million and the repayment of the syndicated loan totaling ¥7,000 million. The current ratio was 275.8 percent, compared to 167.2 percent a year earlier. Working capital totaled ¥48,224 million as of March 31, 2008, compared to ¥34,305 million a year earlier.

Long-term liabilities decreased 61.2 percent, or ¥16,947 million, from a year earlier to ¥44,637 million. Long-term debt increased ¥16,283 million from a year earlier to ¥40,734 million because the Anritsu Group issued the fourth series of unsecured bonds totaling ¥10,000 million and procured a ¥7,000 million syndicated loan. Total interest-bearing debt decreased ¥6,023 million from a year earlier to ¥47,010 million.

Net assets decreased 14.2 percent, or ¥8,774 million, from a year earlier to ¥52,845 million. The ratio of net assets to total assets was 42.3 percent, compared to 43.9 percent a year earlier.

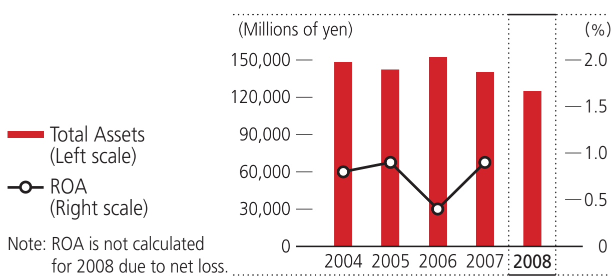
Capital Expenditures

For the fiscal year ended March 31, 2008, capital expenditures increased 20.3 percent compared with the previous fiscal year to ¥2,791 million. The Anritsu Group is concentrating resources in fields related to the ongoing evolution of communication network quality and high performance, including the integration of wireline and wireless communication networks, and the development of next-generation networks. During the year ended March 31, 2008, the Anritsu Group concentrated capital expenditures in the core Test and Measurement segment with the primary objectives of enhancing research and development efficiency and rationalizing its production network.

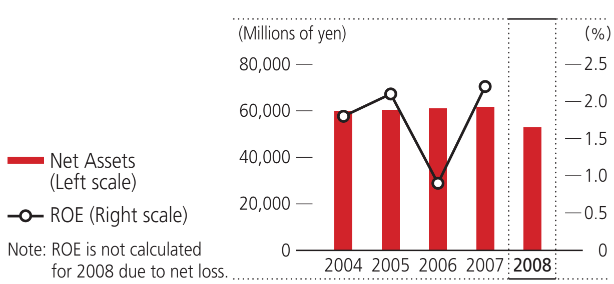
Overview of Capital Expenditures (Millions of yen)

	2008	Change (%)
Test and Measurement	¥2,162	27.2%
Information and Communications	83	(30.5)
Industrial Automation	192	15.3
Services and Others	285	1.8
Sub-total	2,722	20.2
Eliminations or corporate	69	24.8
Total	¥2,791	20.3%

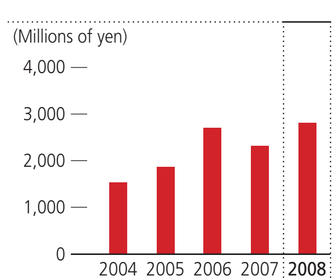
Total Assets and ROA



Net Assets and ROE



Capital Expenditures



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, 2008 follows below.

(Millions of yen)

	2008	Ratio to Segment Sales (%)
Test and Measurement	¥10,576	14.5%
Information and Communications	369	6.4
Industrial Automation	1,092	8.0
Services and Others	347	4.1
Basic Research	1,731	—
Total	¥14,115	14.0%

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) MP1800A Signal Quality Analyzer: Development of 10G Ethernet, Optical Module, and Stressed Receiver Testing

With the increasingly large volume of web content, data transmission capacity is constantly expanding. This is leading to rapid development and production of optical modules for 10G Ethernet and transmission devices equipped with these modules. These conditions are creating a need for test environments with the high repeatability necessary to ensure stable interconnectivity of transmission devices. Anritsu has enhanced the functionality of the MP1800A Signal Quality Analyzer by enabling stressed receiver conformance testing,[4] which contributes to efficient test performance to secure interconnectivity.

Note 4: Stressed receiver conformance testing: Bit error rate testing of 10GbE optical modules and transmission devices by intentionally transmitting a faulty waveform.

2) MD1230B Data Quality Analyzer: Development of a Traffic Impairment Emulator

NGNs are leading communications and video distribution to migrate to IP. For real-time services such as video delivery, exemplified by IPTV, and communications that use Voice over IP (VoIP), raising QoS and quality of experience (QoE)[5] are key to providing high-quality, enjoyable services. High QoE is contingent upon stable operation of networks and transmission devices despite the various conditions that can stress or impair transmission. By enhancing the functions of the MD1230B Data Quality Analyzer, Anritsu has developed a traffic impairment emulator that enables the construction of effective QoE testing environments. It enables highly accurate reproduction of conditions that stress and impair networks, and provides an effective testing environment for communication and broadcast providers, transmission equipment manufacturers and others testing network equipment QoE.

Note 5: Quality of Experience: The perceived quality of service among users.

3) MS2690A/91A/92A Signal Analyzer: Development of Measurement Functions for LTE

With 3G now spreading globally, standardization is progressing for 3.9G, the next-generation communication system featuring even faster data transmission and fewer delays. Moreover, development of base stations, mobile phones, amplifiers, antennae and other equipment for LTE has begun, creating a growing need for the measuring instruments required for LTE technology development. Anritsu has launched the MS269XA series of signal analyzers for next-generation broadband wireless communication signal analysis, and has enhanced functionality by developing software for generating LTE signal waveform patterns and for fast, highly accurate measurement. The MS269XA is a one-box solution for testing transmission and reception performance of base stations, mobile phones and devices for LTE with a simple evaluation system that raises work efficiency. Moreover, its high-speed measurement enables high testing throughput during communication equipment production inspection, which contributes to lower manufacturing costs.

2. Information and Communications

Development of the EN5001A L2SW with an On-Board Elementary Stream (ES) Converter

The EN5001A L2SW with an on-board ES converter has six Fast Ethernet ports and one primary communication port and allows construction of wide-area LANs through existing synchronous digital hierarchy (SDH) transmission channels.

Networks are getting faster and covering wider areas, creating the need for centralized, low-cost monitoring of IP equipment installed in remote locations. The EN5001A L2SW responds to this need by using transmission channels to send maintenance information from remote measuring equipment used in the construction of wide-area LANs to the operations center.

3. Industrial Automation

Development of Quality Management and Control Systems

Given rising concerns about food safety and security, food manufacturers are focusing on strict control of the growing regions and raw materials that are part of the food production process as well as control of the food production processes themselves. To maintain quality, the scope of inspection is expanding from the shipment processes following packaging to raw material processing. Moreover, food manufacturers want quality inspection equipment tailored to the characteristics and shapes specific to their own products, which has resulted in striking diversification of customer needs.

Responding to these market conditions, Anritsu has expanded its product lineup and is developing products that respond to specific customer quality inspection needs.

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, 2008, consolidated ACE was negative ¥750 million, compared to negative ¥1,397 million for the previous fiscal year. Anritsu did not have consolidated ROE for the year ended March 31, 2008 because of the net loss, while ROE was 2.2 percent for the previous fiscal year. The Anritsu Group is now restructuring under a strategy of generating profitable growth while enhancing competitiveness and profitability, and has set the medium-term targets of a consolidated operating margin of 10 percent or higher and ROE of 10 percent or higher.

Outlook and Management Issues for the Year Ending March 31, 2009

For the year ending March 31, 2009, expansion of emerging economies is expected to continue supporting the global economy. Ongoing turbulence in world financial markets, however, warrants attention to factors including concerns about economic recession in the United States, the effect that such a recession would have on Japan and Europe, foreign exchange trends and the worsening of corporate profits that would result. In this severe market environment, the Anritsu Group will deploy the following measures.

In the Test and Measurement segment, Anritsu will begin implementing the measures in Management Innovation 2008 announced in January 2008 to raise profitability. To further improve profitability in the Service Assurance business, Anritsu will promote the Tier 1 strategy and increase efforts outside of EMEA. In the Mobile Handset sub-segment, Anritsu will focus on enhancing measuring instruments used in the development of 3.9G LTE handsets, which is now well under way. In sales, Anritsu will continue to expand sales channels and promote the launch of new products that match market needs by getting closer to customers through sharing development road maps with key customers and strengthening its product planning ability.

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, while strengthening cost-cutting to improve profitability, Anritsu aims to expand by promoting a product strategy of higher added value and differentiation while further accelerating business development in overseas markets

While steadily executing these business strategies, Anritsu will emphasize appropriate management of and response to risks and the shift to new sources of competitiveness. Anritsu will do so by refining and coordinating the internal control system that it is vigorously developing while continuously improving our risk management system and working to achieve its management targets.

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

In the core Test and Measurement segment, Anritsu anticipates sales growth in the Service Assurance business, but expects sales to decline in other Test and Measurement businesses due to restrained capital investment by customers. However, Anritsu expects sales growth to continue in the Industrial Automation segment. Overall, Anritsu projects that net sales will be essentially unchanged from the year ended March 31, 2008.

Anritsu expects the implementation of Management Innovation 2008 to enhance profitability. However, loss on devaluation of inventories, previously recorded in other income (expenses), will be included in cost of sales in accordance with a new accounting standard for inventory valuation effective April 1, 2008. The strong yen and weak dollar will also erode earnings. Consequently, Anritsu expects operating income for the year ending March 31, 2009 to decrease. In addition, Anritsu projects that it will recognize the difference in inventories at the beginning and the end of the fiscal year resulting from the application of the new accounting standard as a charge of approximately ¥1.5 billion included in other income (expenses).

Given the above factors, for the year ending March 31, 2009 Anritsu projects as of April 24, 2008 that net sales will decrease 0.5 percent year on year to ¥100.0 billion, operating income will decrease 16.0 percent year on year to ¥4.5 billion, and net income will total ¥1.0 billion, compared with the net loss of ¥3.9 billion in the year ended March 31, 2008.

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, 2008.

(1) Inherent Risks in the Anritsu Group's Technology and Marketing Strategies

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 quadruple play services incorporating voice, video, internet and mobile, as well as Fixed-Mobile Convergence (FMC) and NGN.

(2) Market Fluctuation Risk

External factors including changes in the economy or market conditions and technological innovation affect the profitability of product lines the Group develops and have the potential to exert a significant material impact on the Anritsu Group's results.

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 quad play services, FMC and NGN are accelerating alliances 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, penetration rate 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 segment, sales to food manufacturers constitute about 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 this segment's performance.

(3) 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 business is about 70 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 increase in mergers, acquisitions and realignment among operators doing business globally and telecommunications equipment manufacturers, which is expected to continue 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.

(4) Foreign Exchange Risk

The Anritsu Group's sales outside Japan account for 55.9 percent of consolidated net sales. The Anritsu Group hedges foreign exchange risk using instruments including forward foreign exchange contracts for foreign exchange 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.

(5) Long-term Inventory Obsolescence Risk

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 result in obsolescence of products and parts, 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.

(6) Risk of Impairment of Goodwill

As of March 31, 2008, the balance sheets of the Anritsu Group included goodwill resulting from the acquisition of an overseas company in order to expand the scope of business of the Test and Measurement segment. The impact on earnings of the Test and Measurement business from changes in the global economy and markets, intensifying competition and other factors has the potential to cause the Group to recognize impairment of goodwill.