

Overview of Operations 2003

2003 is a challenging year for the Company, there were many complicated factors affecting the domestic economy such as substantial increase of unemployment rate, increasing debts in credit cards and households, followed by the shrinkage of consumption. Korean economy was expected to turn more prosperous as the recovery of export market from the second half of the year, the stagnant domestic economy was anticipated to last.

Under the fierce competition among confectionary companies along with the harsh economic environment, the rapid change of forming large-scale distribution market and unfavorable economic condition, the overall market growth rate declined from 14.0% the previous year to 3.7%.

With the unfavorable economic situation, the Company recorded the growth of 5.4% in domestic confectionary market and its market share rate improved by 0.4%p to 25.3% in 2003, solidifying its position as a leading company in the market. In export market, sales substantially grew by 15.4% to record total sales of KRW 511.4 billion in confectionary market.

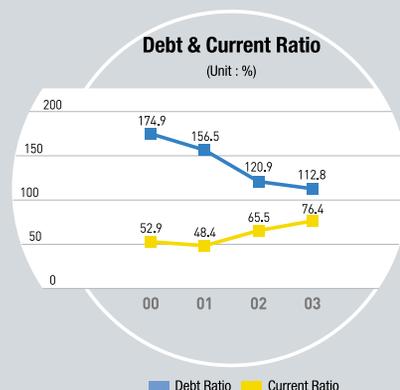
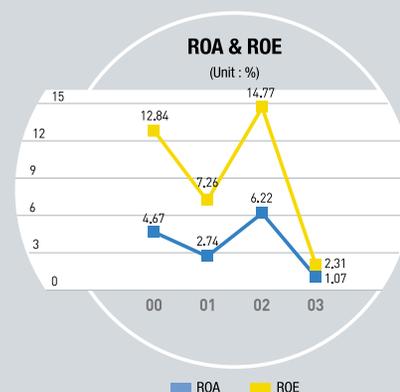
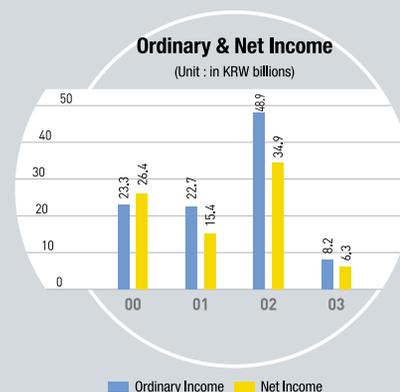
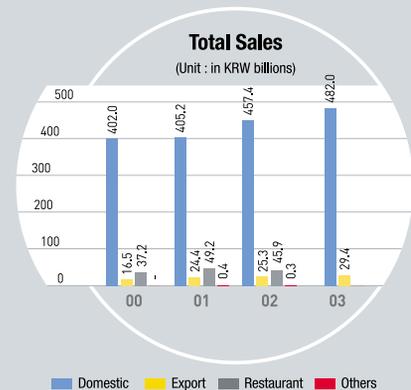
Overall sales slightly decreased by 3.3% due to the separation of restaurant business from the group in 4th quarter of 2002. Accordingly, total sales arose by 5.9% from 2002 except the restaurant business.

Operating income margin posted 9.7%, down by 0.4%p primarily due to the separation of restaurant business, the increase of general & administrative expenses and other expenses. Ordinary income significantly decreased due to the fact that the loss of KRW 28.3 billion incurred from the use of the equity method including the loss of KRW 10 billion from the investment in Tigerpools International and the delay in the operation of lottery business.

One-time expenses from the merger with Tigerpools International and affiliates affected the performance in 2003, but the improvement is expected due to the base impact. Especially, the great performance has been realized in the entertainment businesses such as Mediaplex, Megabox and ON*MEDIA. Of these business lines, Mediaplex involved in the investment and distribution of the movies 'Taegukgi', the surprise hit of the year, Megabox and ON*MEDIA, as a leader in cable TV industry, are anticipated to improve in their performance.

Although there was an investment in the lottery business in 2003, net debt posted only KRW 218.1 billion and debt-to-equity rate continuously improved and recorded 113%, showing a 10% decrease in 2003.

While the stagnant economy seems to be rarely recovered along with the inflation, the Company will focus on core brand strategies and the introduction of new products by reducing the costs and providing a variety of products based on its ideology 'the growth based on profitability'. Furthermore, we continuously enhance our competitiveness in responding to the changeable market situation.



■ FIVE-YEAR SUMMARY

	In millions of KRW	In thousands of USD*	2002	2001	2000	1999
	2003	2003				
For the year						
Sales	511,437	426,980	528,920	479,164	455,669	452,767
Gross profit	205,799	171,814	221,220	197,939	184,866	184,461
Operating Income	49,394	41,237	53,659	39,443	32,446	49,721
Net Income	6,258	5,225	34,889	15,403	26,399	21,890
Depreciation	13,541	11,305	15,437	18,129	19,177	19,756
At year end						
Total Assets	615,000	513,441	560,270	560,858	565,027	492,823
Current Assets	115,075	96,072	107,935	121,832	124,430	117,906
Non-current Assets	499,926	417,370	452,336	439,027	440,596	374,918
Total Liabilities	325,995	272,161	306,644	342,177	359,475	302,985
Capital Stock	27,162	22,676	26,956	26,662	26,534	25,541
Capital Surplus	117,167	97,819	116,416	115,344	114,877	114,884
Retained Earnings	114,813	95,853	113,997	80,891	69,194	47,457
Stockholders' Equity	289,006	241,281	253,626	218,681	205,552	189,838
Financial ratios (%)						
ROA	1.07		6.22	2.74	4.67	4.42
ROE	2.31		14.77	7.26	12.84	12.74
Debt Ratio	112.8		120.9	156.5	174.9	159.6
Current Ratio	76.4		65.5	48.4	52.9	63.3

* Accounts in Korean won have been translated into U.S. dollars, solely for the reader's convenience, at W 1,197.8, the prevailing rate on December 31, 2003.

BALANCE SHEETS

December 31, 2002 and 2003

Assets	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Current assets:			
Cash and cash equivalents (Notes 3 and 8)	₩ 1,152,029	₩ 10,102,400	US\$ 8,434,129
Short-term financial instruments	1,049,080	378,530	316,021
Current investment securities (Note 6)	-	9,615	8,027
Accounts and notes receivable - trade, less allowance for doubtful accounts (Notes 4, 8 and 15)	78,710,307	78,067,439	65,175,688
Accounts receivable - other	471,376	477,338	398,512
Accrued interest income	35,610	7,988	6,669
Prepaid expenses	654,085	842,619	703,473
Inventories (Note 5)	25,527,202	24,985,767	20,859,716
Other current assets	334,812	203,067	169,533
Total current assets	107,934,501	115,074,763	96,071,768
Investments and other assets:			
Long-term financial instruments (Note 3)	23,500	20,500	17,115
Investments in securities (Note 6)	219,395,411	265,336,058	221,519,501
Guarantee deposits	8,263,920	6,548,213	5,466,867
Deferred income tax assets (Note 16)	8,742,051	14,947,338	12,478,993
Total investments and other assets	236,424,882	286,852,109	239,482,476
Property, plant and equipment (Note 7):			
Land	103,834,433	103,834,433	86,687,621
Buildings and structures	80,901,356	80,983,983	67,610,605
Machinery and equipment	139,694,820	145,398,097	121,387,625
Vehicles	10,128,629	12,009,588	10,026,372
Tools, furniture and fixtures	23,868,720	26,085,577	21,777,907
Construction in-progress	11,974,631	11,847,972	9,891,444
	370,402,589	380,159,650	317,381,574
Less accumulated depreciation	(155,038,540)	(167,709,096)	(140,014,274)
Property, plant and equipment, net	215,364,049	212,450,554	177,367,300
Intangibles, net of amortization	546,881	622,888	520,027
Total assets	₩ 560,270,313	₩ 615,000,314	US\$ 513,441,571

See accompanying notes.

BALANCE SHEETS

December 31, 2002 and 2003

Liabilities and Stockholders' Equity	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Current liabilities:			
Accounts and notes payable - trade (Notes 8 and 15)	₩ 37,476,042	₩ 42,578,400	US\$ 35,547,169
Short-term borrowings (Notes 8 and 9)	46,101,226	14,057,544	11,736,136
Accounts payable - other	29,358,589	30,298,555	25,295,170
Advances from customers	15,220	733,650	612,498
Income taxes payable	9,511,792	4,177,070	3,487,285
Accrued expenses and other current liabilities	2,802,302	1,372,357	1,145,731
Current portion of long-term debt, bonds, and capital leases, less discount (Notes 10 and 11)	39,503,490	57,496,085	48,001,407
Total current liabilities	164,768,661	150,713,661	125,825,396
Long-term liabilities:			
Long-term debt and bonds, less discount and current portion (Notes 10 and 11)	124,543,160	157,060,324	131,123,997
Severance and retirement benefits (Notes 12 and 20)	9,843,485	10,214,156	8,527,430
Tenant lease deposits and other	4,241,975	4,643,220	3,876,458
Reserve for loss on sales return	3,246,833	3,363,163	2,807,783
Total long-term liabilities	141,875,453	175,280,863	146,335,668
Total liabilities	306,644,114	325,994,524	272,161,064
Commitments and contingencies (Note 13)			
Stockholders' equity (Note 14):			
Common stock, W5,000 par value			
Authorized - 12,000,000 shares			
Issued - 5,391,296 in 2002 and 5,432,310 in 2003	26,956,480	27,161,550	22,676,198
Outstanding - 4,681,259 in 2002 and 4,722,373 in 2003			
Capital surplus	116,415,775	117,167,486	97,818,907
Retained earnings (Note 14)			
Appropriated	79,300,000	108,200,000	90,332,276
Unappropriated	34,697,273	6,612,590	5,520,613
	113,997,273	114,812,590	95,852,889
Capital adjustment account:			
Treasury stock (710,037 in 2002 and 709,937 in 2003) (Note 14)	(16,607,561)	(16,605,222)	(13,863,101)
Gain on valuation of investments (Note 6)	12,742,717	46,082,867	38,472,924
Stock compensation expense (Note 14)	121,515	386,519	322,690
	(3,743,329)	29,864,164	24,932,513
Total stockholders' equity	253,626,199	289,005,790	241,280,507
Total liabilities and stockholders' equity	₩ 560,270,313	₩ 615,000,314	US\$ 513,441,571

See accompanying notes.

STATEMENTS OF INCOME

Years ended December 31, 2002 and 2003

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Net sales (Notes 15 and 19)	₩ 528,920,711	₩ 511,436,672	US\$ 426,980,023
Costs and expenses:			
Cost of sales (Notes 15 and 19)	307,700,301	305,637,937	255,166,085
Selling, general and administrative expenses (Note 20)	167,561,735	156,404,890	130,576,799
	475,262,036	462,042,827	385,742,884
Operating income	53,658,675	49,393,845	41,237,139
Other income (expenses):			
Interest expense	(17,371,304)	(14,897,108)	(12,437,058)
Interest income	1,045,376	933,568	779,402
Dividend income	781	103	86
Unrealized foreign currency translation gain (loss), net	65,539	(62,554)	(52,224)
Realized foreign currency exchange gain, net	208,893	(135,620)	(113,224)
Gain (loss) on disposal of property, plant and equipment, net	503,202	153,645	128,273
Equity income on investments in affiliated companies, net (Note 6)	10,318,287	(28,285,697)	(23,614,708)
Gain on disposal of investments, net (Note 6)	40,496	(191,710)	(160,052)
Loss on redemption of bonds	(240,000)	-	-
Impairment of investments in securities	(255,128)	(55,350)	(46,210)
Donations	(586,015)	(304,628)	(254,323)
Miscellaneous	1,494,372	1,658,312	1,384,465
	(4,775,501)	(41,187,039)	(34,385,573)
Ordinary income	48,883,174	8,206,806	6,851,566
Extraordinary gain (loss)	-	-	-
Income before income taxes	48,883,174	8,206,806	6,851,566
Provision for income taxes (Note 16):			
Current	11,843,733	9,065,152	7,568,168
Deferred	2,150,396	(7,116,803)	(5,941,562)
	13,994,129	1,948,349	1,626,606
Net income	₩ 34,889,045	₩ 6,258,457	US\$ 5,224,960
Basic ordinary income per share (Note 17)			
(Korean won and U.S. dollars in units)	₩ 7,505	₩ 1,331	US\$ 1.11
Basic earnings per share (Note 17)			
(Korean won and U.S. dollars in units)	₩ 7,505	₩ 1,331	US\$ 1.11
Diluted ordinary earnings per share (Note 17)			
(Korean won and U.S. dollars in units)	₩ 6,976	₩ 1,234	US\$ 1.03
Diluted earnings per share (Note 17)			
(Korean won and U.S. dollars in units)	₩ 6,976	₩ 1,234	US\$ 1.03

See accompanying notes.

STATEMENTS OF APPROPRIATIONS OF UNAPPROPRIATED RETAINED EARNINGS

Years ended December 31, 2002 and 2003

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Unappropriated retained earnings at end of year before reversal and appropriations:			
Unappropriated retained earnings carried over from prior year	₩ 1,591,081	₩ 1,116,014	US\$ 931,720
Increase (decrease) in retained earnings due to equity method of accounting for investments in affiliated companies (Note 6)	499,671	(761,881)	(636,067)
Cumulative effect of changes in principles and practice	(2,282,524)	-	-
Net income for the year	34,889,045	6,258,457	5,224,960
	34,697,273	6,612,590	5,520,613
Reversal of reserve for technology development	2,000,000	1,000,000	834,864
Reversal of voluntary reserve	-	4,000,000	3,339,456
Unappropriated retained earnings available for appropriations	36,697,272	11,612,590	9,694,933
Appropriations:			
Legal reserve	500,000	500,000	417,432
Reserve for business rationalization	400,000	-	-
Reserve for financial position improvement	5,000,000	1,000,000	834,864
Reserve for additional equipment	12,000,000	-	-
Reserve for technology development	6,000,000	4,000,000	3,339,456
Voluntary reserve	7,000,000	-	-
Cash dividends (Note 18)	4,681,259	4,722,373	3,942,539
	35,581,259	10,222,373	8,534,291
Unappropriated retained earnings to be carried forward to next year	₩ 1,116,014	₩ 1,390,217	US\$ 1,160,642

See accompanying notes.

STATEMENTS OF CASH FLOWS

Years ended December 31, 2002 and 2003

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Operating activities:			
Net income	₩ 34,889,045	₩ 6,258,457	US\$ 5,224,960
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	15,437,197	13,540,919	11,304,825
Bad debt written off	3,475,101	5,198,505	4,340,044
Provision for severance and retirement benefits	10,226,661	7,439,355	6,210,849
Payments of severance and retirement benefits, net of transfers	(8,868,778)	(7,231,363)	(6,037,204)
Decrease in accumulated prepayments to Korean National Pension Fund	360,350	284,983	237,922
Amortization of discount on bonds	114,850	13,248	11,061
Amortization of intangible assets	349,090	239,187	199,688
reserve for returned goods unsold	-	116,330	97,120
Gain on disposal of investments, net	(40,496)	191,710	160,052
Loss on disposal of property, plant and equipment, net	(503,202)	(153,645)	(128,273)
Equity income on investments in affiliated companies, net	(10,318,287)	28,285,697	23,614,708
Unrealized foreign currency translation loss (gain), net	(55,993)	62,702	52,348
Loss on redemption of bonds	240,000	-	-
Impairment of investments in securities	225,128	55,350	46,210
Stock compensation expense	121,515	273,154	228,046
Changes in operating assets and liabilities:			
Accounts and notes receivable - trade	(479,326)	(4,551,613)	(3,799,978)
Accounts receivable - other	243,424	(5,962)	(4,977)
Accrued interest income	195,471	27,622	23,060
Prepaid expenses	309,852	(188,535)	(157,401)
Other current assets	214,663	131,745	109,989
Inventories	1,115,508	541,435	452,025
Long-term prepaid expenses	(844,039)	-	-
Deferred income tax assets	1,971,099	(6,205,286)	(5,180,570)
Accounts and notes payable - trade	(468,700)	5,093,897	4,252,710
Accounts payable - other	(1,208,865)	939,967	784,745
Advances from customers	(350,898)	718,431	599,792
Income taxes payable	7,215,118	(5,334,722)	(4,453,767)
Accrued expenses and other current liabilities	965,383	(1,429,947)	(1,193,811)
Tenant lease deposits and other	(123,278)	401,245	334,985
Net cash provided by operating activities	54,407,593	44,712,866	37,329,158

See accompanying notes.

STATEMENTS OF CASH FLOWS

Years ended December 31, 2002 and 2003

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Investing activities:			
Acquisition of marketable securities	₩ -	₩ (1,945,806)	US\$ (1,624,483)
Proceeds from disposal of marketable securities	16,148	-	
Decrease in short-term financial instruments	1,570,950	670,550	559,818
Decrease in long-term financial instruments	-	3,000	2,505
Decrease (increase) in guarantee deposits	(3,205,775)	1,715,707	1,432,382
Acquisition of investments in securities	(35,737,459)	(40,000,000)	(33,394,557)
Proceeds from disposal of investment in securities	1,521,351	41,057	34,277
Increase (decrease) in deposits for employee's group severance insurance	(72,878)	(122,304)	(102,107)
Acquisition of property, plant and equipment	(16,020,605)	(13,129,964)	(10,961,733)
Proceeds from disposal of property, plant and equipment	2,895,298	2,656,184	2,217,553
Increase in intangible assets	(327,262)	(315,193)	(263,143)
Decrease in cash and cash equivalents due to spin-off	(15,500,000)	-	-
Net cash used in investing activities	(64,860,232)	(50,426,769)	(42,099,488)
Financing activities:			
Increase (decrease) in short-term borrowings	(42,049,042)	(32,101,947)	(26,800,758)
Repayment of current portion of long-term debt	(64,862,626)	(39,503,490)	(32,980,039)
Increase in long-term debt and bonds	142,240,649	90,000,000	75,137,753
Decrease in long-term debt and bonds	(24,340,260)	-	-
Decrease in short-term loans	10,284	-	-
Common stock issued for stock warrants	1,369,765	952,880	795,525
Stock issuance costs	(2,724)	(1,910)	(1,595)
Payment of cash dividends	(3,466,726)	(4,681,259)	(3,908,214)
Net cash provided by financing activities	8,899,320	14,664,274	12,242,672
Net decrease in cash and cash equivalents	(1,553,319)	8,950,371	7,472,342
Cash and cash equivalents at the beginning of the year	2,705,348	1,152,029	961,788
Cash and cash equivalents at the end of the year	₩ (1,152,029)	₩ 10,102,400	US\$ 8,434,130
Transactions not involving inflow or outflow of cash:			
Transfer of construction in-progress to appropriate property, plant and equipment accounts	₩ 5,560,421	₩ 2,349,601	US\$ 1,961,597
Transfer of long-term debt to current portion	39,503,490	57,506,475	48,010,081
Acquisition of investments by stock swaps	2,619,048	-	-
Depreciation offset against government grants	12,109	12,109	10,109
Transfer of long-term financial instruments to short-term financial instruments	75,000	-	-
Decrease in assets due to spin-off	83,429,844	-	-
Decrease in liabilities due to spin-off	54,266,623	-	-

See accompanying notes.

1. Organization and business

Orion Corporation ("the Company") was incorporated as Tong Yang Confectionery Corporation in 1956, under the laws of the Republic of Korea to engage in the business of manufacturing and selling confectioneries. On September 1, 2001, the Company, together with all its affiliates (Note 6), separated from the Tong Yang Group of companies to establish its own identity as a confectionery, food and entertainment business group. Accordingly, the Company changed its name from Tong Yang Confectionery Corporation to Orion Corporation on August 29, 2003.

As of December 31, 2003, the Company has four manufacturing plants in Korea to produce biscuits, chocolates, pies and gums. The Company also sells merchandise purchased from Orion Frito-Lay Corp., a 50% owned company organized locally under a joint venture agreement with PepsiCo Foods International Inc. of the United States of America.

The Company's common stock has been listed on the Korea Stock Exchange since June 27, 1975.

2. Basis of financial statements and summary of significant accounting policies

Basis of financial statements | The Company maintains its official accounting records in Korean won and prepares statutory financial statements in the Korean language in conformity with accounting principles generally accepted in the Republic of Korea ("Korean GAAP"). Certain accounting principles applied by the Company that conform with financial accounting standards and accounting principles in the Republic of Korea may not conform with generally accepted accounting principles in other countries. Accordingly, these financial statements are not intended for use by those who are not informed about Korean accounting principles and practices. The accompanying financial statements have been condensed, restructured and translated into English (with certain expanded descriptions) from the Korean language financial statements.

Certain supplementary information included in the statutory Korean language financial statements, but not required for a fair presentation of the Company's financial position, results of operations and cash flows, is not presented in the accompanying financial statements.

Basis of translating the financial statements | Solely for the convenience of the reader, the 2003 financial statements, expressed in Korean won, have been translated to United States dollar amounts at the exchange rate of ₩1,197.80 to US\$1, the prevailing exchange rate on December 31, 2003. This translation should not be construed as a representation that any or all of the amounts stated in Korean won could have been converted to United States dollars at this or any other rate.

Cash equivalents | Highly liquid marketable securities and short-term financial instruments with original maturities of three months or less, and which have no significant risk of loss in value by interest rate fluctuations, are considered as cash equivalents.

Financial instruments | Financial instruments, such as time deposits and restricted bank deposits, which are traded by financial institutions and are held for short-term cash management purposes or which will mature within one year, are accounted for as short-term financial instruments. Financial instruments other than cash equivalents and short-term financial instruments are recorded as long-term financial instruments.

Investment securities | Available-for-sale securities are stated at fair value. The unrealized gains and losses related to changes in the fair value of available-for-sale securities are reported as a separate component of stockholders' equity until realized. Trading securities are stated at fair value, with unrealized holding gains and losses reported as part of net income. Debt securities, classified as held-to-maturity, are stated at the acquisition cost adjusted for the amortization of discount or premium using the effective interest method.

Investment securities are evaluated to determine if they have suffered a loss in value that is other than temporary. The impairment loss is charged to current operations.

Investments in affiliated companies | Investments in affiliated companies over which the Company exercises significant control are stated using the equity method, whereby the Company's initial investment is recorded at acquisition costs and subsequently the carrying value is increased or decreased to reflect the Company's share of the investee's income or loss. If the increase or decrease is derived from changes in the investee's retained earnings, such change is presented as an increase or decrease in the investor's beginning retained earnings. If the increase or decrease is derived from the investee's changes in capital surplus or capital adjustments, then such amount is presented as a valuation gain or loss on investment securities, and is shown in a capital adjustment account within stockholders' equity.

Allowance for doubtful accounts | The Company provides an allowance for doubtful accounts to cover estimated losses that may arise from non-collection of its receivables. The estimate of losses is based on the estimated collectibility of receivables and historical bad debt experience.

Valuation of receivables at present value | Receivables arising from long-term installment transactions are stated at present value. The difference between the carrying amount of receivables and their present value is amortized using the effective-interest-rate method and credited to results of operations over the installment period.

When credit terms (e.g., principal, interest rate, payment period) of receivables from debtors experiencing financial difficulties (e.g., court receivership, debt restructuring, financial workout) are unfavorably changed from the perspective of the Company, such receivables are stated at present value and the difference between the carrying amount of such receivables and their present value is charged to current operations.

Foreign currency translation | The Company's books and records are maintained in Korean won. Transactions conducted in foreign currencies are recorded in Korean won based on the prevailing exchange rates when the transactions are made. Assets and liabilities denominated in foreign currencies are translated into Korean won at the exchange rates in effect at the balance sheet date. The resulting unrealized foreign currency translation gains (losses) are credited (charged) to current operations.

Inventories | Inventories are stated at the lower of cost or net realizable value. Cost is determined by specific identification for materials in transit, and the moving average method for all other inventories.

Property, plant and equipment and depreciation | Property, plant and equipment are stated at cost, except for assets which were revalued in accordance with the Korean Assets Revaluation Law.

Depreciation of property, plant and equipment has been provided using the declining balance method (straight-line method for buildings and structures acquired after January 1, 1995) over the following estimated useful lives:

	Useful lives of assets acquired from January 1, 1995	Useful lives of assets acquired before January 1, 1995
Building and structures	50	2~60
Machinery and equipment	10	2~10
Vehicles	5	2~15
Tools, furniture and fixtures	5	2~54

The Company has provided for depreciation on assets acquired after January 1, 1995 without retaining a 10% residual value in its accounts. Assets acquired prior to January 1, 1995 have been and will continue to be depreciated up to 90% of their acquisition costs, recognizing a 10% residual value to be disposed at equal amounts for three years after accumulated depreciation reaches 90% of their acquisition costs.

Maintenance and repairs are expensed in the year in which they are incurred. Expenditures that enhance the value or extend the life of an asset are capitalized as additions to property, plant and equipment. Interest expenses and financing charges on borrowings related to the construction or acquisition of property, plant and equipment are capitalized as part of the cost of the assets during construction period. The Company incurred total interest expense of ₩14,897,108 thousand in 2003 (₩17,371,304 thousand in 2002), of which ₩15,708 thousand (₩67,131 thousand in 2002) was capitalized.

Leased assets | Property, plant and equipment acquired under capital leases and the related lease obligations are recorded at the discounted present value of non-cancelable lease payments. Assets acquired under capital leases are depreciated using the same method as that provided for other assets acquired through purchase or construction. Rental expenses incurred for assets leased under operating leases are charged to current operations.

Intangible assets | Intangible assets are amortized using the straight-line method over periods of 5 years.

Discount (or premium) on bonds | The difference between proceeds from bonds (less bond issue and other related costs) and the face value of bond is presented as a deduction (or addition) from (to) the face value of the bonds and is amortized using the effective interest rate method over the life of the bonds.

Consideration for stock warrants of bonds | Interest expense on bonds with stock warrants is recognized using the effective interest rate which equalizes the issued amount of bonds to the present value of the future cash outflow of bonds with stock warrants. Accordingly, the differences between accrued interest and interest paid are presented as an addition to the nominal value of the bonds as a long-term accrued interest account.

Severance and retirement benefits | In accordance with the Korean Labor Standards Law and the Company's regulations, employees and directors with more than one year of service are entitled to severance and retirement benefits upon termination of their employment based on years of service, rates of pay in effect at the time of termination and certain other factors. The annual provision is sufficient to state the estimated obligation arising from services performed to and at rates of pay in effect at the end of year. Funding of this liability is not required by Korean law.

The lesser of 10% of annual payroll expense or 40% of the accumulated severance and retirement benefits provision is deductible for corporate income tax reporting purposes, unless benefits are actually paid or the non tax-deducted portion is deposited with financial institutions. Accordingly, the Company had deposited the required portion of its severance and retirement benefits obligation with life insurance companies. Since the Company's employees are individually nominated as the vested beneficiaries of these deposits, such deposits have been offset against the Company's liability for severance and retirement benefits at December 31, 2002 and 2003 (Note 12).

In accordance with the Korean National Pension Law prior to revision, the Company had prepaid a portion of its severance and retirement benefits obligation to the Korean National Pension Corporation ("KNPC") at a certain rate of payroll expense, up through March 31, 1999. Such accumulated prepayments have been offset against the Company's liability for severance and retirement benefits as of balance sheet dates. In accordance with the revised Korean National Pension Law, addition to such prepayments were no longer required effective April 1, 1999.

Revenue recognition | The Company recognizes revenue from sale of finished products and merchandise at the time of delivery.

Income taxes | Korean GAAP requires the recognition of deferred tax assets and liabilities arising from temporary differences between the financial reporting and tax reporting bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates which are expected to be applied to taxable income in the period such temporary differences are expected to be recovered or settled.

Earnings per share | Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock issued and outstanding during the period. Diluted earnings per share measures the performance of the Company over the reporting period while giving effect to all potential common shares, such as options, warrants and convertible debt, that were dilutive and outstanding during the period.

Use of estimates | The preparation of financial statements in conformity with Korean GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Korean GAAP revisions for 2004 | The Korean Accounting Standards Board has issued new accounting standards with the intention to revise Korean GAAP and disclosure rules to meet international practices. The revised accounting standards include changes in the areas of inventories, discontinued operations, construction contracts and troubled debt restructuring. Korean companies should apply such revised accounting standards for the first fiscal year starting after December 31, 2003 with the exception of the accounting for discontinued operations which should be applied from the fiscal year starting after December 31, 2004. Early adoption of the revised accounting standards is allowed with the exception of the accounting for discontinued operations. The cumulative effect on prior years of the changes in accounting standards will be primarily charged or credited to opening retained earnings with disclosures made on the effect of the changes.

The Company plans to adopt the revised accounting standards from January 1, 2004 with the exception of the accounting for discontinued operations which will be applied from January 1, 2005.

Restatement of 2002 financial statements | The Company adopted SKAS No. 4 in 2003, which requires the Company to recognize provision for loss on sales returns at the point of selling. The Company restated its financial statements as of December 31, 2002. This change resulted in a decrease of 2003 net income by ₩116,000 thousand and decrease in retained earnings by ₩2,283,000 thousand, for the cumulative effect of the change as of December 31, 2001.

Regarding this change, ordinary income, net income, ordinary income per share and earning per share for the past three years were restated as follows:

	Korean won in thousands		
	2000	2001	2002[*]
Ordinary income	₩ 23,165,977	₩ 21,802,478	₩ 48,883,174
Net income	26,316,276	14,778,273	34,889,045
Ordinary income per share	5,215	3,157	7,505
Earning per share	5,215	3,157	7,505

[*] There was no change in 2002.

In addition, the Company adopted SKAS No. 6 which requires that appropriations of retained earnings should be recorded after these are approved at the annual shareholders' meeting which is normally held after the balance sheet date. In prior years these were recorded at the balance sheet even before these were approved by stockholders. The Company restated its financial statements as of December 31, 2002, resulting in decrease of dividends payable as of December 31, 2002 by ₩4,681,259 thousand and increase in retained earnings by the same amount.

3. Cash and cash equivalents, and financial instruments

Cash and cash equivalents, and financial instruments as of December 31, 2002 and 2003 consisted of the following:

<u>2002</u>	Korean won in thousands		
	Cash and cash equivalents	Short-term financial instruments	Long-term financial instruments
Cash on hand	₩ 88,767	₩ -	₩ -
Checking accounts	1,063,262	-	-
Time deposits - Korean won denominated	-	974,080	-
Installment deposits	-	75,000	-
Restricted deposits	-	-	23,500
	₩ 1,152,029	₩ 1,049,080	₩ 23,500

<u>2003</u>	Korean won in thousands		
	Cash and cash equivalents	Short-term financial instruments	Long-term financial instruments
Cash on hand	₩ 9,799,837	₩ -	₩ -
Checking accounts	302,563	-	-
Time deposits - Korean won denominated	-	378,530	-
Installment deposits	-	-	-
Restricted deposits	-	-	20,500
	₩ 10,102,400	₩ 378,530	₩ 20,500
U. S. dollars (Note 2)	US\$ 8,434,129	US\$ 316,021	US\$ 17,115

Restricted deposits of ₩23,500 thousand as of December 31, 2002 and ₩20,500 thousand as of December 31, 2003 represent amounts with banks as guarantee deposits for the maintenance of checking accounts.

4. Accounts and notes receivable - trade

Accounts and notes receivable - trade at December 31, 2002 and 2003 consisted of the following:

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Accounts Receivable	₩ 51,471,853	₩ 50,213,670	US\$ 41,921,581
Notes receivable	28,492,103	29,882,409	24,947,745
	79,963,956	80,096,079	66,869,326
Allowance for doubtful	(1,253,649)	(2,028,640)	(1,693,638)
	₩ 78,710,307	₩ 78,067,439	US\$ 65,175,688

5. Inventories

Inventories as of December 31, 2002 and 2003 consisted of the following:

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Merchandise	₩ 4,775,755	₩ 5,105,202	US\$ 4,262,149
Finished goods	9,480,484	8,969,683	7,488,465
Work in-process	1,002,820	1,317,749	1,100,141
Raw materials	6,327,157	6,007,693	5,015,606
Supplies and parts	1,125,514	1,126,528	940,498
Raw materials in-transit	2,815,472	2,458,912	2,052,857
	₩ 25,527,202	₩ 24,985,767	US\$ 20,859,716

6. Investments in securities

Investments in securities (except investments in affiliated companies) at December 31, 2002 and 2003 consisted of the following:

Description	Investee	Korean won in thousands				Ownership
		Acquisition Cost Dec. 31, 2003	Net asset value Dec.31, 2003	Book value		
				Dec. 31, 2003	Dec. 31, 2002	
Held-to-maturity	Public bonds	₩ 777,165	₩ 777,165	₩ 777,165	₩ 753,775	-
	Fantagy CBO	₩ 200,000	₩ 73,960	₩ 73,960	₩ 129,310	-
	Hanvit CBO	₩ -	₩ -	₩ -	₩ 90,000	-
	Hanmaeum CBO	₩ -	₩ -	₩ -	₩ 101,710	-
		977,165	851,125	851,125	1,074,795	
Current Portion		₩ (9,615)	₩ (9,615)	₩ (9,615)	₩ -	
		967,550	841,510	841,510	1,074,795	

(Continued)

Description	Investee	Korean won in thousands				Ownership
		Acquisition Cost Dec. 31, 2003	Net asset value Dec. 31, 2003	Book value		
				Dec. 31, 2003	Dec. 31, 2002	
Avail-for-sales	Orion Reports Corp.	₩ 2,150,000	₩ 1,863,129	₩ 2,150,000	₩ 2,150,000	86.00%
	Orion Beverage Corp.	₩ 100,000	₩ 163,388	₩ 100,000	₩ 100,000	100.00%
	Korea Investment Corp.	₩ 58,800	₩ 18,522	₩ 18,522	₩ 12,642	0.08%
	Haitai Store Co., Ltd.	₩ 166,480	₩ 5,369	₩ 5,369	₩ 6,826	0.12%
	Orion Food (Rus) Co., Ltd	₩ 1,912,416	₩ 1,912,416	₩ 1,912,416	₩ -	100.00%
	Others	₩ 69,560	₩ 62,714	₩ 76,873	₩ 108,247	-
		₩ 4,457,256	₩ 4,025,538	₩ 4,263,180	₩ 2,377,715	
Total		₩ 5,424,806	₩ 4,867,048	₩ 5,104,690	₩ 3,452,510	

The 2003 impairment loss on the Fantasy CBO amounted to ₩55,350 thousand and 2002 impairment loss on Fantasy and Hanmaum CBO's amounted to ₩238,980 thousand. Because of the delisting of Chonggu Co., Ltd. ("Chonggu") from Korea Stock Exchange, Chonggu was reclassified as non-current securities and 2002 impairment loss on Chonggu amounted to ₩16,148 thousand. Orion Reports Corp. and Orion Beverage Corp. are small-sized companies with total assets less than ₩7,000,000 thousand as of December 31, 2002 and 2003, and therefore, the equity method of accounting was not applied.

The public bonds and investment bonds will mature as follows:

Year	Korean won in thousands	
	Public bonds	Investment bonds
2004	₩ 9,615	₩ -
2005 to 2009	710,385	73,960
2010 and after	57,165	-
	₩ 777,165	₩ 73,960

Investments in affiliated companies accounted for by the equity method at December 31, 2002 and 2003 consisted of the following:

2002	Korean won in thousands			Equity ratio [%]
	Acquisition cost	Proportionate share in net asset value or market value	Carrying value in balance sheet	
Orion Frito-Lay Corp.	₩ 2,703,346	₩ 29,298,985	₩ 26,672,537	50.00
Buy the way Inc.	25,393,012	24,853,787	24,821,130	54.59
Orion Food Co., Ltd.	11,370,316	15,207,753	15,174,202	80.26
Orion Food (Shanghai) Co., Ltd.	22,890,134	20,588,936	20,416,135	100.00
On Media Corp.	110,380,527	103,067,334	69,436,936	60.38
Zemiro Inc.	999,000	739,680	2,659	28.16
Mediaplex Corp.	17,999,000	29,043,592	28,973,921	89.99
riseON Inc.	32,754,002	32,786,254	30,445,381	100.00
	₩ 224,489,337	₩ 255,586,321	₩ 215,942,901	

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December 31, 2002 and 2003

2003	Korean won in thousands			Equity ratio (%)
	Acquisition cost	Proportionate share in net asset value or market value	Carrying value in balance sheet	
Orion Frito-Lay Corp.	₩ 2,703,346	₩ 33,492,477	₩ 30,866,822	50.00
Buy the way Inc.	25,393,012	26,038,078	25,969,079	54.59
Orion Food Co., Ltd.	11,370,316	16,015,443	15,988,698	80.26
Orion Food (Shanghai) Co., Ltd.	22,890,134	18,945,497	18,815,168	100.00
On Media Corp.	110,380,527	103,899,663	72,095,795	60.38
Zemiro Inc. (*)	999,000	-	-	-
Mediaplex Corp.	17,999,000	29,643,613	29,582,359	84.16
riseON Inc.	32,754,002	28,776,040	25,591,120	88.83
Tigerpoolsinternational Co.,Ltd	10,000,000	-	-	24.67
Sportstoto Co.,Ltd	30,000,000	-	41,322,327	48.16
	₩ 264,489,337	₩ 256,810,811	₩ 260,231,368	

(*) Zemiro Inc. was merged to riseON Inc. in 2003.

Investments in affiliated companies accounted for by the equity method at December 31, 2002 and 2003 consisted of the following:

2002	Korean won in thousands						Carrying value at Dec.31, 2002
	Carrying value at Dec. 31, 2001	Additional acquisition costs	Equity income (loss) on investments	Gain (loss) on valuation of investments	Retained Earnings	Dividends	
Orion Frito-Lay Corp.	₩ 22,603,066	₩ -	₩ 4,069,471	₩ -	₩ -	₩ -	₩ 26,672,537
Buy the way Corp.	21,230,605	393,012	3,198,927	(229,242)	227,828	-	24,821,130
Orion Food Co., Ltd.	11,034,049	4,598,463	823,238	(1,281,548)	-	-	15,174,202
Orion Food (Shanghai) Co., Ltd.	9,137,416	13,752,718	(1,263,600)	(1,210,399)	-	-	20,416,135
On Media Corp.	57,828,599	10,000,000	886,874	449,620	271,843	-	69,436,936
Zemiro Inc.	999,000	-	(996,341)	-	-	-	2,659
Mediaplex Corp.	12,426,982	8,000,000	5,908,339	2,638,600	-	-	28,973,921
riseON Inc.	-	32,754,002	(2,308,621)	-	-	-	30,445,381
	₩135,259,717	₩69,498,195	₩10,318,287	₩ 367,031	₩499,671	₩ -	₩215,942,901

(Continued)

2003	Korean won in thousands						
	Carrying value at Dec. 31, 2001	Additional acquisition costs	Equity income (loss) on investments	Gain (loss) on valuation of investments	Retained Earnings	Dividends	Carrying value at Dec.31, 2002
Orion Frito-Lay Corp.	₩ 26,672,537	₩ -	₩ 4,194,285	₩ -	₩ -	₩ -	₩ 30,866,822
Buy the way Corp.	24,821,130	-	1,147,949	-	-	-	25,969,079
Orion Food Co., Ltd.	15,174,202	-	841,665	(27,169)	-	-	15,988,698
Orion Food (Shanghai) Co., Ltd.	20,416,135	-	(1,235,310)	(365,657)	-	-	18,815,168
On Media Corp.	69,436,936	-	4,617,978	(1,230,995)	(728,124)	-	72,095,795
Zemiro Inc.	2,659	-	(2,659)	-	-	-	-
Mediaplex Corp.	28,973,921	-	(264,932)	902,230	(28,860)	-	29,582,359
riseON Inc.	30,445,381	-	301,303	(5,150,667)	(4,897)	-	25,591,120
TigerPools InternationalCo., Ltd.	-	10,000,000	(10,000,000)	-	-	-	-
Sports Toto Co., Ltd.	-	30,000,000	(27,885,976)	39,208,303	-	-	41,322,327
	₩215,942,901	₩40,000,000	₩(28,285,697)	₩33,336,045	₩(761,881)	₩ -	₩260,231,368

7. Property, plant and equipment

Changes in property, plant and equipment during 2003 and depreciation expenses for 2003 and 2002 are as follows:

	Korean won in thousands					
	Cost				Depreciation	
	Jan.1, 2003	Additions	Disposals	Dec.31, 2003	2003	2002
Land	₩ 103,834,433	₩ -	₩ -	₩ 103,834,433	₩ -	₩ -
Buildings	76,264,410	42,993	-	76,307,402	(2,345,352)	(2,569,274)
Structures	4,636,946	39,635	-	4,676,581	(203,070)	(246,560)
Machinery and equipment	139,694,820	6,294,535	(591,258)	145,398,097	(7,803,031)	(9,082,544)
Vehicles	10,128,629	2,257,805	(376,847)	12,009,588	(2,111,906)	(1,482,991)
Furniture and fixtures	23,868,720	2,272,054	(55,197)	26,085,577	(1,089,670)	(2,067,937)
Construction in-progress	11,974,631	4,130,212	(4,256,872)	11,847,972	-	-
	₩ 370,402,589	₩ 15,037,234	₩ (5,280,174)	₩ 380,159,650	₩ (13,553,029)	₩ (15,449,306)

Property, plant and equipment have been provided as collateral to the extent of ₩58,714,400 thousand and US\$40,937,000 (total US\$89,955,534) and ₩52,954,400 thousand and US\$40,937,000 (total US\$85,146,718) as of December 31, 2002 and 2003, respectively, in connection with short-term borrowings, long-term debt and bonds, and other current liabilities.

Property, plant and equipment are insured against fire and other casualty losses for up to ₩134,584,470 thousand (US\$112,359,718) as of December 31, 2003 (₩128,586,057 thousand as of December 31, 2002).

The value of the Company's land, as determined by the Government of the Republic of Korea for tax administration purposes, was ₩84,925,839 thousand (US\$ 70,901,602) as of December 31, 2003.

The Company leases certain machinery and equipment under operating lease agreements. A schedule of future minimum lease payments as of December 31, 2003 in connection with these leases is summarized as follows:

Year	Korean won in thousands	U. S. dollars (Note 2)
2004	₩ 370,267	US\$ 309,123
2005	277,701	US\$ 231,842
	₩ 647,968	US\$ 540,965

8. Assets and liabilities denominated in foreign currencies

Assets and liabilities (other than foreign convertible bonds, as noted in Note 10) denominated in foreign currencies as of December 31, 2002 and 2003 are summarized as follows:

	2002		2003	
	Foreign Currencies	Korean won equivalent (in thousands)	Foreign Currencies	Korean won equivalent (in thousands)
Assets:				
Cash and cash equivalents	US\$ 547,171	₩ 656,824	US\$ 785,452	₩ 940,815
Accounts receivable	US\$ 1,688,504	2,026,880	US\$ 982,826	1,177,229
		₩ 2,683,704		₩ 2,118,044
Liabilities:				
Accounts and notes payable - trade			US\$ 1,993,016	₩ 2,387,235
Short-term borrowings	US\$ 4,813,472	5,778,093	US\$ 3,088,662	3,699,599
	EUR 125,672	158,015	EUR 238,220	357,945
		₩ 5,936,108		₩ 6,444,779

9. Short-term borrowings

The Company borrowed operating funds of ₩46,101,226 thousand and ₩14,057,544 thousand (US\$11,736,136) as of December 31, 2002 and 2003, respectively, with annual interest rates ranging from 1.15% to 4.60%.

10. Long-term debt

Long-term debt as of December 31, 2002 and 2003 consisted of the following:

Bank	Korean won in thousands		U.S. dollars (Note 2)	Annual interest rate (%) as of Dec.31,2003
	2002	2003	2003	
Korean won denominated:				
KDB	₩ 9,375,000	₩ 16,875,000	US\$14,088,329	6.3~7.50
Kookmin Bank	20,695,288	20,691,799	17,274,836	3.0~7.50
Korea First Bank	17,000,000	17,000,000	14,192,687	7.1
Woori CLO	7,000,000	-	-	-
Hana Bank	10,000,000	10,000,000	8,348,639	6.98
CHB	10,000,000	20,000,000	16,697,278	5.99~6.23
	74,070,288	84,566,799	70,601,769	
Less current portion:	(9,503,490)	(32,506,475)	(27,138,483)	
	₩ 64,566,798	₩ 52,060,324	₩ 43,463,286	

Scheduled repayments of the above long-term debt outstanding at December 31, 2003 are summarized as follows:

	Korean won in thousands	U. S. dollars (Note 2)
2004	₩ 32,506,475	US\$ 27,138,483
2005	29,509,547	24,636,456
2006	11,887,713	9,924,623
2007	15,979	13,340
2008 and after	10,647,085	8,888,867
	₩ 84,566,799	US\$ 70,601,769

11. Bonds

Bonds (non-guaranteed) as of December 31, 2002 and 2003 consisted of the following:

Series	Korean won in thousands		U.S. dollars (Note 2)	Annual interest rate	Maturity
	2002	2003	2003		
58th	₩ 20,000,000	₩ -	US\$ -	8.00%	Mar. 26.2003.
59th	10,000,000	10,000,000	8,348,639	6.41%	Aug. 17.2004.
60th	5,000,000	5,000,000	4,174,320	7.05%	Aug. 28.2004.
61st	10,000,000	10,000,000	8,348,639	7.25%	Oct. 25.2004.
62nd	10,000,000	10,000,000	8,348,639	7.60%	Mar. 15.2005.
63rd	10,000,000	10,000,000	8,348,639	5.55%	Mar. 16.2005.
64th	10,000,000	-	-	5.67%	May. 9.2003.
65th	10,000,000	10,000,000	8,348,639	5.17%	May. 8.2005.
66th	5,000,000	5,000,000	4,174,320	7.35%	Aug. 22.2005.
68th	-	20,000,000	16,697,278	6.12%	Mar. 26.2006.
69th	-	10,000,000	8,348,639	6.21%	Apr. 28.2006.
70th	-	10,000,000	8,348,639	6.51%	May. 2.2006.
71st	-	10,000,000	8,348,639	6.14%	May. 9.2006.
72nd	-	10,000,000	8,348,639	6.20%	Jun. 13.2005.
73rd	-	10,000,000	8,348,639	6.15%	Sep. 30.2006.
Current portion	90,000,000 (30,000,000)	130,000,000 (24,989,610)	108,532,309 (20,862,924)		
Discount	(23,638)	(10,390)	(8,674)		
	₩ 59,976,362	₩ 105,000,000	US\$ 87,660,711		

The overseas bond with detachable warrants, denominated in U.S. dollars and with coupon interest rate of 3%, were issued in May 1999 to Euro market investors originally for the total amount of US\$ 15,000,000. The bond holders can exercise their warrants during the period from June 16, 1999 through April 30, 2004, at ₩23,232 per share of common stock, and starting on May 1, 2004, the holders may also ask the Company to redeem the bonds, with a guaranteed interest rate of 7.7%. The bondholders had exercised their put-option on May 31, 2000, and accordingly, the US\$15,000,000 was redeemed by the Company in full. In 2003, the bondholders exercised detachable warrants by acquiring common stocks amounting to US\$800,000 (US\$1,150,000 in 2002). Detachable warrants amounting to US\$10,500,000 (US\$11,300,000 as of December 31, 2002) remain outstanding as of December 31, 2003.

Scheduled repayments of the above bonds outstanding at December 31, 2003 are summarized as follows:

	Korean won in thousands	U. S. dollars (Note 2)
2004	₩ 25,000,000	US\$ 20,871,598
2005	45,000,000	37,568,876
2006 and after	60,000,000	50,091,835
	₩ 130,000,000	US\$ 108,532,309

12. Severance and retirement benefits

Changes in severance and retirement benefits for the years ended December 31, 2002 and 2003 are summarized as follows:

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Beginning of year	₩ 27,718,272	₩ 26,785,083	US\$ 22,361,899
Provision during the year	10,226,661	7,439,355	6,210,849
Transferred from affiliated companies	12,006		
Payments during the year	(8,880,784)	(7,231,363)	(6,037,204)
Transferred to affiliate due to spin-offs	(2,291,072)	-	-
End of year	₩ 26,785,083	₩ 26,993,075	22,535,544
Deposits for severance and retirement benefits	(16,073,541)	(16,195,845)	(13,521,327)
Accumulated prepayments to the KNPC	(868,057)	(583,074)	(486,787)
Net balance	₩ 9,843,485	₩ 10,214,156	US\$ 8,527,430

13. Commitments and contingencies

In 2000, the KT&G Corporation invested the amount of ₩26,000,000 thousand in Buy The Way INC. an affiliate of the Company. In relation to this investment, the Company made a commitment under a contract with KT&G, to redeem KT&G's investment in Buy The Way Inc. any time after 2004, at KT&G's option. Also the Company was contingently liable for payment guarantees totaling ₩14,400,000 thousand issued for issuing privately placed conversion bonds by Mediaplex Inc. from October 15, 2003 to October 15, 2005.

In 1995, the Company entered into a twenty-year royalty agreement, with S&A Restaurant Co., Ltd. for the operations of "Bennigan's" family restaurants in Korea. Under the agreement, the Company paid a lump sum royalty of US\$ 150,000 and is committed to pay running royalty at 2.7% of net sales of restaurant business from 1995. On September 30, 2002, the family restaurant division of the Company was spun off into a new company, which was incorporated as riseON Inc. The Company entered into a five-year royalty agreement with Orion Food Co., Ltd. for production, packing, distribution and sales.

The company maintains lines of credit in an aggregate amount of ₩50,000,000 thousand (US\$ 41,743,196) with various financial institutions at December 31, 2003 related to bank overdraft facilities. The Company has also entered into L/C opening and usance credit line with banks up to US\$19,600,000 and ₩4,000,000 thousand (US\$ 3,339,456).

14. Stockholders' equity

The ownership of the Company at December 31, 2003 is as follows:

Stockholder	Shares	Rate (%)
Hwa Kyung Lee	626,800	11.54
Chul Kon Tam	562,984	10.36
Arirang Fund	520,000	9.57
Others	3,722,526	68.53
	5,432,310	100.00

Changes in common stock and paid-in capital in excess of par value in 2002 and 2003 are as follows:

	Common stock	Paid-in capital in excess of par value
January 1, 2002	₩ 26,661,690	₩ 42,997,646
Change in 2002		
Exercise of stock warrants	294,790	1,072,251
	294,790	1,072,251
December 31, 2002	26,956,480	44,069,897
Change in 2003		
Exercise stock of warrants	205,070	745,900
	205,070	745,900
December 31, 2003	₩ 27,161,550	₩ 44,815,797

Paid-in capital in excess of par value and the asset revaluation surplus may not be utilized for cash dividends but may only be used to offset a deficit, if any, or be transferred to capital.

Appropriated retained earnings at December 31, 2002 and 2003 consisted of the following:

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Legal reserve	₩ 4,900,000	₩ 5,400,000	US\$ 4,508,265
Reserve for business rationalization	7,300,000	7,700,000	6,428,452
Reserve for financial position improvement	14,100,000	19,100,000	15,945,901
Reserve for additional equipment	23,000,000	35,000,000	29,220,237
Reserve for technology development	12,000,000	16,000,000	13,357,823
Voluntary reserve	18,000,000	25,000,000	20,871,598
	₩ 79,300,000	₩ 108,200,000	US\$ 90,332,276

The Company purchased 144,460 and 565,577 shares of treasury stock for the purpose of stabilizing the Company's stock price in 1996 and 2001 in accordance with the Korean Securities and Exchange Act. And the Company paid 100 shares for special bonus in 2003.

Legal reserve | In accordance with the Korean Commercial Code, an amount equal to at least 10% of cash dividends is required to be appropriated as a legal reserve until the reserve equals 50% of paid-in capital. The legal reserve may not be utilized for cash dividends but may only be used to offset a deficit, if any, or be transferred to capital.

Reserve for financial position improvement | The Korean Financial Control Regulations for listed companies require that an amount equal to at least 10% of net income, and 50% of net gain, if any, on disposal of property, plant and equipment, after deduction of any applicable tax, be appropriated as a reserve for financial position improvement until ratio of stockholders' equity to total assets equals 30%. At December 31, 2002, the Company's ratio of stockholder's equity to total assets was 47.0% [44.9% at December 31, 2002].

Reserve for research and manpower development | Under the TILL, the Company is allowed to deduct amounts provided as a reserve for research and manpower development from taxable income through appropriations of retained earnings. The reserve is added back to taxable income over three years after a two year grace period.

Voluntary reserve | The voluntary reserve including business expansion reserve is unrestricted.

Stock-option | In accordance with a resolution of the board of directors at their meeting held on January 31, 2002 and January 30, 2003, the Company adopted a stock option plan ("the Plan"), whereby 22,291 and 19,318 shares of common stock are reserved for issuance at ₩36,546 and ₩57,130 per share, respectively to certain officers of the Company. As defined in the Plan, the options are exercisable within seven years, starting from January 31, 2005 and January 30, 2006. The total compensation cost recognized in the income statement for stock-based employee compensation awards for the year ended December 31, 2003 amounted to ₩265,003 thousand (₩121,515 thousand in 2002).

The Black Scholes option | pricing model was used to value the stock option issued. Significant assumptions used to estimate the value of options are as follows:

	2002	2003
· Volatility	45.25%	47.34%
· Risk-free interest rate	7.11%	5.19%
· Dividend yield	1.36%	1.10%
· Expected rate of cancellation	7.15%	7.15%

15. Related party transactions

Transactions with related parties for the years ended December 31, 2002 and 2003 and outstanding balances as of December 31, 2002 and 2003 arising from such transactions are summarized as follows:

2002	Korean won in thousands				
	Sales	Purchases	Accounts receivable and prepayments	Accounts payable	Other
Orion Frito-Lay Corp.	₩ 1,266,964	₩ 96,262,813	₩ 146,161	₩ 22,338,236	₩ -
Orion Food Co., Ltd.	279,811	12,467,901	22,067	1,126,636	-
Buy the way Inc.	2,009,776	425,290	292,719	82,000	-
Orion Food (Shanghai) Co., Ltd.	58,910	856,867	4,104	295,001	-
riseON Inc.	-	-	-	-	87,020,625
	₩ 3,615,461	₩ 110,102,871	₩ 465,051	₩ 23,841,873	₩ 87,020,625

2003	Korean won in thousands				
	Sales	Purchases	Accounts receivable and prepayments	Accounts payable	Other
Orion Frito-Lay Corp.	₩ 1,046,005	₩ 106,716,612	₩ 195,778	₩ 25,278,028	₩ -
Orion Food Co., Ltd.	281,011	14,277,499	59,765	1,855,763	-
Buy the way Inc.	2,670,970	299,406	639,525	90,000	-
Orion Food (Shanghai) Co., Ltd.	74,596	3,727,762	25,024	531,471	-
	₩ 4,072,582	₩ 125,021,279	₩ 920,092	₩ 27,755,262	₩ -
	US\$ 3,400,052	US\$ 104,375,755	US\$ 768,152	US\$ 23,171,867	US\$ -

16. Income taxes

The Company is subject to corporate income taxes, including resident surtax, at the aggregate rates of 16.5% on taxable income up to ₩100,000,000 and 29.7% on taxable income in excess of ₩100,000,000. Effective from 2005, the aggregate tax rates will be reduced to 14.3% on taxable income up to ₩100,000,000 and 27.5% on taxable income in excess of ₩100,000,000. Reconciliation of income before income taxes for financial reporting purposes and taxable income for corporate income tax reporting purposes are summarized as follows (2003 amounts are preliminary and 2002 amounts are final based on the Company's corporate income tax return filed in March 2003):

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Income before income taxes per the accompanying statement of income	₩ 48,883,174	₩ 8,206,806	US\$ 6,851,566
Permanent differences:			
Taxes and dues	126,742	115,696	96,590
Entertainment expenses	10,307	86,499	72,215
Stock option	-	265,004	221,242
Valuation of equity method	531,066	-	-
Investments in securities	(1,586,669)	(761,881)	(636,067)
Other	311,910	-	-
	(606,644)	(294,682)	(246,020)
Temporary differences:			
Foreign currency translation loss	(325,209)	-	-
Allowance for doubtful accounts	929,437	(202,601)	(169,144)
provision for sales warranty	-	116,330	97,120
Reserve for technology development	2,000,000	(3,000,000)	(2,504,592)
Depreciation	482,553	673,648	562,404
Accrued interest income	195,471	27,622	23,061
Equity in come on investments in affiliates	(10,594,226)	28,285,697	23,614,708
Investments in securities	-	761,881	636,067
impairment of investment in securities	-	55,350	46,210
Other	71,584	48,223	40,260
	(7,240,390)	26,766,150	22,346,094
Taxable income	₩ 41,036,140	₩ 34,678,274	US\$ 28,951,640

NOTES TO FINANCIAL STATEMENTS

December 31, 2002 and 2003

Temporary differences vary between amounts shown on December 31, 2002 and January 1, 2003 due to adjustments after tax investigation by tax authorities.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for corporate income tax reporting purposes. Significant changes in cumulative temporary differences for the years ended December 31, 2002 and 2003 are as follows:

2002	Korean won in thousands		
	Opening balance	Net increase (decrease)	Ending balance
Temporary differences			
Foreign currency translation gains	₩ 325,209	₩ (325,209)	₩ -
Allowance for doubtful accounts	4,016,183	929,437	4,945,620
Accrued interest income	(231,080)	195,470	(35,610)
Reserve for technology development	(8,000,000)	2,000,000	(6,000,000)
Equity income on investment in affiliates	31,093,204	(10,849,353)	20,243,851
Depreciation	5,358,509	482,553	5,841,062
Provision for sales warrant	3,246,833	-	3,246,833
Other, net	866,047	326,712	1,192,759
	₩ 36,674,905	₩ (7,240,390)	₩ 29,434,515
Tax rate	29.70%		29.70%
Deferred income tax-asset	₩ 10,892,447		₩ 8,742,051

2003	Korean won in thousands		
	Opening balance	Net increase (decrease)	Ending balance
Temporary differences			
Allowance for doubtful accounts	1,876,611	(202,601)	1,674,010
Accrued interest income	(35,610)	27,622	(7,988)
Reserve for technology development	(6,000,000)	(3,000,000)	(9,000,000)
Equity income on investment in affiliates	20,243,851	29,042,271	49,286,122
Depreciation	5,840,995	673,648	6,514,643
provision for sales warranty	3,246,833	116,330	3,363,163
Other, net	1,192,758	103,573	1,296,331
	₩ 26,365,438	₩ 26,760,843	₩ 53,126,281
Tax rate	29.70%		28.10%
Deferred income tax-asset	₩ 7,830,535		₩ 14,947,338

The effective income tax rates for the years ended December 31, 2002 and 2003 are as follows:

	Korean won in thousands	
	2002	2003
Provision for (benefit from) income taxes	₩ 13,994,129	₩ 1,948,349
Income before income taxes	48,883,174	8,206,806
Effective income tax rates	28.63%	23.74%

17. Per share amounts

17-1. Per share amounts for the year ended December 31, 2002

The Company's basic and diluted EPS for the year ended December 31, 2002 were computed as follows (Korean won in thousands, except for per share amounts):

	Denominator			Numerator		Per share amounts	
	Share(A)	Number of days(B)	(A)x(B)/365	Net income	Ordinary income	Net income	Ordinary income
Net incom/ordinary income				₩34,889,045	₩34,889,045		
Basic EPS							
Beginning balance	5,332,338	365	5,332,338				
Exercise stock warrants	7,690	333	7,016				
	25,634	253	17,768				
	25,634	21	1,475				
Issuance of commom stock	(710,037)	365	(710,037)				
			4,648,560				
Income available common stockholders				₩34,889,045	₩34,889,045	₩7,505	₩7,505
Effective of dilutive securities							
non-exercise stock warrants	333,891	365	333,891				
exercise stock warrants	4,432	32	389				
	14,773	112	4,533				
	14,773	344	13,923	-	-		
Diluted EPS			352,736				
Income available to common stockholders+assumed exercision			5,001,296	₩34,889,045	₩34,889,045	₩6,976	₩6,976

17-2. Per share amounts for the year ended December 31, 2003

The Company's basic earnings per share ("EPS") for the year ended December 31, 2003 was computed as follows (Korean won in thousands, except for per share amounts):

	Denominator			Numerator		Per share amounts	
	Share(A)	Number of days(B)	(A)x(B)/365	Net income	Ordinary income	Net income	Ordinary income
Net incom/ordinary income				₩6,258,457	₩6,258,457		
Basic EPS							
Beginning balance	5,391,296	365	5,391,296				
Exercise stock warrants	15,380	198	8,343				
	25,634	190	13,344				
Issuance of commom stock	(710,037)	365	(710,037)				
	100	120	33				
			4,702,979				
Income available to commom stockholders				₩6,258,457	₩6,258,457	₩1,331	₩1,331

(Continued)

NOTES TO FINANCIAL STATEMENTS

December 31, 2002 and 2003

	Denominator			Numerator		Per share amounts	
	Share(A)	Number of days(B)	(A)x(B)/365	Net income	Ordinary income	Net income	Ordinary income
Effective of dilutive securities							
non-exercise stock warrants	356,085	365	356,085				
exercise stock warrants	10,173	167	4,654				
	16,956	175	8,130	-	-		
Diluted EPS			368,869				
Income available to common stockholders+assumed exercise			5,071,848	₩6,258,457	₩6,258,457	₩1,234	₩1,234

18. Dividends

Cash dividends for the year ended December 31, 2002 and 2003 are as follows:

<u>2002</u>	Outstanding shares	Dividend rates(%)(of par value)	Korea won in thousands
Accrued cash dividends	4,681,259	20%	₩ 4,681,259

<u>2003</u>	Outstanding shares	Dividend rates(%)(of par value)	Korea won in thousands	U.S. dollars (Note 2)
Accrued cash dividends	4,722,373	20%	₩ 4,722,373	US\$ 3,942,539

19. Segment information

The following table presents sales and other financial information by business segment for the years ended December 31, 2002 and 2003:

<u>2002</u>	Korean won in thousands		
	Product	Merchandise	Total
Net sales	₩ 336,839,297	₩ 192,081,414	₩ 528,920,711
Cost of sales	174,736,550	132,963,751	307,700,301
Gross profit	₩ 162,102,747	₩ 59,117,663	₩ 221,220,410

<u>2003</u>	Korean won in thousands		
	Product	Merchandise	Total
Net sales	₩ 294,401,253	₩ 217,035,419	₩ 511,436,672
Cost of sales	154,598,513	151,039,424	305,637,937
Gross profit	₩ 139,802,740	₩ 65,995,995	₩ 205,798,735

The Company's business is broken down into two segments: manufacturing and selling confectioneries and the family restaurant business. The sales from manufacturing and selling of confectioneries accounted for 91.3% of total sales for the years ended December 31, 2002, respectively. The family restaurant business was spun-off on September 30, 2002 as described in Note 20.

20. Added value information

The accounts and amounts which are required to be disclosed in connection with the calculation of the added value of the Company's operations for the years ended December 31, 2002 and 2003 are as follows:

	Korean won in thousands		U. S. dollars (Note 2)
	2002	2003	2003
Labor costs	₩ 83,103,489	₩ 74,476,449	US\$ 62,177,700
Severance and retirement benefits	10,226,661	7,439,356	6,210,850
Employee benefits	16,698,011	14,775,235	12,335,311
Rental expense	3,340,004	1,087,158	907,629
Taxes and dues	1,969,268	1,891,738	1,579,344
Depreciation	15,437,197	13,540,919	11,304,825
	₩ 130,774,630	₩ 113,210,855	US\$ 94,515,658

21. Spin-off

The family restaurant business division was spun off into a new company, which was incorporated as riseON Inc., a wholly owned subsidiary, as approved by stockholders' resolution at their meeting held on August 26, 2002. The opening balance sheet of riseON Inc. as of September 30, 2002 is as follows.

Assets	Korean won in thousands	Liability & Stockholder' equity	Korean won in thousands
Current asset:	₩ 20,234,454	Current liabilities	₩ 22,650,275
Quick assets	18,119,237	Non-current liabilities	31,616,348
Inventory	2,115,217	Total liabilities	54,266,623
Non-current assets:	66,786,171	Capital stock	5,412,000
Investments	19,500,953	Capital surplus	27,342,002
Property and equipment	47,039,018	Stockholder' equity	32,754,002
Intangible assets	246,200		
Total assets	₩ 87,020,625	Total liabilities and stockholders' equity	₩ 87,020,625

22. Subsequent events

In accordance with a resolution of the board of directors at their meeting held on January 30, 2004, the Company adopted a stock option plan ("the Plan"), whereby 21,407 shares of common stock are reserved for issuance at ₩78,400 per share to certain officers of the Company. As defined in the Plan, the options are exercisable within seven years, starting from January 31, 2007.

The company has issued non-guaranteed bonds on January 15, 2004. The bonds consisted of the following:

- Face value: ₩20,000,000 thousand
- Annual interest rate: 6.70%
- Date of issue: January 15, 2004
- Maturity: January 15, 2007

The Company infused a capital of ₩96,000,000 thousand to Sports Toto Co., Ltd. on February 19, 2004.

23. The Korean economy

In common with certain other Asian countries, the economic environment in the Republic of Korea continues to be volatile. In addition, the Korean government and the private sector continue to implement structural reforms to historical business practices including corporate governance. The Company may be either directly or indirectly affected by these economic conditions and the reform program described above. The accompanying financial statements reflect management's assessment of the impact to date of the economic environment on the financial position and results of operations of the Company. Actual results may differ materially from management's current assessment.

INDEPENDENT AUDITORS' REPORT



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The Stockholders and Board of Directors Orion Corporation

We have audited the accompanying balance sheets of Orion Corporation (the "Company") as of December 31, 2002 and 2003, and the related statements of income, appropriations of unappropriated retained earnings and cash flows for the years then ended, all expressed in Korean won. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the Republic of Korea. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above expressed in Korean won, present fairly, in all material respects, the financial position of Orion Corporation as of December 31, 2002 and 2003, and the results of its operations, appropriations of unappropriated retained earnings and cash flows for the years then ended in conformity with accounting principles generally accepted in the Republic of Korea.

As described in Note 15, the Company has had transactions with subsidiaries and affiliated companies.

As described in Note 21, effective September 30, 2002, the Company's family restaurant division ("Bennigan's") was spun off into a new company, which was incorporated as riseON Inc., a wholly owned subsidiary, as approved by the stockholders in a resolution passed at their meeting held on August 26, 2002. At the time of spin-off, the assets and liabilities of Bennigan's were ₩87,020,625 thousand and ₩54,266,623 thousand, respectively, and the excess of assets over liabilities amounting to ₩32,754,002 thousand was capitalized as common stock and capital surplus of riseON Inc.

As described in Notes 6 and 22, the Company acquired 24.67% of Tiger Pools International Co., Ltd. at ₩10,000,000 thousand and 48.16% of Sports Toto Co., Ltd. at ₩30,000,000 thousand in 2003. Subsequently, the Company put in additional investment of ₩9,600,000 thousand to Sports Toto Co., Ltd. on February 19, 2004.

As described in Note 22, on January 15, 2004, the Company issued non-guaranteed bonds at face value amounting to ₩20,000,000 thousand. Further, the board of directors resolved on January 30, 2004 that the Company adopt a stock option plan ("the Plan"), in which 21,407 shares of common stock are reserved for issuance at ₩78,400 per share to certain designated Company officers. As defined in the Plan, the options are exercisable within seven years, starting from January 31, 2007.

INDEPENDENT AUDITORS' REPORT

As described in Note 2, the Company adopted SKAS No. 4 in 2003, which requires the Company to recognize provision for loss on sales returns at the point of selling. Accordingly, the Company restated its 2002 financial statements. This change resulted in a decrease in 2003 net income by ₩116,000 thousand, with no effect on 2002 net income. The cumulative effect of this change as of December 31, 2001 was charged to 2002 beginning retained earnings, amounting to ₩2,283,000 thousand, net of applicable deferred income tax of ₩963,833 thousand. The Company also adopted SKAS No. 6 in 2003, which requires appropriations of retained earnings as of balance sheet date to be recorded after such appropriations are approved at the annual shareholders' meeting, which is normally held after balance date. The Company restated its 2002 financial statements resulting in a decrease in dividends payable as of December 31, 2002 by ₩4,681,259 thousand and an increase in retained earnings by the same amount.

We have also reviewed the translation of the 2003 Korean won financial statements mentioned above into United States dollar amounts on the basis described in Note 2. In our opinion, such statements have been properly translated on such basis.

Accounting principles and auditing standards and their application in practice vary among countries. The accompanying financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries other than the Republic of Korea. In addition, the procedures and practices utilized in the Republic of Korea to audit such financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report and the accompanying financial statements are for use by those who are knowledgeable about Korean accounting principles and auditing standards and their application in practice.

February 21, 2004

