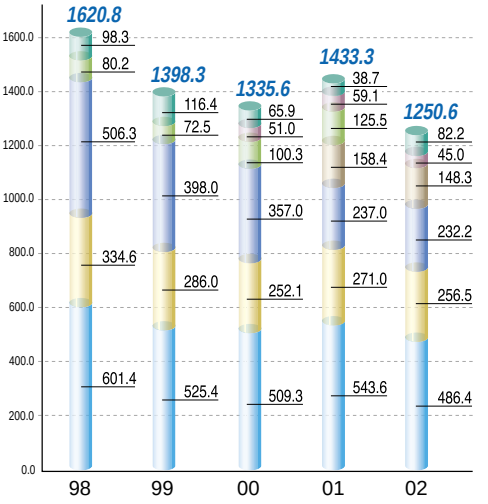
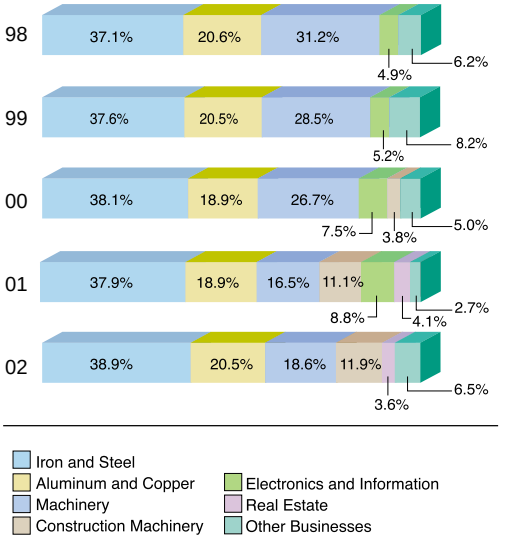
Review of Operations

Segment Sales (Billion ¥)
For the years ended March 31



Notes : These figures include inter-segment sales.

Segment Sales (%)



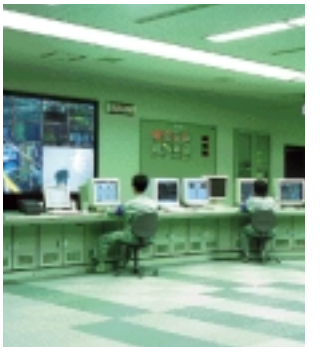
Iron and Steel Segment

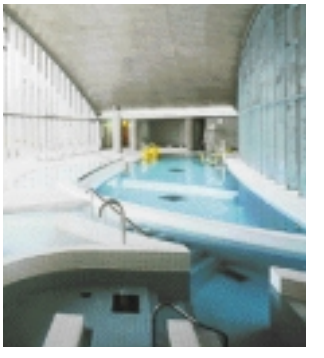
Steel demand slackened in the construction and manufacturing industries due to the sluggish economy and curbs on public-sector investment. In the first half of fiscal 2001, high levels of steel inventories led to a substantial decrease in sales prices. However, in the latter half of fiscal 2001, hefty production decreases brought about steady declines in inventories. The export market continued its downward trend, due to the slowdown in the U.S. economy and increasing market sentiment of a steel glut, but the market bottomed out in the second half of the fiscal year. Thus, prices began to rise toward the end of fiscal 2001 as progress was made in inventory adjustments and the world economy headed toward recovery.

Under these conditions, Kobe Steel was able to maintain its sales volume in exports and in the domestic market. However, worsening economic conditions in Japan led to price decreases, which pushed down steel sales from the previous fiscal year. Robust demand in shipbuilding since fiscal 2000 led to substantial increases in orders for cast and forged marine parts, including crankshafts, and sales soared in fiscal 2001 in comparison to the previous fiscal year. Sales of titanium products reached an all-time high, thanks to heightened demand in Japan from the electrical power, sports, and leisure industries, as well as in nearly all overseas markets. In steel powder products, the languishing North American economy led to market contraction and sales consequently went down. Sales of welding consumables increased, due to firm demand in Japan mainly in shipbuilding coupled with strong demand in Southeast Asia and China. As a result, Kobe Steel's Iron and Steel segment sales fell 10.5%, to ¥486.4 billion, and operating income dropped 75.8%, to ¥11.3 billion.

New Products

Kobe Steel is accelerating product development and application support to meet customers' needs. For the automotive industry, we developed a 100-kilogram class, high strength steel sheet, and leveraged our technologies, including processing, welding, and simulation technologies,





The No. 1 Power Plant at the Kobe Works went on stream in April 2002. The plant has the capacity to generate 700,000 kilowatts of electricity. Nadahama Garden Baden (*right*), a spa facility that utilizes thermal energy generated from the power plant, also opened in April 2002.

to offer improved customer support. For the electrical machinery industry, we commercialized a high-performance heat dissipating coated steel sheet called KOBEHONETSU*. And for the construction field, we introduced Eco-View, a long-life, weathering steel plate for painted bridges.

Kobe Steel undertook investments that sharpen its competitive edge in wire rod, plate and sheet production. We are also upgrading our No. 3 continuous caster at the Kakogawa Works to enhance the quality of a major product—high strength steel sheet.

Group Companies

We turned affiliate company Nippon Koshuha Steel Co., Ltd. into a subsidiary in April 2002, to increase the competitiveness of our bearing steel products, a cornerstone of our specialty steel business. In a move to bolster our wire rope business, the Kobe Steel Group became the main shareholder in Tesac Wirerope Co., Ltd. in April 2001. Furthermore, to become a full-service logistics company for distribution at our steel mills, we plan to combine Shinko Kakogawa Koun Co., Ltd. with Kobelco Logistics, Ltd. in October 2002.

Alliances and Ventures

We entered into an R&D agreement for automotive steel sheet technology with United States Steel Corporation in December 2000. In January 2002, we formed a cooperation alliance with Austria's voestalphine Stahl GmbH in automotive steel sheet technologies. Also in Europe, we formed a strategic global cooperation pact with the Lucchini Group in April 2002 for specialty steel wire rod and bar used in automotive applications. Through these alliances, we have positioned ourselves to serve the global procurement needs of the world automotive industry. Furthermore, PRO-TEC Coating Company in the United States is helping us expand our market share in automotive steel sheet. This joint venture with U.S. Steel is highly regarded in the automobile industry for its quality and technical expertise in hot-dip galvanized steel sheet and high strength steel sheet.

We have taken steps to improve our supply of steel powder in North America and Asia. Subsidiary Kobelco Metal Powder of America, Inc., increased its capacity in 2000, and began producing and marketing SEGLESS™, a graphite segregation-free steel powder, in 2002.

At affiliate Kobe Welding of Korea Co., Ltd., production lines were added, increasing capacity from 600 metric tons to 900 metric tons to meet the huge demand for flux-cored welding wire. Meanwhile, at our Thai affiliate, Thai-Kobe Welding Co. Ltd., a new technology department was established to improve technical services.

IPP Business

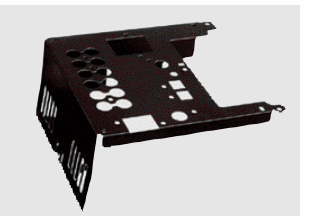
In our wholesale power supply business, the No.1 Power Plant of our Shinko Kobe Power Station began operating in April 2002. Construction of the No. 2 Power Plant is on schedule and the plant will go on stream in April 2004. With each facility having a generating capacity of 700,000 kilowatts, the two together will be able to produce 1.4 million kilowatts. This is expected to contribute substantially to the improvement of Kobe city's self-sufficiency rate for electricity, as well as contribute to our future profitability. As the power station is located in the city, careful consideration has been given to address environmental concerns. Our facility has environmental protection equipment that meets Japan's environmental standards.

We are also making the most of our existing infrastructure and production know-how in such areas as energy saving and disaster prevention functions, while contributing to local industries and community development.

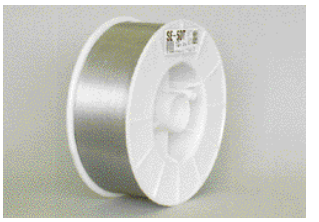
Outlook

In fiscal 2002, supply and demand conditions are expected to continue improving, and the domestic market is forecast to finally turn toward recovery. Nevertheless, conditions remain unpredictable. Steel price increases will be entering a crucial stage that requires a cautious balance with steel supply. Overseas supply is tightening up due to recovery in major markets, including the United States and Asia, and progress is being made in inventory adjustments. However, utmost caution must be exercised amid safeguard measures and other trade issues. The operating environment for cast and forged steel products is expected to be severe. Orders for crankshafts, which are traditionally strong performers, are anticipated to go down. However, demand for titanium products is bullish, while steel powder is expected to improve steadily.

Against this backdrop, we are endeavoring to increase steel prices as well as further expand sales of products in which we excel—specialty steel, steel plate for shipbuilding, high strength steel sheet, and welding consumables. We are moving forward with restructuring and cost-cutting measures, pursuing efficient R&D, and strengthening and enhancing overseas production. Together with our Group companies, we are further bolstering our competitive advantages and augmenting our market presence.



KOBEHONETSU* has seven times the heat dissipating capability of conventional electrogalvanized steel sheet. The new coated steel sheet helps disperse the heat generated by electrical devices and home appliances.



The SE Series of solid welding wires have no copper coating, making them environmentally friendly.

*"KOBEHONETSU" Japanese Trademark Application PND.

Aluminum and Copper Segment

In rolled aluminum products, demand for can stock was strong due to high summer temperatures, soaring sales of *happoshu*—a low-malt, beer-like beverage—and the increasing use of aluminum bottles. However, the stagnant IT market led to a substantial decline in demand for aluminum products used in semiconductor manufacturing equipment and office automation equipment. As a result, sales of aluminum products were down from the previous term.

Sales of rolled copper products also fell below that of the previous year. Shipments of copper strip for semiconductor leadframes declined in the IT slump, and domestic demand for copper tubing for air conditioners diminished as domestic air conditioner manufacturers increased overseas production.

Consequently, sales in the Aluminum and Copper segment declined 5.3 %, to ¥256.5 billion. Despite cost cutting measures, operating income fell 35.9 %, to ¥8.0 billion due to reduced sales.

Product Development

Our R&D activities are focused on the core products of aluminum can stock, aluminum fin material and copper tubing for air conditioners, and copper strip for automotive electrical terminals.

In addition, we are developing new products in the promising automotive, electronics, and information industries.

Products developed for the automotive industry include aluminum sheet with outstanding formability and corrosion-resistance properties for use in body panels, highly shock-absorbent extruded aluminum products for frames, extruded aluminum door beams, and aluminum forgings for suspension systems. We are leveraging our expertise in welding, surface treatment, structural analysis for parts design, and processing as well as working to establish low-cost, mass-production technologies to offer a wide variety of aluminum products to automakers in their quest to reduce vehicle weight.

For the electronics and information industries, we have been marketing high strength, high conductivity copper alloys for leadframes, copper alloys for electrical terminals in response to the rising use of electronic components in automobiles, and high-durability aluminum vacuum chambers used in semiconductor and LCD production. We are also aggressively focusing R&D on environmental solutions and have achieved success in reducing waste emissions and waste recycling.

For the past few years we have kept capital investment to a minimum due to sluggish market growth. However, we are increasing our production capacity for products in the automobile and semiconductor markets where medium-term growth is expected, while closely monitoring market trends. During the period under review, we increased production capacity for aluminum forgings for automobiles and aluminum materials used in semiconductor and LCD manufacturing equipment.

Overseas Activities

Our overseas development activities include promoting business development in Asia, where growth is expected mainly in IT industries. In fiscal 2001, we established Kobe Electronics Material (Thailand) Co., Ltd.—the first copper slitting company in Thailand—to meet anticipated semiconductor and automobile demand. In Singapore, we process and market copper strip and leadframes at Singapore Kobe Pte. Ltd. and Kobe Leadframe Singapore Pte. Ltd. Both companies are performing well and are meeting the needs of the promising Asian market.

We are restructuring operations with little synergy. We shut down Kobe Precision Parts (Malaysia) Sdn. Bhd., which processed parts for hard disk drives, and reduced our interest or sold our equity share in a number of aluminum resource projects. In our overseas operations, we are concentrating our management resources on our core business.

We supply can stock for aluminum bottles, which are growing in popularity. Easy to use, these containers are convenient and recyclable.

Aluminum forgings in suspension systems contribute to lighter cars. Demand for these and other aluminum products are expected to grow.

Outlook

The outlook for aluminum and copper product demand in fiscal 2002 is promising and we forecast improved results. Strong growth in aluminum can stock and a recovery in the IT market are anticipated to increase demand for aluminum sheet and extrusions as well as copper strip. However, copper tubing is expected to decline as manufacturers shift production overseas.

Over the medium term, we predict the use of aluminum materials—sheet, extrusions and forgings—will increase in automobiles. We also anticipate demand will rise for IT-related products such as copper strip for semiconductor leadframes and aluminum materials used in semiconductor and LCD manufacturing equipment. Aluminum in automobiles is especially promising as the use of this material gains momentum.

Under our medium-term management plan, promoting the use of aluminum in automobiles is a key strategy. We intend to meet the need for lighter cars by drawing on our technological prowess including our market-leading expertise in parts design. Our aluminum forgings for suspension systems are increasingly being used in cars. We aim to expand sales of aluminum sheet for body panels and other purposes, as well as extruded aluminum for bumpers and door guards.

In our existing operations, aluminum can stock growth has slowed in recent years due to the increasing use of PET bottles. However, PET bottles are being replaced by aluminum bottles and demand is expected to climb steadily. Like aluminum automotive parts, aluminum bottles are environment-friendly as they are easily recycled and demand is expected to increase significantly.

Looking to the future, we are applying our technological capabilities to create new markets. As a leading company in the aluminum and copper fields, we are further leveraging our international competitiveness in cost, quality and customer service.

Machinery Segment

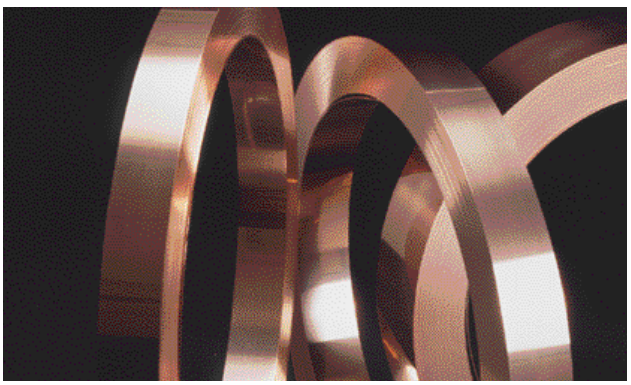
Orders declined considerably in our infrastructure and plant engineering business in fiscal 2001. The municipal solid waste treatment market shrank to one-third that of the previous term and demand in the overseas plant business was weak. In our machinery business, domestic demand for crushers and standard compressors remained sluggish. However, demand picked up for screw compressors—in particular gas turbine fuel gas compressors for IPP use—and optical fiber manufacturing equipment.

Overall orders in this segment fell 29.0%, to ¥166.7 billion. Despite a surge in orders for municipal solid waste treatment plants in the previous term, Machinery segment sales slid 2.0%, to ¥232.2 billion, due in part to lower sales from subsidiaries. However, operating income rose 120.1%, to ¥3.7 billion, reflecting effective overall cost reductions.

Environmental Solutions

Japan is striving to become a recycling society and has implemented new recycling laws. In addition to the prevailing waste treatment methods—incineration and burial—such non-incineration methods as reuse and recovery are increasing in importance.

The Company established the Environmental Solutions Department in fiscal 2001 to expand its activities beyond solid waste and wastewater treatment processes. This department is developing businesses and technology for treating and recycling waste products including used home appliances, end-of-life vehicles, used polyvinyl chloride, and organic wastes. Soil remediation is another area of our environmental restoration activities. As the effective use of generated energy becomes increasingly important in waste treatment, we are stepping up efforts to integrate technologies in the environmental and energy fields.



We have developed high strength, high conductivity copper alloys for terminals, connectors, and semiconductor leadframes.

The ITmk3® Process produces high quality iron nuggets, while emitting 20% less carbon dioxide than blast furnace operations. The photo shows the bench-scale plant at the Kakogawa Works.

We already have a strong track record in the soil cleanup business. We are one of 15 founding member companies of the Japan Earth Environment Examination Purification Union. The purpose of this organization is to foster information exchange and know-how on soil remediation with different industries to improve treatment technologies for such pollutants as volatile organic compounds and heavy metals.

Engineering Opportunities

In the energy field, we have focused our lineup on liquefied natural gas (LNG) vaporizers and reactors. We are aggressively expanding our activities to include LNG satellite bases, LNG receiving terminals, and cogeneration facilities.

We are actively promoting our core direct reduced iron processes. In addition to the highly successful MIDREX® Direct Reduction Process, we are marketing the FASTMET® Direct Reduction Process. In the United States, we are building a demonstration plant for the ITmk3® Process, a next-generation ironmaking technology, in anticipation of bringing the process to a commercial level of operation.

New Machinery Markets

In the machinery business, we substantially improved the energy-saving function of our screw compressors with the development of compressors driven by internal permanent magnet motors. In addition, we are striving to not only strengthen our existing product lineup for the environmental and energy industries, but also create new products for new markets.

Overseas, in fiscal 2000 we set up Kobelco Compressors (Shanghai) Corporation as the Chinese base for our standard compressor operations and have since established Kobelco Compressors (Tianjin) Corporation to market and service standard compressors in northern China.

Amid an increasingly harsh market environment and intensifying competition, the Company is boosting the value of its products and technologies to improve its competitive edge, while actively pursuing businesses in the growing environmental and energy fields. The Company is also investing its energies in expanding its business by creating new product menus, developing new types of machinery, and entering new markets. Through business and technology, the Company is actively contributing to lessening the burden on the environment and creating a recycling society.

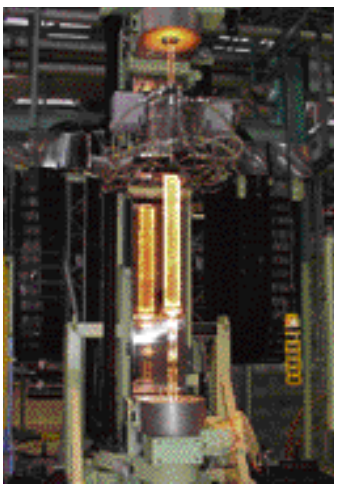
Construction Machinery Segment

Domestic demand for construction equipment declined significantly due to slumping orders for public works, weak private-sector construction, and lower capital investment from equipment rental companies. Overseas, demand for construction equipment in Europe and the United States leveled off, but increased nearly 50% in China in fiscal 2001. Southeast Asia also showed signs of recovery. Nevertheless, these increases were not enough to offset the slack demand in Japan, Europe, and the United States. As a result, segment sales fell 6.4%, to ¥148.3 billion, and operating income dropped 64.3%, to ¥1.9 billion.

New Products and Attention to Cost

Under these conditions, Kobelco Construction

This screw compressor with a high-speed (7,200 RPM) IPM motor features increased airflow and a variable speed drive.



Shipments of optical fiber drawing towers have been strong in recent years. In the future, we aim to market a full lineup of products to cover the entire process, from raw material preform rods to optical fiber drawing towers to post-process products.

Machinery Co., Ltd., which runs Kobe Steel's construction equipment operations, is focusing on its stock business, which includes used equipment sales, parts, and maintenance services. Kobelco launched new flagship products – the SR Series and Dynamic Acera Series of hydraulic excavators with improved features to handle exhaust emissions – and is also targeting the recycling market.

To further reduce operating costs, Kobelco consolidated crane production. The Company has also reorganized and integrated excavator and crane sales and service operations. To increase operational efficiency, it revised development processes, shortened lead times, and improved distribution.

Global Alliances

In January 2002, Kobe Steel and Kobelco completed a global alliance with CNH Global N.V. of the Fiat Group. With this partnership, Kobelco acquired all of CNH's construction equipment operations in Oceania, Southeast Asia, and China as well as obtained exclusive distribution rights for CNH's construction equipment in these geographical areas. The alliance enables Kobelco to become a full line supplier of construction equipment in Japan and the Asia-Pacific region, with the ability to meet a broader range of customer needs. In the period under review, CNH acquired 10% of Kobelco's issued stock, which later increased to the current 20%, as well as 65% of the issued stock of Kobelco's subsidiary, Kobelco Construction Machinery America LLC.

Kobelco also began producing and marketing equipment in collaboration with Tadano Ltd. and entered into a marketing alliance for road equipment with BOMAG of Germany as part of a concerted effort to broaden its product menu.

The 200SR is one in a series of excavators with zero tail swing. We pioneered this space-saving features now found in both mini excavators and excavators.

Overseas Business

Kobelco leveraged the weaker yen to increase sales in Europe and the United States. Kobelco Construction Machinery America LLC in the United States launched a new series of hydraulic excavators and introduced crawler cranes designed for the North American market as part of an aggressive effort to boost sales. However, the slowdown of the U.S. economy precipitated by the September 11 terrorist attacks led to reduced sales and profits in the period under review.

For the Netherlands-based Kobelco Construction Machinery (Europe) B.V., the weaker yen and efforts to form an integrated sales structure with dealers in Europe resulted in higher sales, but profits were down.

Marketing company Kobe International (S) Co., Pte. Ltd. established a used equipment center in the latter half of fiscal 2001 to strengthen the stock business, but sluggish demand for new equipment led to a decrease in sales and profits.

Kobelco was actively involved in China's rapidly expanding market. At Chengdu Kobelco Construction Machinery, Co., Ltd., market expansion and heightened demand coupled with the introduction of new equipment led to higher sales and profits.

In Thailand, Thai Kobelco Construction Machinery, Ltd. (TKCM) also saw high sales and profits. In addition to excavator production and marketing, TKCM became a production base for parts and components, with an expanded menu for these products.

Looking Ahead

Kobelco is moving forward with the worldwide business development of its excavator operations. The global alliance with CNH is facilitating a smooth startup of Fiat Kobelco Construction Machinery S.p.A, a production base in Europe, as well as the launch of new products in the domestic market.

In the crane business, Kobelco is maximizing the benefits of its production tie-up with Tadano. Overseas, Kobelco is focusing on expanding sales, especially in North America, the biggest market for crawler cranes, and in China where growth continues to be strong.

Real Estate Segment

Despite such stimulus measures as an extension on housing tax breaks and continued low interest rates, new housing starts fell and the real estate market remained difficult. Against this backdrop, the Kobe Steel Group made strong efforts to increase sales, but lackluster domestic consumption due to the stagnant economy, lower real estate prices due to significant drops in land prices, and changes in the types of real estate on the market—in particular an increase in high-priced properties—led to a 23.7% drop in sales, to ¥45.0 billion. Operating income fell 41.6%, to ¥8.0 billion, primarily due to changes in the types of property sold.

Focus on Regional Development

Through affiliate Shinko Kosan, Ltd, the core of our real estate business, we steadily expanded our activities to cover real estate sales, rental and leasing, brokering, renewal activities, and building management. Our Land Development Department in Kobe Steel has been using company landholdings, including unused factory land, to promote urban development, condominium sales, and property rental and leasing.

A case in point is our ongoing development of O's Town, a vast housing and commercial complex in Akashi, Hyogo. We are also selling condominiums in the Tokyo metropolitan area and in Kobe, primarily at Maya Seaside Place—a condominium project in the new city center in eastern Kobe.

Development is progressing at O's Town, a large-scale complex with a mix of housing and commercial facilities in the Okubo area of Akashi, Hyogo Prefecture. Approximately 1,500 families have moved into condominiums since their completion in March 1997.

In our leasing operations, we have new property in the Osaka-Kobe area including a commercial establishment and an employee dormitory. Construction work includes such projects as the Hyogo Prefectural Museum of Art in the new city center in eastern Kobe. The Company also provides building management for Kobe Wing Stadium, which was used in the 2002 FIFA World Cup™, and a university in Hyogo Prefecture.

Merging Real Estate Operations

We anticipate conditions in the real estate business will intensify and land redevelopment projects will increase in scale. For these reasons, we absorbed affiliate Shinko Kosan, Ltd. into Kobe Steel on March 1, 2002. We concluded that merging our operations is the best way for our real estate business to continue growing in future years.

Other Businesses Segment

A total of 33 subsidiaries and eight affiliates are engaged in this segment covering such fields as electronics-related equipment, IT systems, superconducting products, specialty alloys and other new materials, information services, materials inspection, pressure vessel fabrication, trading, and travel services.

Segment sales dropped 49.6%, to ¥82.2 billion, and operating income fell 96.9% to ¥900 million, owing mainly to the sale of a semiconductor subsidiary.