

Message from the President

Economic conditions in the first half of fiscal 2002 continued to be difficult. Although exports to Asia increased, domestic personal spending and capital investment were weak as deflationary pressures mounted.

In our business operations, steel, aluminum, and copper sales were dampened due to the slumping domestic economy. However, machinery sales were firm and the start-up of a power plant in our IPP (independent power producer) business also bolstered sales. As a result, consolidated net sales totaled ¥577.4 billion, dipping 0.1% from the same period last year. Overall cost reductions enabled operating income to rise 126.3% to ¥34.5 billion, while net income increased to ¥5.2 billion, versus a loss for the same period last year.

Iron and Steel

Japan's production of crude steel rose over the same period last year. Although severe conditions persisted amid low capital investment and construction, overseas demand particularly in Asia recovered and led to a rise in exports. In addition, a sharp decrease in inventories tightened the market. However, sluggish domestic demand resulted in lower steel sales. Sales also went down in our welding business. While exports mainly to Asia were strong, domestic demand in the construction industry was sluggish.

Conversely, sales were up for marine castings and forgings and titanium products for power and desalination plants. The start-up of our power plant in the IPP business also contributed to overall sales. As a result, segment sales rose 4.5% to ¥252.5 billion, while operating income increased 178.3% to ¥21.3 billion.

Aluminum and Copper

Shipments of rolled aluminum products went up due to a rising demand for bottle cans and an increase in aluminum plate used in semiconductor manufacturing equipment. Aluminum extrusions for the automotive market were also firm, leading to higher overall aluminum sales over the same period last year.

Shipments of rolled copper products also increased. Copper strip rose due to a recovery in IT demand, leading to higher overall copper sales over the same period last year. However, domestic air conditioner makers continued to shift production overseas, lowering domestic demand for copper tube.

Higher aluminum and copper shipments were offset by low raw material prices, leading to a 3.4% decrease in segment sales to ¥128.1 billion. However, cost reductions and the strong performance of overseas subsidiaries contributed to a 36.2% increase in operating income to ¥6.4 billion.

Machinery

Domestic orders decreased 34.3% to ¥52 billion due to a sharp drop in orders for municipal solid waste treatment plants. Overseas orders for equipment for the nuclear power industry and rotating machinery were firm, leading to a 40.5% increase to ¥14.9 billion. Total orders decreased 25.5% to ¥67.0 billion and the backlog of orders was ¥170.8 billion.

Previous years' orders for solid waste treatment plants resulted in a 4.7% increase in segment sales to ¥98.4 billion. Operating

income was ¥141 million versus a loss in the same period last year.

Construction Machinery

Demand for construction equipment in Japan went down sharply due to curtailed public works and low capital investment. While orders in North America and Europe were sluggish, the Chinese market was strong and Southeast Asian demand was on a recovery path. As a result, segment sales were flat at ¥73.3 billion and operating income rose 30.2% to ¥1.5 billion, in comparison to the same period last year.

Real Estate

Despite low mortgage rates and the extension of tax breaks for new homes, housing starts are anticipated to fall for three consecutive years. Segment sales went down 32.2% to ¥15.8 billion. Operating income decreased 46.8% to ¥2.0 billion. Factors include weak consumer interest, low real estate prices, and the higher number of housing sales in the same period last year.

Other Businesses

In fiscal 2001, the partial equity transfer of an information system subsidiary led to a 35.6% decrease in segment sales to ¥25.5 billion. Operating income rose sharply to 2.2 billion owing to improved performance in a semiconductor inspection subsidiary.

Corporate Highlights

A new, strategic area is our IPP business. The No. 1 Power Plant of our Shinko Kobe Power Station began commercial operation in April 2002. A second power plant currently under construction is to start up in April 2004. At that time the power station will have a combined capacity to generate 1.4 million kilowatts and will boost Kobe City's self-sufficiency for electricity.

Looking at the second half of the fiscal year, conditions will be increasingly severe. In these difficult times, we further strengthened our ties with Nippon Steel Corporation and formed an alliance with Sumitomo Metal Industries, Ltd. in November 2002. In this three-way alliance, the companies intend to take an equity share in each other. Going one step further, we anticipate higher efficiencies and cost reductions in our Iron and Steel business that will contribute to greater profitability.

We are accelerating the selection and consolidation of our businesses to implement change and improve our financial performance. We are building a stabler profit base, working to eliminate undisposed deficits, and decreasing our interest-bearing liabilities.

As we become a stronger and more profitable company, we thank you for your understanding and ask for your continued support.

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Koshi Mizukoshi
President and Chief Executive Officer