

Message from the President

Japan's economy continued to improve in the first half of fiscal 2005, ended September 30, 2005. Demand in capital investment and personal spending was robust owing to higher corporate profitability. In addition, the U.S. and Asian economies, including China, continued to be strong.

On this background, Kobe Steel's consolidated net sales rose ¥104.8 billion to ¥789.5 billion, in comparison to the same period last year. Operating income increased ¥40.8 billion to ¥108.2 billion, and pretax ordinary income went up ¥40.3 billion to ¥85.4 billion. Kobe Steel took an extraordinary loss on the separation of the real estate business from the parent company, effective October 1. The loss arising from a fire at Kakogawa Works in May was also taken as an extraordinary loss. This led to aftertax net income of ¥36.7 billion.

<Net Sales>	(billions of yen)		
	FY2005 First Half	FY2004 First Half	%
Iron & Steel	366.4	294.0	24.6%
Wholesale Power Supply	31.0	27.5	13.0%
Aluminum & Copper	152.4	145.9	4.4%
Machinery	113.8	91.9	23.8%
Construction Machinery	106.4	106.6	(0.2%)
Real Estate	17.2	16.9	1.9%
Electronic Materials & Other Businesses	28.2	25.3	11.5%
Eliminations	(26.0)	(23.4)	-
Total	789.5	684.7	15.3%

<Operating Income>			
	FY2005 First Half	FY2004 First Half	%
Iron & Steel	69.0	34.9	97.5%
Wholesale Power Supply	8.3	9.6	(13.5%)
Aluminum & Copper	12.2	8.5	44.3%
Machinery	3.1	0.2	1,369.7%
Construction Machinery	3.6	4.4	(17.6%)
Real Estate	1.4	1.7	(17.0%)
Electronic Materials & Other Businesses	8.5	6.5	31.2%
Eliminations	2.0	1.6	-
Total	108.2	67.4	60.6%

Iron & Steel

Domestic steel demand for medium- and high-grade steel products, used mainly in the automotive and shipbuilding industries, was quite strong in the period under review. However, the supply-demand balance worsened as market conditions for general steel products weakened due to China's rising crude steel capacity, leading to a softening in the market. To maintain export prices in this situation, Kobe Steel decreased shipments of steel products, although overall shipments rose over the same period. Kobe Steel was able to steadily increase steel prices owing to the tight supply-demand situation for medium- and high-grade steel products.

Domestic demand for welding consumables was firm mainly in the automotive and shipbuilding industries. Overseas, demand from the automotive and shipbuilding industries and energy projects was strong.

As a result, segment sales increased 24.6% to ¥366.4 billion, and operating income increased by ¥34.1 billion to ¥69.0 billion.

Wholesale Power Supply

Segment sales rose 13.0% to ¥31 billion owing to an increase in the electricity price due to the rise in coal prices. Due to equipment inspection to maintain stable operation, operating income decreased by ¥1.3 billion to ¥8.3 billion.

Aluminum & Copper

Shipments of rolled aluminum products decreased over the same period last year. Domestic sales volume increased owing to higher shipments of aluminum can stock, a major product, due to further use in aluminum bottle cans, but exports fell considerably, which led to a decrease in overall can stock shipments. Due to higher demand in the previous year's summer season for aluminum fin stock used in air conditioners, shipments of fin stock decreased in the half-year period. Demand for aluminum extrusions was also weak.

Demand for rolled copper products was similar to the same period last year. Copper strip for automotive terminals continued to be strong, but strip for semiconductors entered an adjustment phase. Demand for copper tube for air conditioners decreased in the first half of fiscal 2005, a reaction to the hot summer last year, and exports also fell.

Although sales volume decreased, higher ingot prices and an improvement in the product mix enabled segment sales to increase 4.4% to ¥152.4 billion. Operating income increased ¥3.7 billion to ¥12.2 billion.

Machinery

Domestic orders increased 3.6% to ¥68.5 billion due to a rise in standard compressors used in capital investments. Overseas orders rose 32.8% to ¥41.8 billion. Orders were strong for non-standard rotating machinery used in the energy, petroleum and gas industries, as well as for tire machinery. Orders from the energy field for such products as pressure vessels were also robust. As a result, total orders increased 13.0% to ¥110.3 billion, and the backlog of orders was ¥244.7 billion.

Owing to strong orders, machinery segment sales went up 23.8% to ¥113.8 billion in the half-year period. Operating income increased ¥2.9 billion to ¥3.1 billion.

Construction Machinery

The Japanese market for construction machinery was strong due to the rise in capital investment and reduced inventories in Japan brought about by high exports of used machines. Overseas, Indonesia entered an adjustment phase, but demand in Southeast Asia was firm. Europe and North America were on an expansion trend, and the falling Chinese market had bottomed out. As a result, overall demand for construction machinery was firm.

Although the demand environment was in general favorable, the downturn in the Chinese market had a considerable effect. As a result, construction machinery sales dipped 0.2% to ¥106.4 billion, and operating income went down ¥0.8 billion, versus the same period last year, to ¥3.6 billion.

Real Estate

The number of new condominiums sold in the Tokyo metropolitan area gradually increased owing to the improved economy. However, in the Osaka metropolitan area, the number of units sold was flat.

As the number of housing starts and property handovers were low, segment sales were flat at ¥17.2 billion. Operating income went down ¥0.3 billion to ¥1.4 billion.

Electronic Materials & Other Businesses

Due to continued strong demand for target material used in LCDs, segment sales increased 11.5% to ¥28.2 billion and operating income rose ¥2.0 billion to ¥8.5 billion.

Outlook

In the second half of the fiscal year, Japan's economy is forecast to continue on an expansion trend. Although there is concern over a slowdown in the U.S. economy and rising inflation brought about by rising oil prices, domestic capital investment and personal spending are expected to be strong.

In the Kobe Steel Group's Iron & Steel segment, although the market for general steel products is expected to continue being soft, demand for medium- and high-grade steel products from domestic manufacturers is forecast to be robust. In the Machinery segment, orders for compressors, rubber and tire machinery, and energy-related equipment are also anticipated to be firm. Based on these business conditions, Kobe Steel is growing its "Only One, Number One" distinctive products and implementing strategic capital investments that will enable it to further improve its business competitiveness.

On September 1, 2005, Kobe Steel marked its centennial anniversary. Looking at the next 100 years, we are focusing on manufacturing. With an unquenchable spirit, we will continue to supply high-quality products and services that meet the numerous needs of our customers and aim to further raise our corporate value.

December 2005



Yasuo Inubushi
President and CEO

(* Ordinary income is operating income after adjustments of net financial revenue and net expenses generated on a regular basis, including seconded employees' salaries net of reimbursement.)