



From left: Hideki Yamamoto, Chairman, Masamichi Takemoto, President

The “Muscle Plan” Halts Performance Decline

Although the operating environment during fiscal 2003, ended March 31, 2003, was affected by an array of negative factors, including a worldwide decline in stock prices, sluggish consumer spending and protracted deflation in Japan, Nitto Denko Corporation and its consolidated subsidiaries nevertheless made solid advances in performance by aggressively focusing business activities on growth industries. Net sales were up 11.7% from the previous fiscal year, to ¥378,705 million, and operating income rose 75.5%, to ¥33,902 million.

The decline in results, considered unavoidable in light of the difficult fiscal 2003 operating conditions, unexpectedly turned into a V-curve recovery. This pleasant surprise is unquestionably traceable to the introduction of the *Muscle Plan*. Fortunately, the measures we took to maintain the Company’s profit-making capability were launched at an early stage before the downside could gather momentum. If it had not been for the nearly ¥9,000 million cutback of fixed costs, the Company may well have been driven into dire straits. Another major benefit reaped through the

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Management Plan

1 Muscle Plan

In fiscal 2002 the Nitto Denko Group experienced an unprecedented decline in results triggered by cataclysmic market changes. In light of the new market realities, the Company decided that it urgently needed to reform corporate essentials so that profits could be maintained, even if at the cost of some decrease in production. The G-2002 Mid-Term Management Plan was frozen and the Muscle Plan implemented as a program focused on carrying out a productivity reform by March 2003.

Target ▶▶▶

Cut annual fixed costs around ¥9,000 million by achieving every reform goal with regard to the three productivity aspects of manufacturing, distribution and head office administrative functions.

▶ Domestic manufacturing fixed costs

In April 2002, the Kyushu Plant was spun off and a personnel cutback initiative was implemented that allowed freedom in deciding the number of personnel at any given site.

▶ Total operating expenses

Work was started to unify Group distribution, chiefly through the establishment of SCM centers.

▶ Administrative support fixed costs

A reassessment of administrative services from the ground up was carried out and work begun on eliminating those functions determined to be redundant or unnecessary.

improvement of corporate essentials under the Muscle Plan was the instilling of a fresh “we can build a strong Nitto Denko” mentality among employees.

As the year progressed, results seemed almost too good during the first quarter, only to hit rock bottom during the second. The third quarter was expected to follow on the heels of the second, but in fact, turned in a strong performance in the medical and membrane sectors, with firm underpinning from tapes and semi-conductors. During the fourth quarter, the sharp rebound in the LCD-related products optical sector was particularly notable.

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Fiscal 2004: Training Camp for the Next Big Advance

To use a baseball metaphor, fiscal 2003, the year the Muscle Plan was introduced, was an individual training period preceding the start of group training camp in fiscal 2004 (from April 1, 2003 to March 31, 2004). The first year of the Muscle Plan, 2003, was used to build up basic strengths, while 2004 will be a period for choosing the lineup and preparing for the long pennant race. It will be a time for deciding what products and business sectors will play the

role of the cleanup hitters for pushing up business results and which products will serve as the starting pitchers, middle relievers, closers. We plan to continue this optimization of player deployment based on careful analysis of the product and business sectors currently making the biggest contributions and those we expect to be the star performers five years from now. We see the *New Mid-Term Management Plan* being launched in fiscal 2004 as a three-year plan envisioning Nitto Denko in five years. The primary focus is on how strong a team can be built over the next three years. Fiscal 2004 will be a training camp period for transforming Nitto Denko into a company ready to take on world-class competitors.

The first stage of the Muscle Plan provided the Company’s individual groups with a muscular organizational alignment centered on the production divisions. But from the viewpoint of the Company as a business group, Nitto Denko has by no means yet attained muscularity. In carrying out the second stage, muscle building will equate to enhancing the functionality of the head office and the productivity of the marketing, distribution and R&D segments. The Muscle Plan represents a perpetually continuing

2 New Mid-Term Management Plan (April 2003 to March 2006)

New Mid-Term Management Plan target: Establish double the lineup of global niche top products and a singular corporate culture by promoting Group management unhindered by national borders or organizational barriers.

Chief Measures ▶ ▶ ▶

Creation of global niche top businesses

- ▶ Building of a sales and marketing system in China
- ▶ Business expansion in the United States and Europe
- ▶ Strengthening R&D capability
- ▶ Creation of new businesses through industry-government-academic collaboration
- ▶ Reformation of harvest business profitability

Establishing the One-NITTO culture

- ▶ Simplification of Group structure

Realization of speedy management and business execution

- ▶ Entrenching of governance system and separation of managerial and executive functions
- ▶ Revising management decision-making system

Performance Plan

	FY2003	FY2006
Operating income	¥33,902 million	¥55,000 million
Operating income ratio	9%	12%
ROA	9%	15%

process to be relentlessly pursued till it becomes a new segment of the Nitto Denko DNA.

Against this backdrop, our goal in fiscal 2004 is to shift to new growth strategies. At Nitto Denko, the key to offering customers the products they really want and need has always been to stay at the customer's side and listen carefully. This basic growth strategy will now be played out on the global stage. And the process will involve not only new products from Japan but also new offerings from all over the world. Around the globe, we intend to exploit every burgeoning bud showing promise for growth as the Company moves forward under the new 2004 banner of "Double the Lineup of Global Niche Top Products - Grow to the Next Stage through Rapid Evolution and Deepening Technology."

Transformation Phase 5: Globalization

The Nitto Denko Group has gone through four major transformations in response to changing market realities. The first phase was "business diversification," the second "overseas expansion" of manufacturing operations, the third "re-focusing on manufacturing

businesses," and the fourth "building a technology-oriented company," all of which ran in parallel with the Company's global niche top strategy. The Company is currently moving into a fifth phase of globalization. This will involve broadening Nitto Denko's field of vision beyond just Japanese and Japanese-owned businesses to encompass businesses in Europe, North America and Asia. Increasingly, new approaches to business will emerge from groups in countries all over the world, including Japan, and be implemented by all groups in concert. The search for new ideas and technologies for transforming area niches into global niches will be intensified.

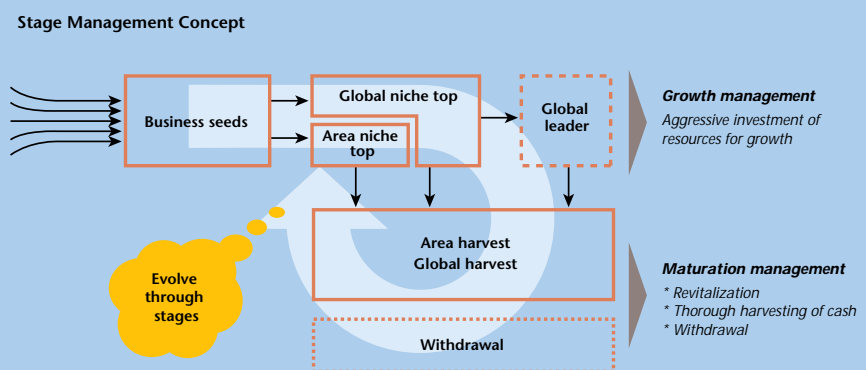
Over the course of five years, some products are certain to become prime candidates for withdrawal owing to changes in global practices and product needs. The Company must be prepared to make product tradeoffs. The importance of accurately assessing product and technology life cycles can be expected to increase. For this, the Nitto Denko Group will introduce *Stage Management*. Based on a global awareness, this management will take into account that a product that has already matured in Japan

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Management Plan

3 Stage management

Nitto Denko is committed to creating global niche top businesses utilizing not only Japanese resources but also those of group members around the globe. Stage management was introduced to achieve this by enabling every area worldwide to create products and businesses with potential for global development. The method adopted in stage management is first to broadly classify businesses into 1) those in the growth stage (business seeds, area niche top, global niche top), and 2) those in the no-growth but stable stage, and then to take action matched to the respective stages. This objective analysis of business stages enables prompt decisions regarding the best times for effective investment and for withdrawal from the business. The aim is to double the number of global niche top products by deliberately speeding up the growth pattern cycle.



may well still be a growth product in some other world market. Simply stated, it will be directed at *global optimization from the viewpoint of the Group as a whole.*

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Vision of the Nitto Denko Group in Five Years

The setting of concrete numerical targets is, to be candid, not practical. Markets are not stable enough to foresee conditions five years from now. But this does not deter us from the goal of making Nitto Denko into a top-tier company by world standards. What this means in terms of numbers will become evident automatically during the push forward. The strategies for reaching this goal are, in combination, the substance of the New Mid-Term Management Plan.

A prerequisite to achieving world-class excellence is the training



and deployment of people who can meet the challenges of world markets, people with ideas that reflect a global outlook, people

who can think from the viewpoint of optimizing the Nitto Denko Group as a whole. Persons of outstanding ability employed by overseas Group companies will be sought out and placed in positions where they can apply their capabilities to the full.

Nitto Denko also needs to continue to build itself into a technology-oriented company. This means broadening and intensifying R&D.

It means strengthening new product development capability. It means keeping so closely in touch with customers as to be able sense their changing needs and priorities from



the twitch of an eyebrow. And it requires speedy, precise information gathering capability, bold and appropriate decision-making power, and the ability to act with speed and flexibility. By perfecting and bringing these qualities into good balance, we want to make the Nitto Denko Group a company that is constantly on its toes. This, we believe, is the essence of thoroughly implemented speedy management. Management speed is the Company's greatest asset.

Globalization

4 Global Optimization— Supervisory company established in China

Nitto Denko (China) Investment Co., Ltd. was established in July 2002 as a company for centralizing supervision of the strategic business investments and management infrastructure of the Nitto Denko Group in China. In China, the growing number of foreign companies establishing production bases and the rapid growth of internal demand are making the Group's China strategy increasingly important. The establishment of the supervisory company is aimed at enhancing scale merit and Group synergy through various means, including shared information.

6 Stronger, more extensive M&A— Acquisition of AcoustiSeal, Inc.

In December 2002, Nitto Americas, Inc., which supervises Group operations in the United States, acquired AcoustiSeal, Inc., a Missouri-based company engaged in the manufacture and marketing of automotive sealing materials. The objectives of the acquisition were to add complementary products to the Nitto Denko Group's existing product line so as to solidify the Group's position as a total solutions provider in the sealing material field and to strengthen marketing access to the three big U.S. automakers.

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Collaboration with overseas universities and research institutions

is being vigorously promoted as a way of bolstering and accelerating research and development. Not all development work needs to be done in-house. *Stepping up M&A* is another option. In-house ventures will also be aggressively pursued as a source of additional seeds of growth.

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One new measure being used to speed up management is the *separation of managerial and executive functions*. Delegation of authority is needed for faster implementation of business decisions, while the management side needs to make prompt and unerring decisions with foremost attention to global affairs. Everything is aimed at increasing speed. The separation of functions also contributes to management transparency. NITTO needs to be a single entity from whatever angle it is viewed. That is why we are intent on establishing a "One-NITTO" culture, on creating a company whose global components share the same management policies, business strategies and business decision implementation standards under the concept of the "NITTO WAY."

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Pinpointing the Buds of Core Products

So what businesses will drive the Nitto Denko Group five years down the road? While the optical sector is currently doing a fine job as cleanup hitter, it is certain to peak out eventually. The Company must be on the lookout for replacements. The medical sector, including transdermal drug delivery patches is likely to break out as a powerful force on world markets from around fiscal 2007. Among membrane products, high-polymer separation membrane modules that provide basic support for water treatment technologies can be expected to enjoy surging growth in response to the ongoing global expansion of water-related businesses. The tape and film sectors also have high growth potential, thanks to the role they play in revolutionizing the manufacturing processes of many high value-added products. About half of flexible printed circuits (FPCs) production is now centered in Japan. A shift to global production is indispensable. The plan for Japan is to boost the ratio of high value-added specialty parts production.

Technology

5 Building R&D muscle through collaboration

A joint research project being carried out by U.S.-based Nitto Denko Technical Corp. in cooperation with the University of Arizona is starting to pay off with some interesting results. Nitto Denko Technical Corp. was established in Oceanside, California in 2000 to conduct R&D in the field of advanced materials for optical communications and bioscience, with an eye directed 10 to 20 years into the future. It has since launched joint research initiatives with the University of Arizona, the University of California at San Diego and other institutions in the United States. During fiscal 2003, a project being conducted in cooperation with a group headed by Dr. Peyghambarian at the University of Arizona achieved two breakthroughs in optical communications-related materials. As application of optical communications is certain to move beyond the realm of trunk lines into home telecommunications and electronic equipment, the two newly developed materials are expected to make a substantial contribution to the next generation of optical communication devices.

Promotion of industry-government-academic and other types of collaboration is to be vigorously promoted as an avenue to strengthening research and development overseas.

In a short-term view of the Company's operations, we believe fiscal 2004 will be a turning point for the LCD business. In the optical sector, the question is whether demand generated by LCD TVs will swell sufficiently to take over from personal computers and mobile phones as a new growth engine. If the strategy we are taking, including the building of a new plant, succeeds in fiscal 2005, prospects for five years for now will be excellent. We think the Company will be able to maintain its niche top status.

The tape materials sector ought to benefit from a synergistic effect produced by demand from the automotive industry. This will enable it to move ahead with the creation of new products and fresh demand in close liaison with customers.

The electronics sector's all-out effort to minimize production costs, such as through the expansion of production in China, can be expected to keep it on a steady upward course.

In the specialty products sector, whose mainstays are medical and membrane products, the outlook is for higher profits than in fiscal 2003. From here on, the sector's biggest challenge will be global expansion.

During fiscal 2004, "Double the Lineup of Global Niche Top Products" will remain the central theme of the corporate business strategy for leading the Group to continued growth through energetic development of new products of enhanced value in niche product sectors. We believe that Nitto Denko can achieve its fiscal 2004 goals of an operating income ratio of 10%, operating income of ¥40,000 million and net sales of ¥400,000 million.



Hideki Yamamoto

Chairman



Masamichi Takemoto

President

Corporate Governance

7 Separation of management and executive functions

On April 1, 2003, a corporate governance reform was put in effect for improving managerial soundness, strengthening and speeding up the conduct of business and increasing unified Group management power. Management decision-making functions and business execution functions were clearly differentiated in a move to separate the two. An operating officer system was introduced to ensure faster and more powerful conduct of the Company's businesses. The newly created operating officers are responsible for optimizing the performance of their assigned area of business. Concomitantly, with the introduction of the operating officer system, the Board of Directors was reduced from 14 members to 9, and the term of office of both directors and operating officers was set at one year.