

## To Our Shareholders

Last year's active investments in growth areas helped us achieve sales of ¥514,868 million and an operating income of ¥70,019 million.

### Fiscal 2005 Achievements

The Japanese economy recovered steadily in fiscal 2005, led in part by the booming digital economy and a strong upswing in capital investment. The pace of growth was slowed, however, by skyrocketing prices for energy and primary raw materials. In the second half of the year, moreover, uneasiness about economic conditions in the U.S. and China hampered exports and prompted production cuts in manufactured goods.

Against this backdrop, Nitto Denko Group continued to forge ahead with selection and focus, with special attention given to growth areas in electronics and automotive products. We gained ground in the market for information-related appliances and devices, concentrating our efforts on LCD-related products and circuit materials for FPDs, cellular phones and other products. We made further advances with industrial materials and engineering plastics for the automotive sector and the office automation market. In the medical segment, where we expect to generate strong future revenues and profits, our efforts turned to transdermal therapeutic patches and other promising medical-related products. Nitto Denko Group is also boosting operational efficiencies by gradually withdrawing



**Masamichi Takemoto**  
President

from low-value-added general-purpose products and by disposing of businesses with weak group synergies. As a result of these and other activities, Nitto Denko achieved another year of outstanding performance in fiscal 2005, with both sales and profits climbing to record highs.

Net sales in fiscal 2005 were ¥514,868 million, a 13.7% increase compared to fiscal 2004 (all comparisons hereafter are year-on-year for the same period). Operating income jumped 25.2% to ¥70,019 million, slightly above our initial projection of ¥70 billion. Net income also rose significantly, up 25.3% to ¥41,843 million, thanks largely to increased capacity utilization due to the positive impact of expanded sales, successful reductions in supply prices for raw and auxiliary materials, and improved production yields. These improvements were achieved despite various negative factors, including lower product selling prices, soaring oil prices and the resultant cost increase for certain raw and auxiliary materials, a stronger Japanese yen and increased depreciation expenses.

### Distribution of Profits

The pillar of Nitto Denko's dividend policy is to provide shareholders with a stable stream of profits. Nonetheless,

Nitto Denko is still on a growth path, and it operates in an extremely competitive industry that continues to undergo intense and rapid change. Our survival and future growth cannot be secured without proactive investments in R&D and production technologies. These indispensable investments keep us in step with (and ahead of) the rapidly advancing technological frontier, and they allow us to respond more quickly to customer needs. We are convinced that farsighted investments will also bring greater value and profit to our shareholders. Our policy from this point forward will be to calculate fair and appropriate dividend payments based on a comprehensive review of our investment plans, financial condition, profitability levels, dividend payout ratios and other relevant factors.

In fiscal 2005, Nitto Denko increased dividends to ¥50 per share, up ¥10 compared to fiscal 2004.

### Prospects for Fiscal 2006

The Japanese economy in fiscal 2006 is expected to continue along the path of cyclical adjustment that started in fiscal 2005. In the second half, we foresee a recovery in demand in the U.S. and Europe for information-related equipment, and this should help Japanese production regain its vitality,

## Nitto Denko's Corporate Branding Activities

# Flexible Technology Company

Nitto Denko enjoys high marks among analysts and the business community, but recognition among the general populace remains low. Although we have grown to include 113 companies in 24 countries employing 22,000 people, the fact is that even some of our employees do not fully understand the value and quality of their own company. This must be remedied if Nitto Denko hopes to join the ranks of the world's top-class corporations. Toward this end, Nitto Denko Group launched a project in July 2004 to raise its corporate brand (CB) value.

Improved CB value tends to be equated with better visibility, but there are also other major benefits. At this time, we feel we should focus most on improving employee motivation and nurturing people who can stand on their own in any country where they work. We want employees who take pride in their company, employees who are constantly improving their skills and aiming for excellence, and employees who are capable of saying "No" to behavior inconsistent with Nitto Denko's CB. We boost employee awareness in all these directions, and we believe doing so will contribute greatly to Nitto Denko's sustained growth while simultaneously minimizing potential risks.

We are committed to expanding our brand activities in this fashion and to creating a virtuous cycle, one that raises the quality and motivation of our human resources, one that improves customer satisfaction and corporate performance, one that leads in turn to higher levels of performance and eventually to the return of further profits to shareholders. This is the essence of our campaign to raise our CB value.



## To Our Shareholders (continued)

especially for electronic devices. Nevertheless, with a robust recovery of the U.S. economy seeming unlikely, we envision only a gradual trend toward a recovery.

More than 70% of all sales by Nitto Denko Group are related to the electronics market, and the favorable results we have enjoyed to date reflect the healthy condition of the electronics industry. However, we feel that such favorable conditions are unlikely to continue given the significant fluctuations of the global electronics industry and the increasing intensity of price competition in this market. Therefore, our efforts should focus on laying the groundwork and the stepping-stones that will spark advances in fiscal 2007 and beyond.

In light of these considerations, Nitto Denko is aggressively developing strategies to ensure growth in fiscal 2006 and beyond. In fiscal 2006, we will continue to pursue our selection and focus strategy, which aims to strengthen our operations in growth areas like electronics and automotive, and to identify and develop new "Global Niche Top" products.

We anticipate great future growth in several areas; for example, in the FPD industry, we are concentrating efforts on LCD-related products such as optical compensation films and polarizing films for large-scale LCD panels, as well as

surface protection products. In the automotive sector, we have expanded our share of business with Japanese transplants, and in fiscal 2006 we also intend to aggressively boost our market share among overseas automakers. Elsewhere, Nitto Denko is leveraging its expertise and strengthening its position with circuit materials for small hard disk drives used in mobile music players and other mobile information devices. We will continue to focus on these and other existing growth areas, while simultaneously pushing forward with the development of "Next-Generation Growth Engines," including our transdermal therapeutic patches.

Nitto Denko is working hard to improve production yields by reducing its overall industrial waste and strengthening its recycling efforts. Our group is also exploring ways to streamline logistics to keep pace with globalization.

In fiscal 2006, we forecast net sales of ¥580 billion (12.7% increase), operating income of ¥77 billion (10.0% increase), ordinary income of ¥75.5 billion (5.1% increase) and net income of ¥48 billion (14.7% increase). These projections take into account various factors, including the impact of exchange rate fluctuations and changes in the scopes of consolidation among our affiliates.

### MID-Term Management Plan (Fiscal 2006-2008)

## One-NITTO Dream Plan Step 2



## One-NITTO Dream Plan Step 2 (fiscal 2006-2008)

A major objective of Nitto Denko Group, and one designed to spark further corporate growth, is to become a "Global Excellent Company" by fiscal 2008. One important requirement for achieving this status is to create a highly efficient and value-adding corporate culture. By fiscal 2008, we are aiming for a return on assets (ROA\*) of 12% and an operating margin of 17%, numbers comparable to the performances of top-class global companies. To achieve our goals, we developed and launched a mid-term management plan in fiscal 2004 entitled "One-NITTO Dream Plan (fiscal 2004-2006)." The plan is devoted to corporate growth, and focuses more than ever on our "Global Niche Top" strategy.

It also underscores our aggressive pursuit of portfolio selection and focus as well as globalization. Indeed, having achieved record-high results in the plan's first two years (fiscal 2004 and 2005), we feel that the achievement of our fiscal 2008 target is well within reach. Our mission is to achieve continuously healthy business results and to consistently boost our corporate value among our stakeholders and society at large.

*\* Based on net income*

We don't have high expectations for a favorable business environment in fiscal 2006. This is why we must pursue strategies that promise strong results in fiscal 2007 and beyond.

## "Global Niche Top" Strategy Drives Our Growth

Nitto Denko's Global Niche Top (GNT) strategy has been the foundation of its growth. This GNT strategy consists of the following. Before entering a market we ask three questions: Is the market growing?; Does the market have areas for niche products?; and Does Nitto Denko have technology, competencies, and information that will differentiate it in this market? If we can answer 'Yes' to these three questions, then we will invest heavily in management resources, such as human resources, and develop products that will gain a number one share world-wide in the market. By developing and introducing GNT products, we have been able to keep the engines of growth going from one generation to the next.

At present we have 10 GNT product categories, including products such as polarizing films for LCDs and reverse osmosis membranes for semiconductor washing. Moreover, for FPDs, automotive, cellular phone, environmental-electronics industries, we have identified 22 other GNT product candidates, such as transparent conduction film for FPDs, steel plate reinforcement materials for automobiles, and internal pressure regulation materials for automobiles and consumer electronic devices. In this fiscal year we plan to select 14 of these candidates and develop them into full-fledged GNT products.



Polarizing film for LCDs



Retardation film for LCDs



Polarization conversion system for LCDs



Transparent epoxy encapsulating resin



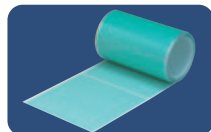
Semiconductor wafer protection and fixing tapes



Reverse osmosis membrane for semiconductor cleaning wafer



Thin metal core board for magnetoresistive heads



Thermal release sheets



Surface protection film for automobiles



Transdermal therapeutic patches

## To Our Shareholders (continued)

Over the mid-term we will pursue strategic capital investments and shift to “growth engine” products with higher added value to enhance our Global Niche Top strategy.

Yet, despite the many successes of our Dream Plan, we realize we are still only halfway home in reforming our corporate culture. This is why we launched the new One-NITTO Dream Plan Step 2 (fiscal 2006-2008). Step 2 stresses qualitative growth in Corporate Social Responsibility (CSR) promotion and brand value improvement, and it reinforces our goal of becoming a “Global Excellent Company.” We also launched a program in fiscal 2005 entitled “Corporate Brand (CB) Value Improvement Initiatives.” For fiscal 2006, we established new corporate units devoted to both CB value improvement and CSR promotion. The Step 2 plan has concrete numerical targets, namely operating income of ¥100 billion in addition to the targets for fiscal 2008 stated above.

Strategic capital investments over the medium term will spearhead a shift to higher value-added “growth engine” products.

### Capital Investment Strategy

Our strategic capital investments in fiscal 2006 will be concentrated both on existing and next-generation growth engines. Nitto Denko’s current growth engine is

## R&D Sections Synchronize with Manufacturing Sites

### *Kameyama Plant Technical Center*

Kameyama Plant, near Nagoya in central Japan, is the stronghold of Nitto Denko’s Electronics Products Division. In August 2005, we will open a technical center at the site. The Center will be responsible for consolidating the group’s electronics-related R&D, and is expected to further accelerate the company’s R&D efforts in the field of flexible printed circuits, semiconductor-related materials and electronic processing materials.



Kameyama Plant Technical Center

### *NDT New Research Center*

A new research center was opened in Nitto Denko Technical Corporation (U.S.) in May 2005. This site specializes in the R&D of materials relating to optical communications, genomics and nanoceramics. We have high hopes for this new addition to our R&D family.



NDT New Research Center

the electronics segment, which is centered on FPD panels. In fiscal 2006, we will pursue first-stage investments of ¥14.5 billion to boost our production capacity of optical films by about 1.6 times. This investment, we believe, will allow us to keep in step with growth in the LCD market. This plan covers funding for the construction of a new processing facility at our Onomichi site in Japan, thereby introducing a new process to improve productivity. A new logistics center will be established as well to deal with increased material flow. We also plan to invest aggressively at our Kameyama Plant in Japan, where we will introduce a new film-orienting line and construct a new site annex.

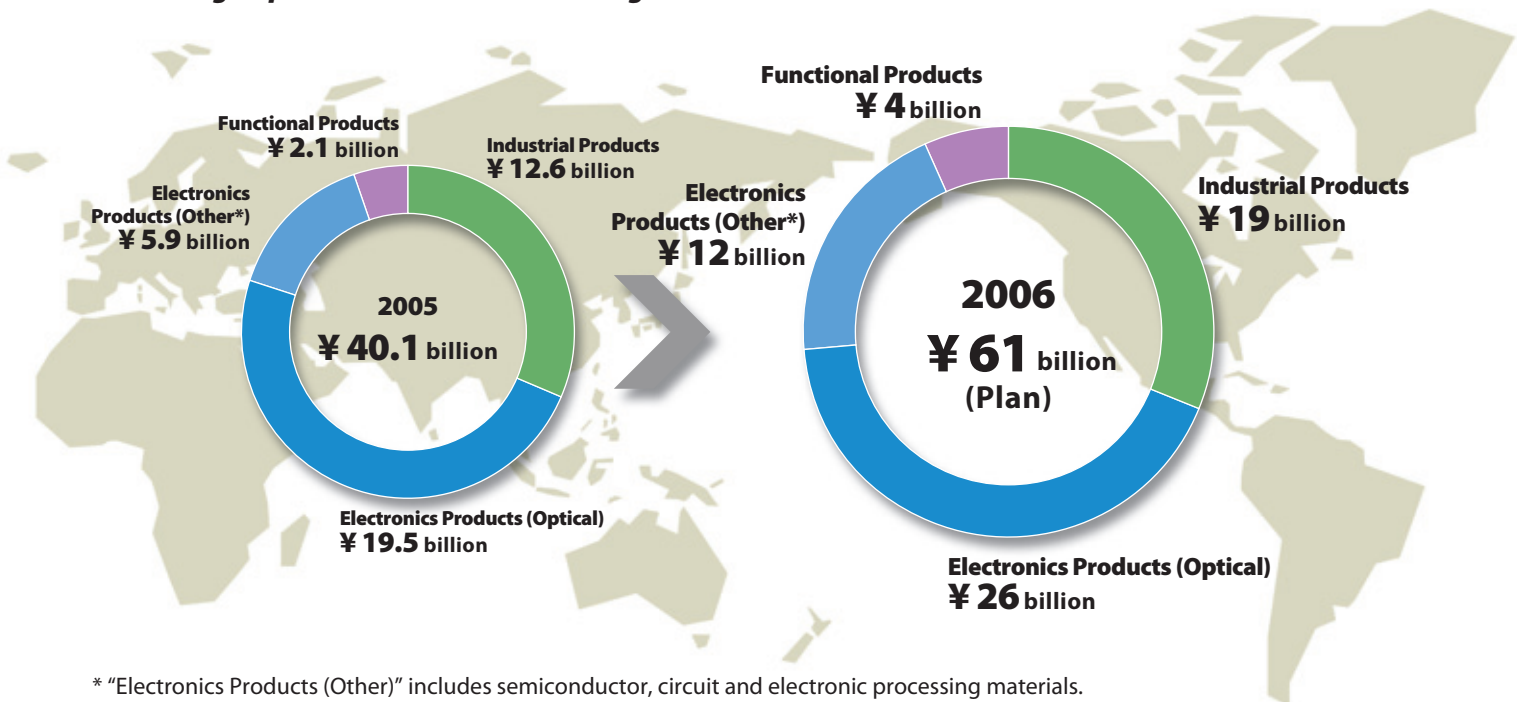
We anticipate substantial growth in the FPD market, mainly in TV applications, despite the intensely competitive nature of this industry. We intend to maintain our top share of this market by taking advantage of Nitto Denko's four strengths—differentiated technologies, overwhelming production capacities, unparalleled know-how acquired from customer ties and close relations with suppliers.

Automotive products, we believe, are one of the most promising next-generation growth engines. The

automotive market represents a substantial market for us, as one vehicle alone can utilize more than 20 products from the Nitto Denko lineup. In the past, most of our sales were directed at Japanese car manufacturers, but henceforth we plan to aggressively grow our automotive business by targeting overseas automakers in the U.S., Europe and Korea, and by leveraging the success and know-how we have accumulated in Japan.

To achieve our objectives, we have established a network of technical centers to conduct product evaluations on vehicle frames supplied by our client automotive manufacturers. We have technical centers in Detroit, the U.S. (established Dec. 2002), Toyohashi, Japan (Oct. 2003) and Genk, Belgium (June 2005). In fiscal 2004, we launched the Global Automotive Business Strategy Group, an organization that cuts across our operating units to ensure an integrated group approach to the automotive industry. This move, combined with a strong networking among our worldwide production sites and technical centers, has improved our responsiveness to the market and strengthened our ability to develop products that respond to customer needs.

### Increasing Capital Investment for Growing Demands Worldwide



\* "Electronics Products (Other)" includes semiconductor, circuit and electronic processing materials.

## To Our Shareholders (continued)

Circuit materials are another next-generation growth engine. Our Kameyama and Suzhou (China) plants currently manufacture flexible circuit boards for use in cellular phones and other devices. In the future, we plan to reinforce our global production setup and our ability to meet expanding demand by embarking on integrated production in Vietnam. The new Vietnamese facility will be involved in all production stages, from initial to final processing.

Another important target is the market for thin metal core boards for magnetro resistive heads (MRH), which are used in HDD assemblies. HDD usage has now expanded beyond the traditional personal computer market into the markets for cellular phones and mobile music players. MRH demand is increasing rapidly in step with such developments. To meet this growing demand, we plan to expand our MRH capacity by installing a 10th facility at our Kameyama Plant. We have also established a new company to carry out integrated production in southern China, and steps are being taken to start operations in the near future. These additions to our production network will help to shorten lead times and improve our crisis management in case of natural disasters.

Nitto Denko Group is committed to boosting its overseas production capacity to meet expanding global demand. We will also proceed with capital investments in Japan to boost our production capacity and improve product quality, especially for FPD-related materials.

In fiscal 2006, we anticipate capital expenditures of ¥61 billion, and we intend to back this up with active strategic capital investments during the next three years.

### Future Growth Engines

Our strategic investment strategies go beyond medium- and long-term frames. We also believe it is important to look at a longer time horizon, to take steps now that will foster our growth well beyond fiscal 2008. We are focusing currently on two promising markets: (1) medical products and (2) polymer separation membranes.



The mainstay products in our existing medical business include transdermal therapeutic patches and adhesive medical tapes. Our ongoing focus is on introducing new products in cooperation with drug manufacturers in the U.S. At the same time, we plan to begin selling our existing Japanese products — those that already enjoy large market shares in Japan — in China and other Asian nations. These efforts are expected to significantly improve our financial performance in fiscal 2007 or fiscal 2008 and beyond. Another area of great interest is the market for polymer separation membranes, products that continue to enjoy steadily increasing demand due to global water shortages and water pollution. Nitto Denko has achieved a certain degree of success in this field, having already introduced reverse-osmosis membranes for seawater desalination in China and elsewhere in years past. Even so, the time has come for us to contemplate a unique and dedicated membrane business, one that maximizes our strengths and minimizes indiscriminate market-chasing. From this point forward, Nitto Denko will move with selection and focus on key markets toward achieving the goals of “Global Niche Top” strategy.

These and other initiatives will spearhead our group efforts as we strive to become a Global Excellent Company and the business partner of choice among our customers.

A handwritten signature in black ink that reads "Masamichi Takemoto". The signature is written in a cursive, flowing style.

Masamichi Takemoto  
President