

Analysis of the Business Result

1. Summary of Overall Business

During the past fiscal year, the Japanese economy continued on its recovery, while consumer spending remained somewhat flat, improvements were seen in business earnings, capital investment and employment conditions. In the U.S., although housing construction stalled, overall consumer spending increased and the economy continued its modest expansion. In Asia, China led the continued expansion, while in Europe, the economy recovered supported by an expansion in domestic demand.

In these economic environments, despite the continued growth of the flat panel display (FPD) industry, a key market for Nitto Denko Corporation and its consolidated subsidiaries (the Group), sales of LCD-related products were influenced significantly by the steep decline in the market price of large-size LCD TVs. Business relating to the electronics industry, (hard disk drives (HDD) and cellular phones) and the automotive industry and polymer separation membrane industry (water-related businesses) remained robust but were unable to counter the reduced performance of LCD-related products.

Compared with the previous year, sales have increased by 8.5% to 679,822 million yen. In terms of profits, however, due to the drop in price of LCD-related products and the deterioration of product yields, as well as an increase of depreciation costs related to capital investment, operating income decreased by 22.6% to 69,037 million yen, ordinary income decreased by 25.4% to 67,319 million yen and net income decreased by 25.5% to 41,201 million yen.

2. Summary by Business Segments

Industrial Products

Sales of bonding and joining products for cellular phone components and for small-size LCDs remained robust due to production expansion of cellular phones. Increases were mainly experienced throughout East Asia. Sales for HDD related components also remained strong. Among surface protection products, sales of surface protection film (the product name "E-MASK") for FPD industry were hampered by customer production adjustments in the latter half of the term but remained robust on a year-on-year basis. Sales of automotive paint protection film and metal sheet protection film also remained strong. Sales of sealing materials for peripheral components of cellular phones, flat TVs, game gadgets and for automobiles also continued their strong performance. However, sales of products for use in housing and building leveled off due to a steep increase in raw material costs.

For the segment, sales increased to 268,888 million yen (up 7.0%) and operating income rose to 28,019 million yen (up 22.2%).

Electronic Products

Sales of LCD-related products were significantly influenced by product price decreases, despite the growth in demand for LCD TVs, and greater production efficiencies. While sales for cellular phones remained robust, sales as a whole remained sluggish. In relation to semiconductor related products, sales of environmentally-friendly resin and resin for advanced device remained robust, while sales of general purpose resin remained flat due to production adjustments by customers in the latter half of the term. With regard to printed circuit products, sales for cellular phones remained robust as did sales relating to the storage industry. In the area of electronic processing products, semiconductor package adhesive sheets expanded their share in overseas markets, and sales of processing materials for small



electronic components remained robust, while wafer-protection adhesive tape and taping system for the semiconductor manufacturing process leveled off. As a result, sales increased to 356,941 million yen (up 9.0%) and operating income decreased to 31,449 million yen (down 46.4%).

Functional Products

In relation to medical related products, sales of transdermal therapeutic patches for asthma and ischemic heart disease were influenced by drug price reductions. These reductions were compensated for due to our business streamlining efforts. Sales of local anesthesia patches remained robust. Among medical and sanitary products, despite the withdrawal of some products, sales of our medical and sanitary products as a whole remained strong.

Sales of polymer separation membranes remained strong largely due to new contracts and replacements for ultra-pure water for the semiconductor and LCD industries in Japan, new contracts for wastewater treatment in the U. S., and for seawater desalination plants in the Middle East and in Europe. This all transpired whilst new products with varied industrial applications gained recognition within the Chinese market.

In relation to plastic engineering products, sales of functional products for office automation (OA) and the sales of information equipment and porous film materials for automotive parts, electronic parts, home appliances and for environmental use remained robust. As a result, sales increased to 53,991 million yen (up 13.6%) whilst operating income increased to 9,568 million yen (up 26.3%).

3. Summary of Geographic Area

In Japan, Asia and Oceania, LCD-related products and industrial products for home and information electronics such as LCD TVs, cellular phones and office automation equipment remained strong. Due to the acceleration of decreasing product thickness and the functional enhancement of information electronics, sales of industrial products have increased steadily. However, LCD-related products were influenced by a significant decrease in the market price of large-size LCD TVs.

As a result, sales in Japan decreased to 268,364 million yen (down 1.04%), and operating income decreased to 52,535 million yen (down 31.7%). As for Asia and Oceania, production of panels for LCD TVs increased in Korea and Taiwan, but due to a sharp decrease in LCD panel prices, sales of LCD-related products were influenced by the price decline. As a result, sales increased to 345,321 million yen (up 16.2%), but operating income decreased to 12,382 million yen (down 1.5%).

In Europe, sales of industrial products used in the automobile and cellular phones remained robust. As a result, sales increased to 23,787 million yen (up 22.6%), and operating income increased to 1,587 million yen (up 128.7%).

In North America, despite a trend in earnings recovery due to productivity reform of industrial products and the polymer separation membrane business, sales to U.S. automotive manufacturers remained sluggish. Moreover, a new product of transdermal therapeutic patches (for hypertension) has not yet obtained drug approval, so sales as a whole remained sluggish. As a result, sales in North America increased to 42,349 million yen (up 9.8%), with an operating loss of 663 million yen, despite an improvement of 414 million yen when compared with the last fiscal year.

4. Financial Condition

As of the end of the consolidated fiscal year, cash and cash equivalents (further referred to below as “cash”) decreased to 74,551 million yen, 12,132 million yen down from the end of the previous consolidated fiscal year. The status of each cash flow and major cash flow-related factor is outlined below.

Cash flows from operating activities

Net cash provided by operating activities totaled 63,032 million yen. This was mainly attributable to an increase in net income before taxes of 65,100 million yen, depreciation of 40,169 million yen and purchase liabilities of 9,849 million yen, and to a decrease in accounts receivable of 11,613 million yen and an outlay of corporate taxes of 37,124 million yen and other payments.

Cash flows from investing activities

Net cash decreased as a result of investing activities totaled 77,285 million yen. This was mainly attributable to a decrease in an outlay of 77,716 million yen for the acquisition of fixed assets.

Cash flows from financing operations

Net cash increased as a result of financial operation totaled 879 million yen. This was mainly attributable to a decrease of 10,777 million yen for dividends paid and an increase of 10,000 million yen in commercial paper.

The following table shows the changes in the Group’s cash flow indices:

	2003	2004	2005	2006
Equity ratio (%)	57.3	58.9	57.7	60.4
Equity ratio on a market value basis (%)	240.2	208.7	296.2	152.4
Debt redemption period (year)	0.4	0.3	0.3	0.6
Interest coverage ratio	193.3	169.0	92.1	57.1

- Note 1. Respective indices are obtained by calculating the financial results on a consolidated basis with the following formulae.
- Equity ratio: $\text{equity} \div \text{total assets}$
 - Equity ratio on a market value basis: $\text{total market value of shares} \div \text{total assets}$
 - Debt redemption period: $\text{liabilities with interest} \div \text{cash flow from operating activities}$
 - Interest coverage ratio: $\text{cash flow from operating activities} \div \text{interest payment}$
2. Total market value of shares is obtained by multiplying the closing price of a share at the end of the year by the number of shares issued at the end, after deduction of treasury stock.
3. Liabilities with interest represent all the liabilities included in the consolidated balance sheet for which interest is paid.
4. Cash flow from operating activities and interest payments used here are those included in the consolidated cash flow statement.