Toshiro Ota
Chairman and Representative Director

Katsuhiko Takeshita
President and Representative Director

Strengthening Competitiveness

On April 4, 2002, Noritz Corporation agreed to a broad-ranging business alliance with TOTO Ltd., to increase its competitiveness. Combining their respective strengths, the two companies will mutually supply products and components as well as collaborate on distribution and after-sales services.

It has already been agreed that TOTO will cease production of gas-related water heaters, and within the year, Noritz will commence production and after-sales servicing of TOTO-brand gas-related water heaters. Given that both companies share many of the same clients (sales agents), the companies plan to share their respective distribution systems to make more effective use of their quick-delivery systems. The companies are considering further cooperation on other products, components, and incidental services, and will gradually implement such plans during fiscal 2002, ending December 31, 2002.

The Noritz Group is currently implementing its "Creation 21" long-term management plan. The plan's basic policy is the strengthening of the Group's operational structure. The management strategies specified in the plan target increased profitability in the product-related business, the establishment of a customer service-related business, and the promotion of business alliances. The alliance with TOTO is consistent with these policies. We will continue to make aggressive efforts to maximize the reciprocal merits afforded by this and future alliances.

The merging of the technological and R&D capabilities of both companies will enable the development of more attractive products. We expect to boost efficiency and raise competitiveness, made possible through the shared infrastructure, which allows for the mutual supply of parts and materials and collaboration in distribution and after-sales services.

Fiscal 2001 in Review

The Parent Company's Performance

Noritz introduced the most recent three-year management plan, which ended in the fiscal year under review, in fiscal 1999. We achieved an increase in sales for two consecutive years while income also rose. In the third and final year, fiscal 2001, sales continued their upward trend, although net income declined. Net sales rose 10.2% compared with the previous fiscal year, to ¥154.5 billion. This was due to strong sales of gas-related water heaters and system products, such as bathroom- and kitchen-related equipment, following a business tie-up with Harman Co., Ltd. Operating income, however, fell 12.4%, to ¥7.7 billion, due to a downturn in sales prices and rising selling, general and administrative expenses. During the year under review, the Company recorded a special loss of ¥2.8 billion resulting from the introduction of revised retirement benefit accounting. As a result, net income dropped 59.7%, to ¥1.0 billion.

Looking at performance by business sector, sales of gas-related water heaters and air conditioners increased 5.1%, while system bathrooms and kitchens rose 11.0%. As a product group, gas-related water heaters, related components, and system baths saw substantial growth. In the hot-water heater group, the strongest growth was seen in gas water heaters, kerosene-fired water heaters and peripheral appliances. In contrast to the 20-to-30% growth registered annually since 1998, previous fiscal year, this category showed year-on-year growth of 121.0%.

Looking at performance by business segment, in our water heater business, for the fourth consecutive year we expanded our market share for each of our main products comprising this segment—bath heaters, kerosene-fired water heaters, and gas-related water heaters. Water heaters held a market share of 33.4%.

In system bathrooms and kitchens, we expanded our market shares for system bathrooms, vanity units, and system kitchens. During the past year, market share was won through sales of popular, mass-market items. In the future, however, we intend to raise our unit price by focusing on sales of high-grade and luxury items.

In fiscal 2001, our break-even point deteriorated by four percentage points, to 86.5%. Sales price reductions could not be covered by cutting materials costs, and distribution costs rose due to the growth in the number of system products manufactured, leading the variable cost ratio to decline 0.8 percentage point, to 65.1%. The fixed cost ratio fell 0.7 percentage point, to 30.1%. This is attributable to higher personnel costs resulting from the introduction of new retirement benefit accounting, as well as rising R&D for new products and sales promotion costs. As a result, the operating income ratio dropped 1.3 percentage points, to 5.0%. The Companywide unit sales price declined about 4.0% on average from the previous year.

Policy Implementation and Results

Regarding the market demand for water heaters in the previous year, tax cuts for housing loans in the first half of the year stimulated consumer incentive to spend until July, after which demand turned sluggish. As a result, demand for the year surged 102%, year-on-year. Demand for heater products, including both heat-source units and peripheral equipment, has grown into a market exceeding ¥50 billion annually. With regard to sales, we have introduced a variety of sales approaches specifically for the renovations market. Maintenance leases have also risen to the ¥1 billion level. We are convening business consultation forums nationwide. Last October, in a tie-up with the Harman Group, we started selling Harman-brand products, as well as supplying Harman with products on an original equipment manufacturing (OEM) basis.

In product development, we expanded our lineup of peripheral components for water heaters. In bathroom- and kitchen-related equipment, we introduced full model changes within a competitive price range for system bathrooms, system kitchens, and vanity units. We have also developed new gas-related water heaters and system bathrooms targeting the market for renovations, while our leading gas appliances have undergone full model changes.

As part of our Group-structure strategy, we converted our subsidiary Kanto Sangyo Co., Ltd., into a wholly owned subsidiary. Noritz also raised its share of Harmanpro Co., Ltd., to 90%, making it a consolidated subsidiary. In addition, we hold a 40% stake in Harman, a subsidiary of Osaka Gas Co., Ltd., accounting for this investment with the equity-method.

Financial measures taken include the retirement of 1.52 million shares of our own stock. Also, we completed the full redemption of our convertible bonds. As for financial indicators on a consolidated basis, return on assets was 0.7%, return on equity was 1.3%, and free cash flow was ¥9.88 billion.

Regarding the performance of our affiliates, Taisei Kogyo Corp., Shinwa Kogyo Corp., and Kanto Sangyo Co., Ltd., all saw extremely favorable performances. Harmanpro, Tada-Smith Co., Ltd., and Suoh Kinzoku Kogyo Co., Ltd. barely remained in the black. Noritz Jusetsu Corp., which was in the red during the previous fiscal year, returned to the black. Noritz Techno Service Corp. and Shanghai Noritz Co., Ltd., remain in the red.

New housing starts in fiscal 2001 fell 5%, from the previous year, to 1.17 million units, and new housing starts are expected decline 5%, to 1.12 million units in fiscal 2002. Hot-water heaters for new homes comprise 30% of demand, and replacement purchases for existing homes account for the remaining 70%. The Company expected aggregate demand for household hot-water heating units to fall 3% from the previous year's level.

The unit price, which had been expected to decline 3% from the previous year's level, fell 4.7%, creating a harsh operating environment.

The Start of Long-term Management Reforms

Such a challenging operating environment has prompted Noritz to consider drastic reform. To this end, the Company has devised a 10-year management plan entitled "Creation 21." Over the next 10 years, Noritz aims to communicate to its target audience—its customers, staff, business partners, shareholders, and society in general—that it is the company that provides "the hot water necessary for a fully satisfying lifestyle." Our basic strategies are to increase customer satisfaction, strengthen our business structure, activate the Noritz Group, and take environmental protection measures. Corporate value is comprised of customer value, shareholder value, societal value, employee value, and financial value. We intend to improve all five by setting targets, and thereby raise corporate value.

Our first medium-term management plan, which will end in 2004 and is an integral part of "Creation 21," calls for the review of management, product development, production, sales, and services. This will be done from the customer's perspective and will allow us to enact the changes necessary for creating a foundation for customer-focused management. We reformed our areas of operation, and reorganised operations. In addition to our product division, we have newly created a components division, a service division, an overseas division, and a new business division.

Regarding our management targets for fiscal 2011, Noritz is aiming for consolidated net sales of ¥250 billion and operating income of ¥20 billion, with an ROA and ROE each of 10%. For 2004, these targets are set at net sales of ¥200 billion, operating income of ¥12 billion, an ROA of 7.5%, and an ROE of 6%. We consider this year the time to begin laying down the groundwork for creating customer-focused management bases.

As our basic policy, we intend to strengthen point-of-contact sales. We are undertaking anticipatory investments of ¥0.6 billion, primarily focusing on IT, and are shifting to a sales system that enables closer contact with customers. We intend to place greater emphasis on profits. To increase contact with end users, we plan to use showrooms, online communications, and to expand the function of our customer consultation centers.

In production, we will expand the activities of Noritz New Production Systems (NRPS). This is supply chain management (SCM) targeting complete consumption production that corresponds to demand. By making and delivering the necessary items in the required amounts at the time needed, and including distribution, we can speed up the process and make substantial reductions in management costs.

Future Outlook

For the three-month period between October and December, Harmanpro contributed ¥7.1 billion to consolidated net sales in fiscal 2001. During the current fiscal year, our net sales are expected to total ¥27.5 billion and operating income ¥5.0 billion, for a net loss of ¥0.1 billion owing to the integration of our production facilities for gas-related equipment. We intend to streamline operations by reconfiguring production bases, raising efficiency in R&D, undertaking joint distribution, and conducting overseas sales in a mutually complementary manner.

As for the four new divisions (excluding the product division), the service division targets net sales totaling ¥23.0 billion (currently ¥9.3 billion) in 10 years, the components division ¥10.0 billion (¥1.4 billion), the overseas division ¥12.0 billion (¥0.9 billion), and new business division ¥5.0 billion (¥0.2 billion).

In fiscal 2002, Noritz aims to record net sales of ¥178 billion, an increase of 15.2%, operating income of ¥8.0 billion, a rise of 3.7%, and net income of 2.1 billion, a 211.3% increase.

Toshiro Ota

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Chairman and Representative Director

K. Takeshita

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