

Financial Review

Results of Operations

Net Sales

In fiscal 2005, ended December 31, 2005, the Japanese economy continued on a moderate recovery trend supported by expansion in private capital investment against a background of improvement in corporate profitability and growth in consumer spending. However, concerns remained about the prolonged period of high crude oil prices, rising prices of industrial materials, and other circumstances, thus damping any possible optimism regarding future trends in the economy. In the Company's business fields, new housing starts, principally in the multi-unit dwelling area, experienced a rising trend, but overall demand was stagnant. Also, along with the movement toward using more electrical appliances, price competition grew substantially more intense, thus leading to a continuation of challenging operating conditions.

Amid this business environment, we at the Noritz Group began to implement our Create 21 Second-Phase Medium-Term Management Plan and moved forward with strategies in three specific areas: the "new value" strategy, which focuses on developing high-value-added products in response to the requests of our customers, the "Houresh" (house refresh) strategy, which calls for strengthening our marketing framework for housing reform and refurbishment services, and the global strategy, under which we are upgrading and strengthening our overseas marketing network.

As a result of these and other initiatives, consolidated net sales increased 2.6%, to ¥176.0 billion. However, as a consequence of slippage in sales prices and higher raw material costs, operating income was down 9.7%, to ¥6.9 billion, and net income declined 13.7%, to ¥4.3 billion.

Cost of Sales and SG&A Expenses

The cost of sales rose 3.2%, to ¥122.7 billion, and the cost of sales to net sales ratio increased 0.4 percentage point, to 69.7%, largely due to the increases in raw material costs. As during the previous fiscal year, sales prices were down, but this was due to a change in the product mix and the policy of manufacturers of gas-related water heaters to lower prices to counteract the rise in the number of all-electric housing units, a development that reflected the competition among energy suppliers in the gas and electric power fields.

In addition, as a result of expenditures for future growth, including the costs of advertising and promotion as well as R&D, and after-service costs, selling, general and administrative (SG&A) expenses rose 3.2%, to ¥46.4 billion. This led to a 0.2 percentage point deterioration in the SG&A ratio and a 0.6 percentage point decline in the operating profit ratio, to 3.9%.

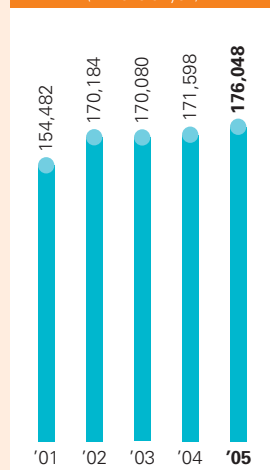
Other Income (Expenses)

Other income (expenses), net, which amounted to ¥1.3 billion in fiscal 2004, declined ¥0.5 billion for the fiscal year under review, to ¥0.7 billion. The principal reasons for this decline were the absence of the gain on the return of the substitutional portion of the employee pension fund reported in the previous fiscal year and a ¥0.3 billion increase in the loss on sales and disposal of property, plant and equipment. As a result, income before income taxes fell 14.0%, to ¥7.7 billion.

Reflecting the above items, net income was down 13.7%, to ¥4.3 billion, as mentioned previously. Return on sales deteriorated 0.5 percentage point, to 2.4%. Similarly, the return on equity (ROE) decreased from 5.9% in the previous year to 4.9% in fiscal 2005.

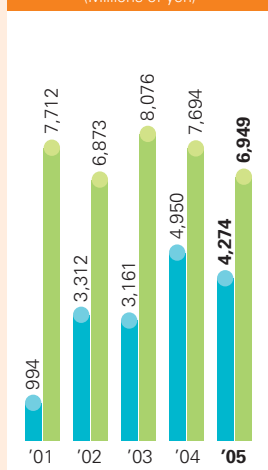
Net Sales

(Millions of yen)



Net Income and Operating Income

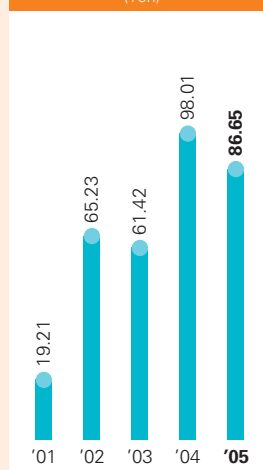
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● Net Income
● Operating Income

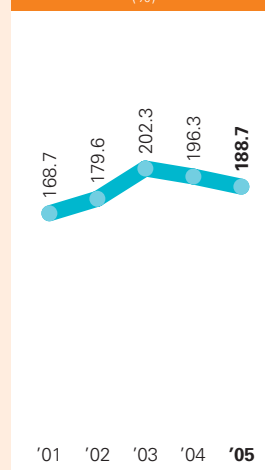
Net Income per Share

(Yen)



Current Ratio

(%)



Financial Position

The total assets of the Noritz Group at fiscal year-end amounted to ¥151.5 billion, ¥2.8 billion higher than at the previous fiscal year-end. Of this total, total current assets declined ¥0.7 billion, to ¥87.1 billion. This was primarily owing to a decline in cash and time deposits accompanying the purchase of ¥2.0 billion in Japanese government bonds, a decline in current assets due to the sale of ¥3.5 billion in trust beneficiary certificates, and other factors.

Total non-current assets expanded ¥3.5 billion, to ¥64.5 billion, largely due to purchases of Japanese government bonds, strategic investments, and other developments, which resulted in an increase in the balance of investment in securities of ¥7.3 billion. This more than offset a decline in long-term deferred tax assets of ¥2.3 billion accompanying reductions in the reserve for employees' retirement benefits and the reserve for directors' and statutory auditors' retirement benefits.

The Noritz Group's total liabilities decreased ¥0.6 billion, to ¥60.7 billion. Of this total, current liabilities rose ¥1.4 billion, to ¥46.1 billion. This was mainly due to higher balances of notes payable and accounts payable in connection with purchases of raw materials. In addition, long-term liabilities declined ¥2.0 billion, to ¥14.6 billion. The principal factors accounting for this decrease were a ¥1.1 billion decline in the reserve for employees' severance and retirement benefits as the result of the transference of a portion of the Company's lump-sum retirement payment plan to a defined contribution pension plan and a decline of ¥0.4 billion in the reserve for directors' and statutory auditors' retirement benefits.

The Group's shareholders' equity increased ¥3.3 billion, to ¥89.1 billion. This was primarily due to an increase of ¥2.9 billion

in retained earnings and a gain of ¥2.3 billion in net unrealized holding gains on securities, which more than offset an increase of ¥2.2 billion in the item "treasury stock, at cost," which is deducted from shareholders' equity.

As a consequence of these developments, the Group's shareholders' equity ratio increased 1.2 percentage points, to 58.8%. In addition, shareholders' equity per share rose to ¥1,860.92, from ¥1,750.82 at the end of the previous fiscal year.

Cash Flows

As a result of the movements in cash flow items described below, cash and cash equivalents at the end of the fiscal year under review amounted to ¥15.9 billion, ¥5.2 billion lower than at the end of the previous fiscal year.

Net cash provided by operating activities increased ¥3.0 billion, to ¥8.1 billion. Principal factors that accounted for this development included income before income taxes of ¥7.7 billion, depreciation of ¥5.6 billion, a reduction in the reserve for employees' retirement benefits of ¥1.1 billion, an increase in trade notes and accounts receivable of ¥1.6 billion, and an increase in procurement payables of ¥1.4 billion.

Net cash used in investing activities declined ¥6.6 billion, to ¥9.7 billion. This was primarily due to a net withdrawal of time deposits of ¥1.0 billion as well as net outflows from acquisition and sale of securities of ¥5.5 billion, versus expenditures of ¥5.1 billion used for the acquisition of property, plant and equipment.

Net cash used in financing activities declined ¥0.1 billion, to ¥3.6 billion. The principal factors accounting for this included payments of dividends amounting to ¥1.4 billion and payments of ¥2.2 billion to purchase the Company's outstanding common stock.

