

A Message from the Management



Katsuhiko Takeshita
Chairman and Representative Director



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Review of Performance in Fiscal 2007

Fiscal 2007, ended December 31, 2007, was the final year of our Create 21 Second-Phase Medium-Term Management Plan. Noritz Corporation reported consolidated net sales of ¥180.0 billion, 1.1% lower than for the previous fiscal year. Operating income amounted to ¥2.4 billion, 59.4% lower than for the previous fiscal year. We reported a net loss of ¥1.2 billion for the fiscal year (compared with net income of ¥3.0 billion in the previous fiscal year).

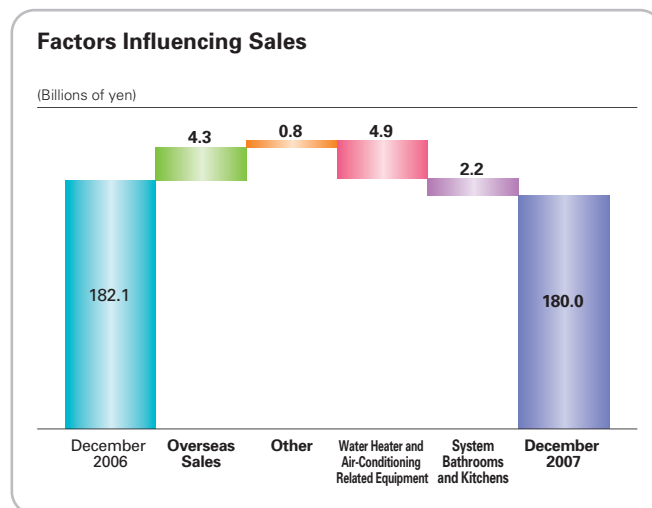
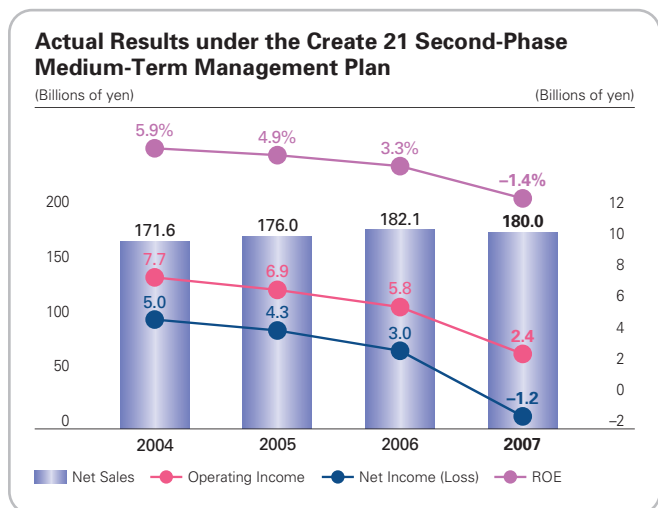
Factors leading to declines in net sales and income (loss) included the marked drop in demand for gas-fired and kerosene-fired water heaters and lower sales of system bathrooms and kitchens accompanying the deterioration in consumer psychology caused by problems related to Japan's national pension system. Other developments having an adverse impact on performance included the plateauing of the

cost of raw materials, such as copper and plastics, at high levels. Although the Companies' sales in overseas markets expanded, investments in the marketing infrastructure, including business locations and personnel, in advance of demand growth resulted in higher selling, general and administrative expenses.

Moreover, the Companies wrote off certain extraordinary losses, including principally ¥2.2 billion for safety inspections of gas-powered bath water heaters and ¥1.2 billion in the loss on the impairment of fixed assets.

Results of the Create 21 Second-Phase Medium-Term Management Plan

Performance in fiscal 2005 met targets set in the Create 21 Second-Phase Medium-Term Management Plan, but results for fiscal 2006 and fiscal 2007 were below target. Net sales in



fiscal 2007, as mentioned, the final year of the plan, were ¥180.0 billion, which was ¥5.0 billion below the target level of ¥185.0 billion. Net income fell short of the planned target of ¥5.0 billion by ¥6.2 billion. Compared to our target of 6% for return on equity (ROE), ROE amounted to -1.4%.

Sales of water heater and air-conditioning related equipment were almost on target, despite a decline in domestic demand owing the marketing drive of manufacturers of competing electric-powered units. This was the result of an increase in the Company's market share and expansion in overseas sales, principally in North America and China. In the categories of bathroom and kitchen-related equipment, sales of system bathrooms and system kitchens were considerably below target, but sales of built-in glass top ranges

manufactured by Harman Co., Ltd., a subsidiary specializing in this field, exceeded the planned levels.

On the other hand, prices of raw materials, principally copper, rose sharply in 2006, leading to an increase in material costs of ¥3.0 billion. In 2007, material costs remained at high levels, resulting in a further rise in costs of ¥2.0 billion. Although we adopted measures to lower costs and pushed through a revision in the manufacturer's asking prices in the second quarter, these measures were insufficient to absorb the rise in raw material costs.

Net income (loss) was adversely affected in 2006 and 2007 by the emergence of quality issues at Noritz and Harman. In 2006, we reported expenses for the repair of bathroom heating and dehumidifying units we recalled on a voluntary basis amounting to ¥7.5 billion. In 2007, we reported extraordinary losses of ¥2.2 billion related to gas-fired water heaters and built-in ranges.

In Japan, the awareness of product safety in society, in general, has risen as a result of accidents involving gas- and kerosene-fired as well as electric-powered equipment. As a consequence, the Consumer Products Safety Law was revised in 2007, and, beginning in 2009, inspections will become mandatory under the law.

Initiatives and Objectives under the Third-Phase Medium-Term Plan

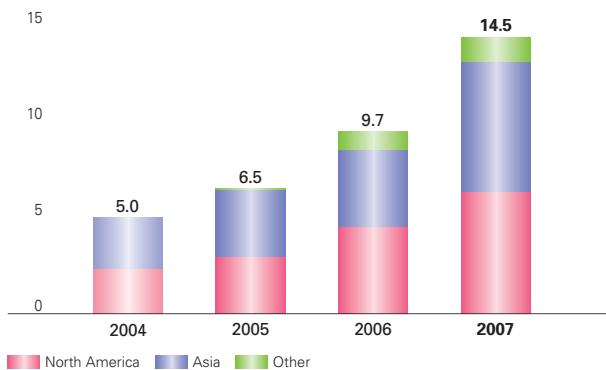
Based on a review of the Create 21 Second-Phase Medium-Term Management Plan, the Company has formulated the Create 21 Third-Phase Medium-Term Management Plan, which will run from 2008 through 2010. The performance targets under this new plan are as follows.

Changes in the Operating Environment

In Japan, more so than in the past, manufacturers of household equipment are being required to respond to environmental issues and product safety problems. Competition among gas-, kerosene-, and electric-powered equipment is growing more intense, and the gas- and kerosene-fired segments of the household equipment industry are forecast to undergo realignment as some manufacturers exit the field. In addition, realignment in the household system equipment area is

Trends in Overseas Sales

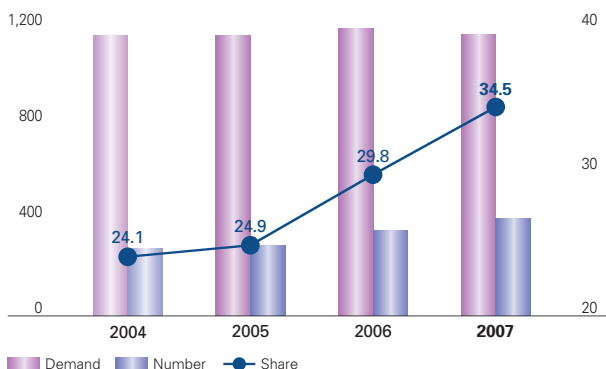
(Billions of yen)



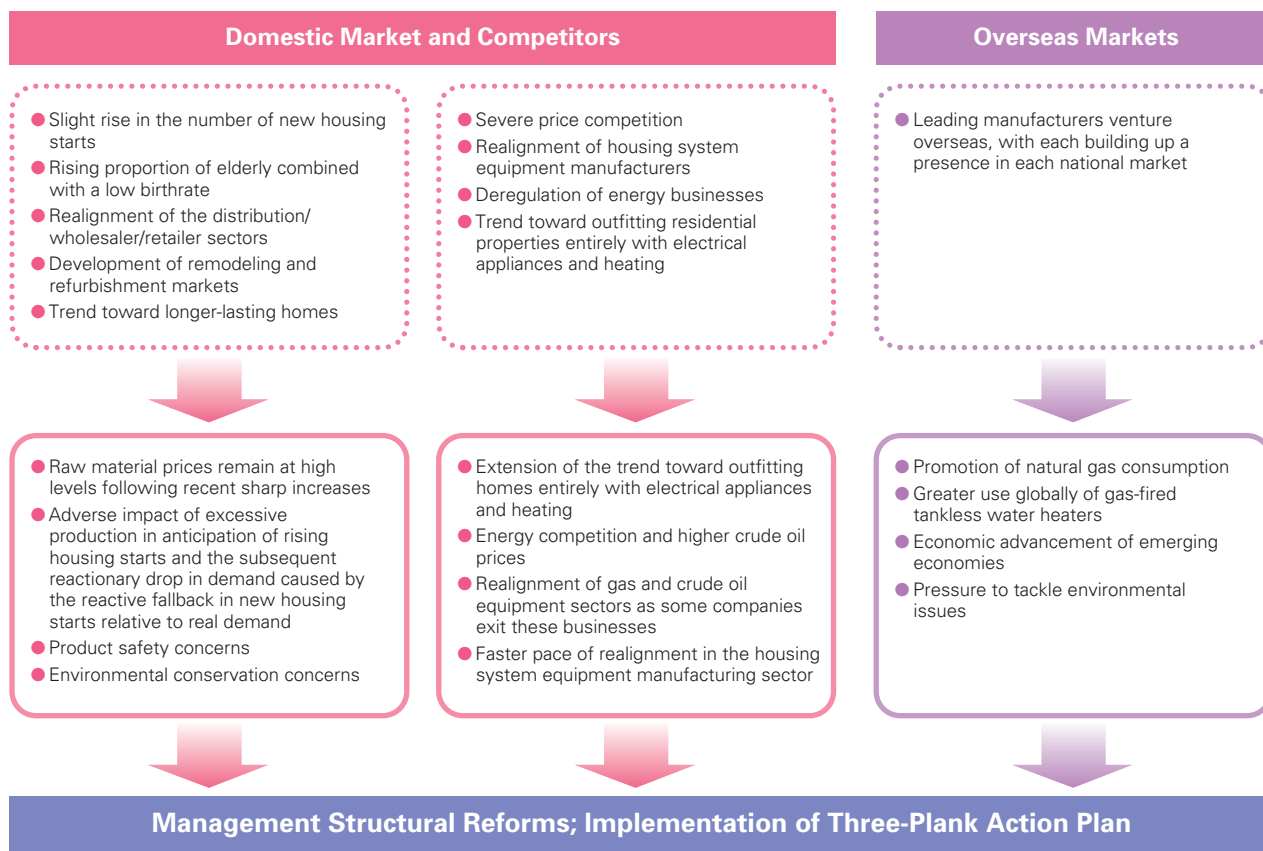
Domestic Unit Sales and Market Share of Gas Built-in Top Ranges

(Thousands)

(%)



Current Status of and Changes in the Business Environment



forecast to accelerate. The delay in new housing starts that resulted from revisions in Japan's housing construction code will be resolved gradually, but the decline in the number of housing starts will continue. Also, the industry as a whole is working to identify and stimulate demand for the renovation of the existing housing stock, but a rapid rise in demand is considered unlikely because of such background factors as uncertainty about the future and slow growth in incomes.

Overseas, along with the growing concern for environmental issues, important trends include the encouragement of the use of gas as an energy source and the global shift toward tankless gas-fired water heaters. Economic growth is expected to continue in the developing economies, but competition for raw material resources will give rise to higher prices of basic materials, including crude oil.

Management Vision—Keeping Our Sights on Our 10-Year Goals while Dealing with Sudden Changes in the Operating Environment

To continue our growth in 2011 and beyond, our objective over the next three years is to prepare the way to respond effectively to the major changes in the business environment that have occurred over the past three years. To accomplish this, we must take action in three areas. In Japan, where expansion in demand for household equipment is not expected, we must (1) restructure our domestic business operations and (2) develop new businesses. On the other hand, in overseas markets, where gas-fired household equipment is on an upward trend, we must (3) generate earnings as quickly as possible.

We have three major strategies for taking action in these three areas.

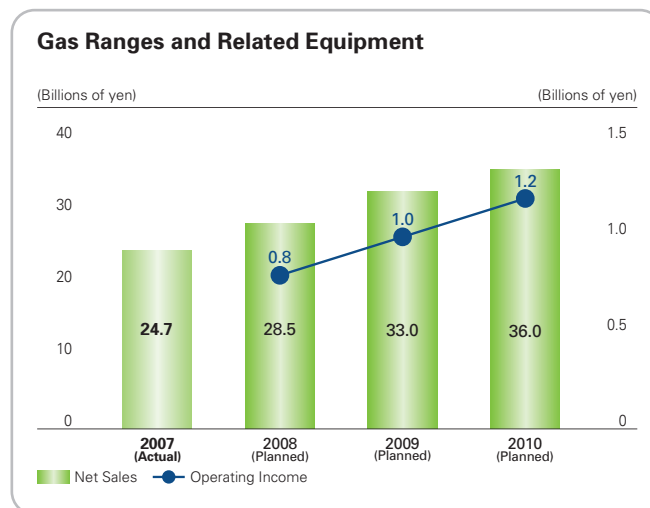
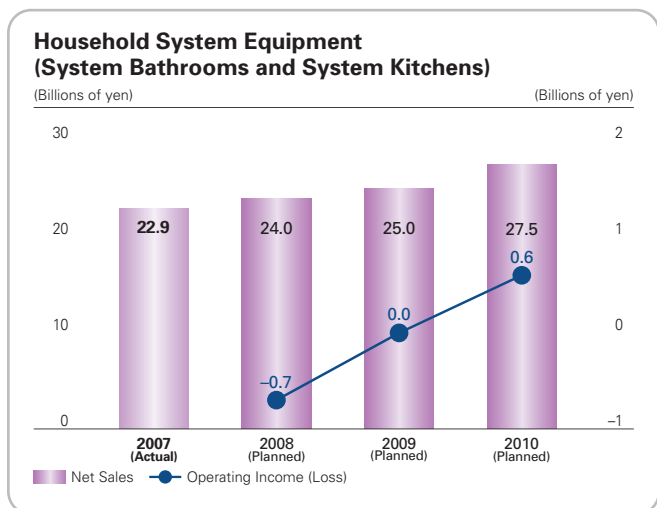
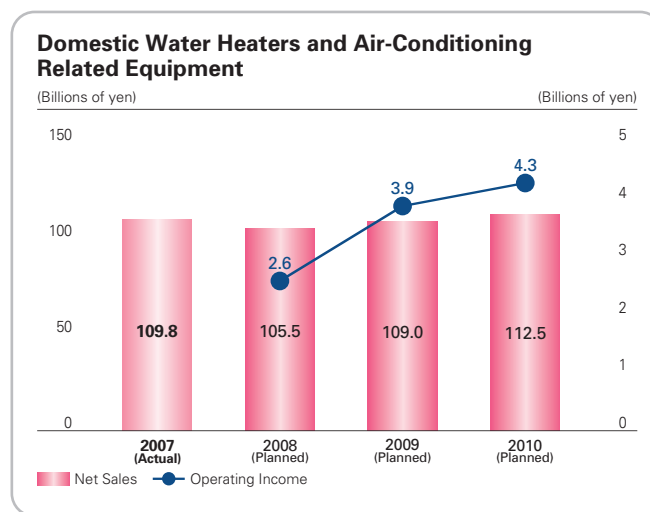
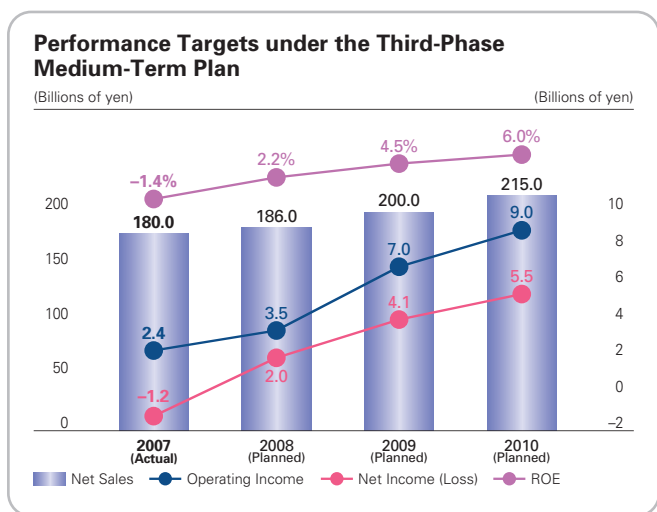
- Our “new value strategy” for implementing structural reform in our existing businesses and shifting our resources to new businesses
- Our “Houresh (house refresh) strategy” for improving our responsiveness to consumers and identifying demand for the renovation of existing housing
- Our “global strategy” for using our management resources in the field of gas-fired equipment to expand our overseas business activities

As we implement these three policies, more so than previously, we must contribute to (1) protecting the natural environment and saving energy as well as (2) enhancing safety and providing peace of mind.

Restructuring Domestic Operations

Although we cannot count on the expansion of demand in Japan for gas- and kerosene-fired water heating equipment, we intend to move ahead with the following specific policies for the realignment of domestic operations.

- Increase the ratio of Noritz sales of high-efficiency water heaters to 20% of total water heaters it sells and increase unit prices
- Newly enter the field of gas fan heaters
- Achieve reductions in manufacturing costs through alliances with other companies in the system bathroom and system kitchen fields
- Work to recover public confidence through periodic inspections at user expense of gas- and kerosene-fired



water heaters that have been in service for a long period. (As a result of accidents involving the gas- and kerosene-fired equipment of other manufacturers in 2006, these units have acquired a reputation having safety problems.)

- Transfer customer relations personnel to city gas and LP gas sales routes to expand sales of household systems equipment (including system kitchens and system bathrooms)
- Expand the area where we apply the direct retail sales model
- In collaboration with Harman, expand sales of gas ranges that have sensors on all burners, as will be required by law

Establishing Our Overseas Operations

During 2007, we completed activities to put our infrastructure in place for selling tankless gas-fired water heater equipment around the world. These activities included establishing sales locations, mainly in North America and China, completing a new plant in Shanghai in 2007, and obtaining certifications for selling gas-fired water heating equipment meeting the standards of various countries. As a result of the initiatives, in 2010, we are aiming for overseas sales of ¥30.0 billion and operating income of ¥2.0 billion. Plans for key products going forward include expanding sales of our tankless water heating equipment for commercial use, which are the first units to obtain American Support Material and Equipment (ASME) certification. At our new plant in China, we have already commenced the production of key parts in-house as well as

finished products and will expand sales not only within China (including Hong Kong) but also exports to Brazil and Europe.

Reforms in Management Structure

To attain our targets for performance, we must expand sales in Japan and reduce operating costs. We plan to work toward cutting fixed costs, including personnel, office-related, and other expenditures, by ¥2.0 billion and reducing costs of materials and major functional parts by ¥1.0 billion annually. Our specific goals are

- Reducing parent company personnel by 10% and
- Integrating and consolidating production and marketing locations for the Noritz Group as a whole.

Return to Shareholders

Noritz's basic policies for providing a return to shareholders are to pay continuing, stable cash dividends and maintain a dividend payout ratio of 35% on a consolidated basis. Basic policies for the use of retained earnings are

- Developing new technologies for addressing environmental issues,
- Improving and expanding the quality assurance system and responding proactively to market quality risk, and
- Developing new business activities.

As we implement our initiatives under the Create 21 Third-Phase Medium-Term Management Plan, we look forward to your continuing advice and support.

April 2008

K. Takeshita

Katsuhiko Takeshita
Chairman and Representative Director

S. Kanzaki

Shigeharu Kanzaki
President and Representative Director

