

A close-up photograph of a child's hands and feet. The child is wearing a light-colored long-sleeved shirt with horizontal stripes and blue denim jeans. The child's hands are positioned as if they are pushing or pulling a wooden toy bus on a light-colored, reflective floor. The background is softly blurred, showing a white wall and a wooden door frame.

Special Feature: Our Efforts towards Sustainable Growth

Creating Warm, Rich Living Spaces

The Sumitomo Forestry Group has now entered a new stage of growth, taking our sustainability and profitability to new heights. We recognize that the more “premium” we receive from our customers, the higher our levels of sustainability and profitability become. We will endeavor to further enhance the advantages we now possess in all our marketing, products, and services with the aim of hearing from our customers that, “the Sumitomo Forestry Group is the one to realize the ‘rich and warm’ living space we have been seeking.”

We will increase the Sumitomo Forestry Group's presence in growth business areas and geographical regions.

No.1



The External Environment Surrounding the Housing and Housing-Related Businesses

—We See Great Opportunities,

but the Environment Still Remains Unfavorable

Housing starts in Japan peaked in fiscal 1997, at 1.63 million starts, then fell steadily through fiscal 2003. Housing starts subsequently began a mild recovery trend, driven by strong demand for built-for-sale houses, rising 2.5% in fiscal 2004 and 1.7% in fiscal 2005. However, in the Sumitomo Forestry Group's main market of owner-occupied housing, starts remain at a low level despite a one-off rise in fiscal 2004. Despite several promising factors—including (1) the increasingly dilapidated state of the stock of non-earthquake-resistant housing; (2) a living environment that lags behind that of other advanced countries; and (3) children of baby boomers entering their first home-buying years,— the current situation still does not permit optimism about significant latent demand turning into actual demand.

Efforts to Address the Situation and Achieve Differentiation

—The Importance of Accurately Assessing Customer Needs

The key is to overcome the competition by tapping what demand there is

Although the overall industry environment still does not permit optimism, this does not mean that we at Sumitomo Forestry think that growth is impossible. In our view, the key lies in how much and how surely we can tap the demand that we see regardless of the macro environment. In other words, we place a great deal of importance on increasing our market share. We are steadily achieving positive results in this respect, which

gives us confidence. The Group's share of owner-occupied housing starts was 1.78% in fiscal 1995, and has risen steadily since then, reaching 2.80% in fiscal 2005.

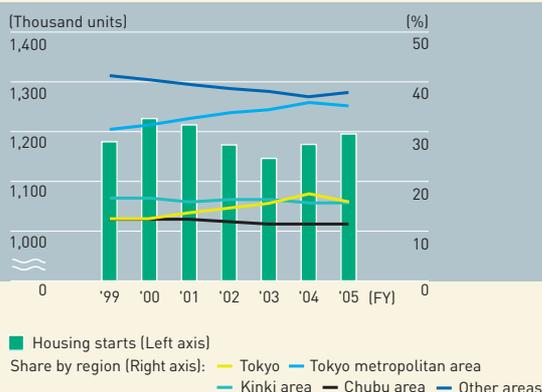
Differentiation in products and services has helped to increase market share

Essentially, this increase in market share means that our customers support us more than before, and that they feel a special attraction to Sumitomo Forestry's products and services that they do not feel toward those of other companies. In other words, the differentiation of our products and services has helped to strengthen the Sumitomo Forestry brand.

Differentiating Factor 1: Design and Product Strength

With lifestyles and values becoming ever more diverse, customers want things that are unique to them. Sumitomo Forestry has been putting effort into built-to-order housing with a high degree of design freedom. The Company has over 1,800 architects, and for each housing unit ordered, assigns an architect to work full time on its design in order to make the customer's dream home a reality. This enables us to give physical shape to our customers' vision regarding everything from overall house layout, exterior, and interior to details such as the width of staircases and the position of lighting fixtures. We have also increased our originality in terms of the materials we use, as we have raised the percentage of domestic timber used in our housing products to 41%, and have achieved a stable supply of specific high-quality timber using our network for timber and building materials procurement. Moreover, we have increased product quality in terms of performance, setting strict standards for air quality and noise and thermal insulation, as well as earthquake resist-

New Housing Starts Nationwide in Japan and Regional Breakdown



Custom-Built Detached Houses Sold by Sumitomo Forestry (Tokyo)



ance, durability, fire resistance, and security. In addition to these standards, we further ensure our product quality by conducting thoroughgoing quality management for each house and taking full responsibility for the work of our construction contractors.

**Differentiating Factor 2:
A Thoroughgoing Customer-First Policy**

One of the four action guidelines in our corporate philosophy is to act with customer satisfaction first and foremost in mind, and we are aiming to create houses that achieve 100% customer satisfaction. One of the most prominent manifestations of this corporate stance is our meticulous after-sales maintenance. In 1999, we established specialized customer service centers in each of our 54 offices nationwide and set up a system to provide telephone consultation 24 hours a day, 365 days a year through call centers staffed with specialist engineers after business hours and on holidays. In April 2003, we introduced the Long Support System, a maintenance program including regular upkeep and remodeling proposals that remains in effect for 60 years from the time of a home purchase. Sumitomo Forestry received a METI (Ministry of Economy, Trade and Industry) Minister Award for Exemplary Consumer Focus in fiscal 2005 in recognition of these efforts. In addition, the percentage of referral orders, which is an indicator of customer satisfaction topped 30% in fiscal 2005, in contrast to the historical average of around 15%.

**Differentiating Factor 3:
Comprehensive Strength and a Track Record as Timber Professionals**

Sumitomo Forestry has been living with and learning from forests and utilizing trees as a renewable resource for over 300 years, since its foundation in the 17th century. The Company has continued to practice sustainable forest management while broadening its

range of operations to include timber and building materials manufacturing and distribution, wooden house construction, and housing-related operations, maintaining timber and housing as the core of its operations. The Company began full-scale operations of custom-built wooden housing in 1975, and thus was not the earliest of Japan's major homebuilders to enter this business. However, thanks to its keen eye for wood and its broad wood building materials procurement capabilities, its technical capabilities—particularly its ability to leverage the qualities of wood in the homebuilding process—and its customer-first mindset, the Company has gained customer recognition as Japan's leading builder of custom-built wooden houses.

Strategies for Accelerating Growth and Improving Sustainability:

—Placing the Focus on Growth Regions and Business Areas

**Strategy 1:
Further Expanding Our Market Share in Growth Regions**

To further expand the lead we have achieved through our differentiation strategy, we intend to carry out an efficient business strategy that involves, in part, placing a priority on establishing operations in areas where demand is likely to increase substantially going forward, and investing resources in such areas. We plan to gradually expand our target regions to Japan's three largest urban areas, and to eventually include all major domestic cities. For the time being, however, we are carrying out measures aimed at increasing our competitiveness through a higher market share in the Tokyo metropolitan area, particularly Tokyo itself. As a stepping-stone to achieving this goal, we aim to record the largest share of owner-occupied housing starts in Tokyo by fiscal 2007. The Company currently has the second largest-share of owner-occupied housing starts in Tokyo, and our immediate goal is to increase housing starts to over 1,000 per year as quickly as possible (we were at 891 units as of fiscal 2004).

Net Sales and Recurring Income Targets for Priority Growth Businesses

(Millions of yen)	FY2005 (Actual)		FY2006 (Plan)		FY2008 (Target)	
	Sales	Recurring income	Sales	Recurring income	Sales	Recurring income
Overseas operations	43,478	1,765	46,000	2,200	52,000	3,700
Housing stock	32,034	1,111	37,200	1,500	45,000	2,300
Remodeling	25,418	723	29,800	1,200	36,500	1,800
Real estate transaction	6,616	388	7,400	300	8,500	500
Collective housing	47,993	826	43,400	600	54,000	1,500

Note: All figures are on a simple aggregate basis (i.e., prior to consolidation adjustments).

Background to and Current Status of the Tokyo Metropolitan Area Strategy

We aim to become the No. 1 company in terms of share of owner-occupied housing starts in Tokyo because construction starts in the Tokyo metropolitan area have remained consistently high, even in periods when they slumped in Japan as a whole, and because we expect them to remain high going forward. Moreover, while the total population of Japan is projected to peak in 2006, the population of the Tokyo metropolitan area is expected to continue trending upward through 2015—a full 10 years after population growth turns negative for the nation as a whole*—with the rate of decline in working population remaining small.

In addition, there are many densely built-up and irregularly shaped parcels of land in Tokyo, and a home-builder needs to have strong design capabilities including the ability to comply with various regulations. This condition allows us to fully demonstrate our design skill and helps us to differentiate ourselves from the competition. If we are able to achieve the top share of the market in the nation's capital, we think it will have a positive effect on our brand. We consider achieving this goal a milestone on the way to greater accomplishments, and once we achieve the top share in Tokyo, we will turn our attention to achieving the top share in the prefectures surrounding Tokyo, as well as the main prefectures of the Kinki and Tokai regions.

* The National Institute of Population and Social Security Research
"Japan's Future Estimated Population" (January 2002)

Efforts to Overcome Our Weaknesses

1) Developing Housing Products for Urban Areas

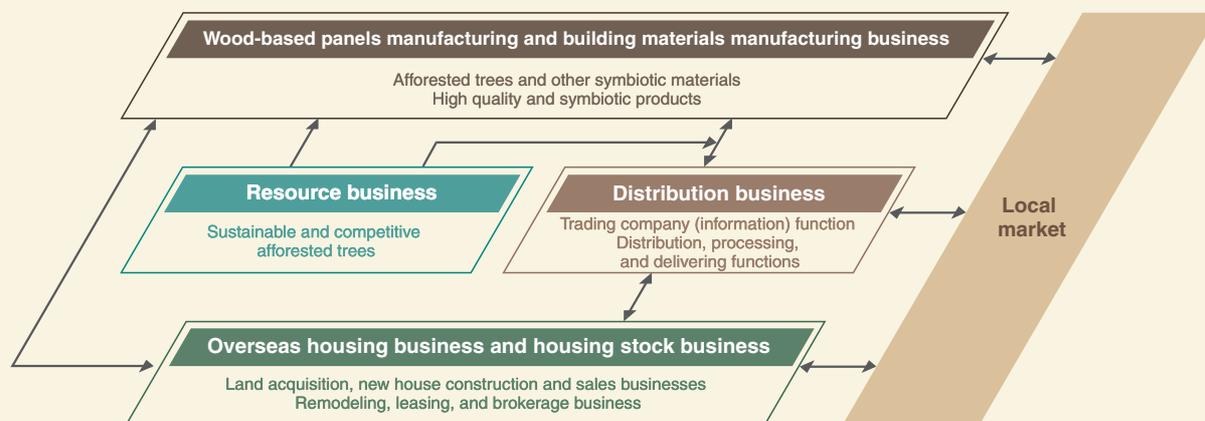
Our previous product lineup was not sufficient to meet the strong demand for three-story housing in urban areas. To bolster our lineup, in fiscal 2005 we launched sales of Proudio-BF, a housing product using the new "Big Frame" method for building three-story wooden houses. In this method, big columns bear the horizontal force, making it possible to attain sufficient strength with fewer walls, thereby greatly increasing freedom of planning, including the freedom to design floor plans with large open spaces. Moreover, Proudio-BF makes use of the skeleton-infill concept, which enables the layout to be changed in accordance with the occupant's lifestyle. We have thereby succeeded in creating a type of housing that can be utilized over several generations, helping to build up a stock of high quality housing.

2) Enhancing Our Sales Network

As part of our efforts to bolster our marketing capabilities in Tokyo, in fiscal 2005 we increased the number of salespeople assigned to the Tokyo area by 18, bringing the total to over 160. We also reviewed our organization, and in April formed a Tokyo Housing Business Division, thereby establishing a system for comprehensively promoting our strategy for all of the Tokyo metropolitan area. In addition, we have established a presentation team tasked with increasing the proposal capabilities of the sales staff, as well as a new marketing group dedicated to tapping corporate sales routes. Going forward, we plan to enhance our efforts to target the approximately 14,000 customers for whom the Group has in the past built houses in Tokyo.

Along with these personnel enhancements, we are working to renovate existing model home displays and build new ones and to strengthen our sales bases. In fiscal

Relations among Overseas Operations



2005 we built three new model home displays and renovated eight others, and in fiscal 2006 we plan to build one new model home display and renovate three others, bringing the number of sales bases in Tokyo to 28. In addition, we are putting greater effort into marketing through means other than our model home displays, such as through “Sumai Haku” housing fairs and other customer-drawing events.

3) Bolstering Land-Related Measures

We are working to strengthen our ability to win customers —primarily first-time homebuyers— who do not have their own land through the Tochi Kara Support System, which supports homebuyers in finding the right plot of land for construction in cooperation with local real estate agents. This business accounted for 7.9% of all orders in fiscal 2003, rising to 11.4% in fiscal 2005.

In addition, as part of our land-related measures, in fiscal 2005 we established a real estate team and with the goal of achieving the top share of owner-occupied housing starts in Tokyo, laid out the framework for accelerating land purchases. In fiscal 2006, we plan to purchase a total of 50 land parcels, for use in our measures to win customers without their own land, including land for constructing built-for-sale housing and land for sale with condition to build.

Strategy 2: Further Cultivating Growth Business Areas

In terms of Sumitomo Forestry’s growth as a company, our most important task is to increase the earnings of our mainstay business. However, it would be decidedly

unhealthy for the Company to become too heavily weighted toward one field. With this in mind, and to further accelerate top-line growth and enable sustainable growth over the longer term, we have identified three businesses —overseas operations, housing stock business, and collective housing business— as priority growth businesses, and are allocating resources to these businesses on a priority basis. Although all three of these businesses are quite small at present, we boast the fact that we established the housing business as a new undertaking in 1975, and the Housing and Housing-Related Business now accounts for 56% of consolidated sales. We have steadily established secure footholds in these priority growth businesses based on meticulous surveys, and going forward we plan to prudently, yet aggressively, build out these businesses.

Overseas Expansion

We are expanding our overseas operations, primarily our building materials manufacturing operations in the Pacific Rim. Through the importing operations of our timber and building materials distribution business, we have built a relationship of trust with various nations, and have expanded overseas operations based on thorough surveys of the political and economic situations in these nations. This has enabled us to achieve a strong track record and a long history in this area. With some of our overseas manufacturing bases having histories that go back over 30 years, we have built solid regional bases. Today, we view the emergence of various Asian nations —most notably China— and the growth of the U.S. housing market as major new business opportunities.

State of Progress in Overseas Housing Operations

	North America	China
Date launched	September 2002	November 2004
Results	Local joint-venture Bennett-SFS L.L.C. established; 56 houses in eastern Seattle sold as of the end of 2004	30% equity stakes taken in Paragon Wood Product (Dalian) Co., Ltd. and Paragon Wood Product (Shanghai) Co., Ltd.
Current status	Roughly 200 built-for-sale houses currently being constructed (as of August 2005)	Participating in a high-end detached housing project in Shanghai since February 2005, with construction beginning in July
Target	120 houses/year	To be determined
Policy going forward	Brand creation and expansion into peripheral businesses and other regions to be considered following establishment of business model	Establishment of cooperative relations with leading developers in the Shanghai region, leading to increased awareness of the Group in China, spread of wooden housing, and future expansion of operations

Primarily through our new International Business Headquarters, established in April 2004, we are working to expand our new businesses by leveraging the expertise and networks accumulated by our existing businesses, while closely cooperating with various bases.

1) Strategy for Further Expanding the Timber and Building Materials Business

The Timber and Building Materials segment supplies timber and building materials not only to the Japanese market, but also to various Asian nations, the U.S., and Europe through a local affiliate in Singapore and US subsidiary Pacific Wood Products L.L.C. It is also working to open new markets by aggressively conducting, through third-country trade, export-import operations in areas where the housing market is likely to be buoyant going forward.

In fiscal 2005, Sumitomo Forestry formed a strategic operating alliance with Dongwha Holdings Co., Ltd. Korea's largest building materials manufacturer, and acquired 10% of the outstanding shares in Dongwha Enterprise Co., Ltd., the core member of the Dongwha Holdings group. Through the alliance with Dongwha Enterprise Co., Ltd., which owns Korea's first MDF factory and its largest particleboard factory, Sumitomo Forestry aims to expand sales in Korea, and to accelerate the development of a wide-area market linking Japanese and overseas bases.

2) Expanding Housing Business in Promising Markets

We began building and selling detached houses built using two-by-four in the U.S. in 2002. In November 2004, we entered the wooden home business in China. In the latter market, the development of the housing market is a core element of economic policy, and in January 2004 the Chinese government implemented the Code for

Design of Timber Structures. In our view, this raised the profile of wooden housing in China, and helped to create an environment for the adoption of wooden housing on a full scale.

There are many issues that must be solved to expand housing operations in overseas markets, which have cultures and operating environments different from Japan's, and we believe we are not underestimating these issues. To enable the steady expansion of new operations, we confirm the profit potential of such operations through feasibility studies, minimize risk by promoting diversification in all aspects of operations, and formulate plans cautiously.

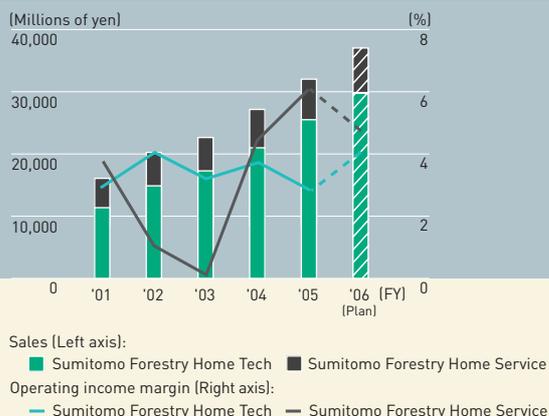
Expansion into Peripheral Fields

1) Housing Stock Business

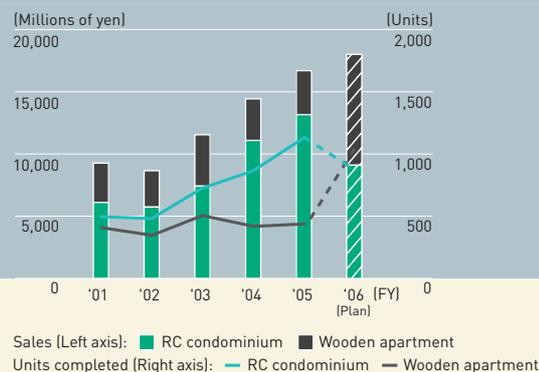
Better housing quality has lengthened the replacement cycle and made it common for people to move or rebuild not because their existing home has become dilapidated, but because they have entered a new stage of life. We believe demand for remodeling and the number of existing homes on the market will increase significantly going forward. The emphasis of the nation's housing policy has shifted from new construction to the utilization of existing stock, and we think this trend will become more pronounced. Wooden houses account for over 90% of Japan's 26-million-unit stock of detached houses, and as experts in the field of wooden houses, we think we are in an extremely advantageous position in this growth market.

Because we expanded our network of business offices and strengthened our marketing capabilities in fiscal 2005, we delayed reaping some of the profits we otherwise might have realized. However, with the steady increase in sales, we aim to achieve our medium-term numerical targets (¥45.0 billion in sales and ¥2.3 billion in recurring income in fiscal 2008).

Housing Stock Business: Sales and Operating Income Margin



Collective Housing Business: Sales and Number of Units Completed



1. Remodeling Business

We have finished building out our business office network nationwide, and we are now working to bolster our sales capability so we can tap the market to the utmost. In fiscal 2005, we hired 102 salespeople and construction supervisors (primarily mid-career employees), bringing the total to 450. In addition, in Osaka we built our first model home display specifically for marketing our remodeling operations. As this has helped to boost renovation orders, proving highly cost-effective, we built a second such model home display in the Hyogo area, and plan to build others in the future.

2. Real Estate Transaction Business

Having close ties to the community is fundamental to our real estate transaction business, and in fiscal 2005 we continued working to augment our business office network in the Tokyo metropolitan area. We also added five locations (three in the Tokyo metropolitan area, one in the Kinki area, and one in the Chukyo area), bringing the total to 51. In addition, to enhance our ability to draw customers via the Internet, in November 2004 we launched Suminavi, an online marketing support system that uses weblogs to enable person-to-person communication between salespeople and customers. At present, Suminavi's content is limited to sales brokerage, but going forward we plan to add content related to leasing and remodeling.

2) Collective Housing Business

It is important to tap leasing demand in urban areas, particularly among younger customers. In the collective housing business, the Collective Housing Headquarters is working to increase benefits derived from tie-ups with Sun Step Co., Ltd., a company added to the Group in August 2003, and it is generating synergies not only in

lease management of leased buildings but also in joint marketing with Sun Step and in the provision of land data received from the owners of the leased properties it manages.

The collective housing business has eight business offices, located primarily in the three main urban areas. It plans to bring this number to 12, and to increase the number of employees to 300 by fiscal 2008. In fiscal 2005, it increased its workforce by 15, primarily hiring employees skilled in land-use consultation, bringing the total to 155.

As part of the effort to bolster our lineup of apartment products, we introduced Succeed M-trust, the Company's first post-and-beam wooden apartment building in which we can leverage our expertise accumulated through the detached housing business. We plan to strengthen and expand our apartment business going forward, and hope to increase the ratio of apartment orders to total orders of collective housing to 50% in the future. In addition, Sun Step expanded its short-term-lease condominium business, as it expects this market to grow, and currently has seven properties that it owns or sub-leases. Going forward, we will continue to invest aggressively in this area, while keeping a firm eye on land-use conditions.