

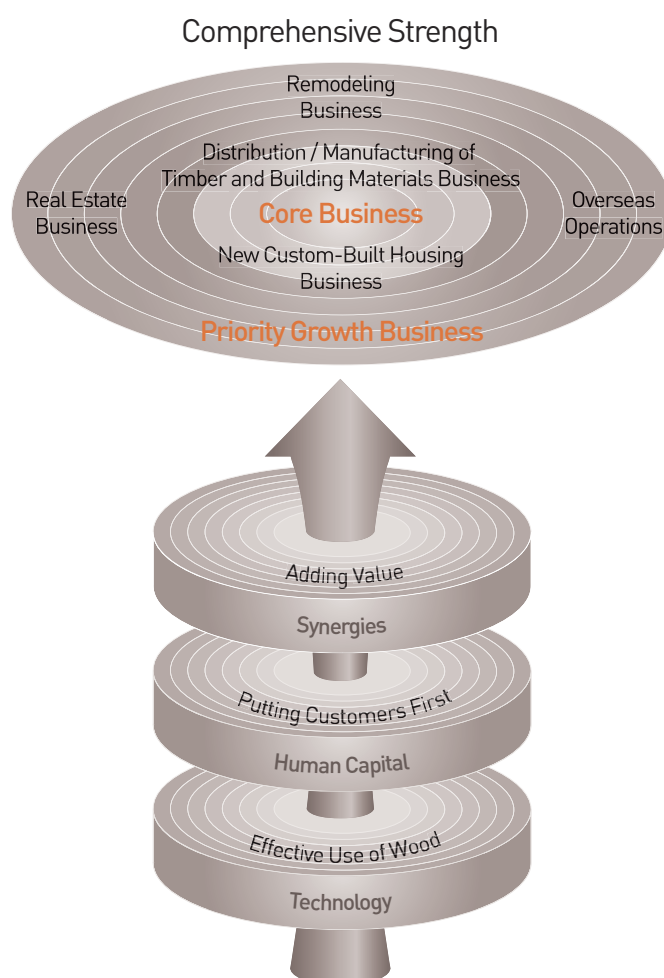
# Annual Report 2007

(Year ended March 31, 2007)



# A TOTAL HOUSING AND WOOD PRODUCTS BUSINESS FOR WOOD-BASED HOUSING ENVIRONMENTS

The Sumitomo group established Sumitomo Forestry in 1691 in conjunction with the opening of the Besshi copper mine to manage the surrounding forestland and the wood material production cycle of timber cultivation, preservation, and harvest. Sumitomo Forestry entered the new custom-built housing business in 1975 and has established its status as the consummate “wood professional” using its knowledge and technology of timber and wood living environments accumulated over more than 300 years. With the forestry business as the foundation, we offer products and services as a total housing and wood products business encompassing timber and building material manufacture and distribution operations, construction and sale of new custom-built housing, remodeling, real estate operations, landscaping and natural environment development, and operations overseas.



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### Forward-Looking Statements

Statements in this annual report with respect to Sumitomo Forestry's plans, strategies, and objectives as well as other statements that are not historical facts are forward-looking statements based on management's assumptions and beliefs formed in the light of information available as of the production of this report. Actual results may differ from those discussed in these forward-looking statements owing to the impact of various factors, including but not limited to changes in the business environment, general economic conditions, and customer preferences.



## HOUSING MARKET

Market Trends are Not Promising but there are Many Opportunities for Our Growth

*The Japanese housing market has moved beyond the growth phase and is reaching maturity.*

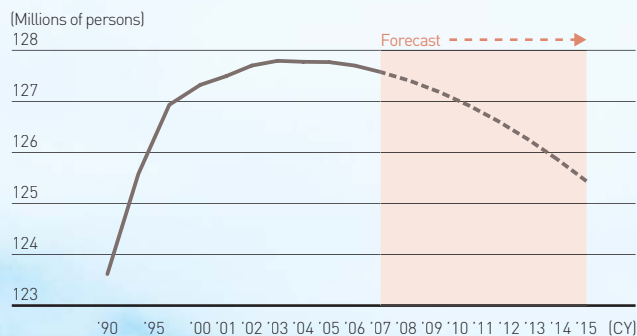
*While we cannot expect the overall market to expand significantly in the future,  
the Sumitomo Forestry Group sees a market with numerous growth opportunities in segments and  
business areas that it has yet to develop.*



## HOUSING MARKET

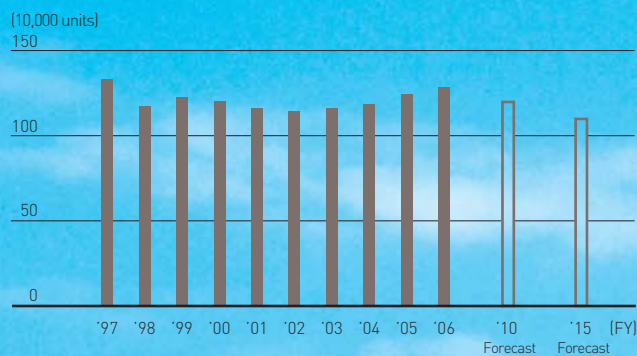


### Population Trend



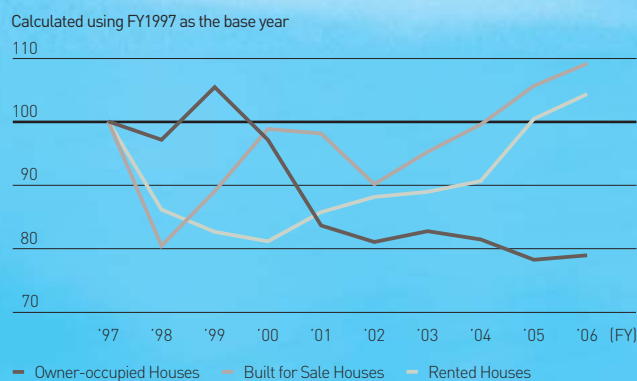
**Japan's Declining Population:** According to the 2005 national census, Japan's total population began declining after reaching a peak of 127.83 million people in December 2004. Changes in lifestyles in favor of marrying later or not marrying have contributed to lowering the birthrate to a current level of about 1.3. This level precludes expectation of a quick recovery in population growth and gives credence to forecasts for the Japanese population to shrink to below 100 million people in 30-40 years.

### Housing Starts Demand Forecast



**Declining New Housing Starts:** Housing purchase demand is currently strong as the present economic environment is supporting improving employment and income levels. However, the market's structural elements of the declining population and growing volume of housing stock indicate that new housing starts will gradually decline over the long term.

### Housing Starts Index by Housing Type



**Owner-occupied Housing Starts:** Since land prices were perceived as hitting bottom in 2001 the boom in condominium demand centered on urban redevelopment has been supporting the volume of new housing starts. Our core business segment of new custom-built housing, however, correlates closely with owner-occupied housing starts, and the segment's growth has stalled in recent years.

Japan's declining birthrate and growing proportion of elderly people has combined to create a period of decreasing population.

These conditions are producing an inevitable decline in the number of the main group of first-time housing buyers - young buyers - and we anticipate a long-term declining trend of new construction housing demand (flow) down to a lower sustainable level.

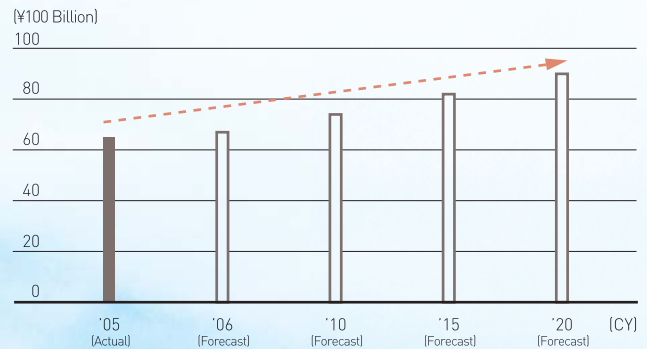
Short-term market trends present a contrast of declining demand for owner-occupied housing alongside rapidly growing demand for built-for-sale housing based on a sense that land prices are bottoming and fueled by urban redevelopment.

## NOT A PROMISING MARKET FOR MANY HOUSING COMPANIES



## HOUSING MARKET

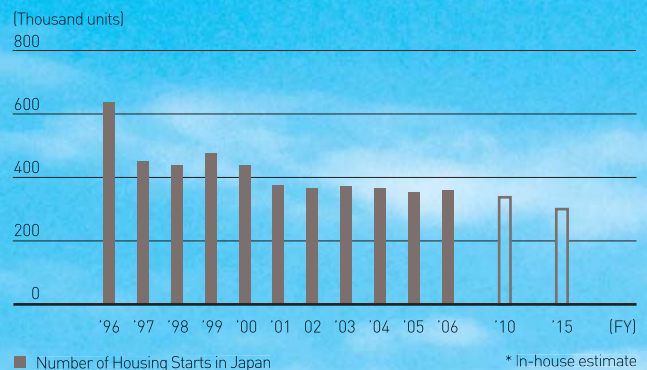
## New Trends in the Remodeling Market



Source: "House Renovation Market 2006", published by Yano Research Institute Ltd.

**Scale of the Remodeling Market:** While the Japanese population started declining at the end of 2004, the volume of housing stock is expected to continue to grow. In addition, demand for remodeling construction is expected to grow. The average lifespan of Japanese homes is estimated to generally be 30 years, which means that current homeowners of the large number of houses built in the 1970s can be expected to generate remodeling demand for earthquake resistance upgrades, to replace major equipment, and also to raise the asset value of their homes.

## Trends in Owner-occupied Housing



**Owner-occupied Housing Demand:** Residential construction starts are expected to decline by about 10% in the next few years. While this will undoubtedly impact the majority of home builders, we believe our company will be relatively unaffected by this trend because of our focus on high-quality housing products that we believe will be well suited to the growing demand for higher quality residential housing. In addition, we are moving into a period when a large volume of the baby boomer generation will be reaching retirement age, and we expect this group to expand demand for personalized homes and relocation-related demand as they seek to establish lifestyles suited to their retirement activities.

## Main Points of the Basic Housing Act

	Current		Planned
Housing Stock Meeting New Earthquake Resistance Requirements	75% (2003)	➡	90% (2015)
Housing Stock with Energy Efficiency Measures	18% (2003)	➡	40% (2015)
New Construction with Housing Performance Disclosure	16% (2005)	➡	50% (2010)

**The Basic Housing Plan Outline:** The government's Basic Housing Plan extends from fiscal years 2006 to 2015 and emphasizes a shift in government housing policy from quantity to quality. The plan focuses on such items as improving housing safety by raising earthquake resistance and improving energy efficiency in anticipation of tighter efficiency regulations in the future.



The Japanese government has responded to the changing environment of the housing market, which includes diversifying and more sophisticated residence needs, the new society structure of shrinking population and household numbers, and tightening environmental regulations, by adopting the Basic Housing Plan that shifts the emphasis of the basic housing policy from quantity to quality.

The policy is essentially intended to help realize a society in which the general public can truly feel and reflect the nation's affluence.

The maturing housing market means that the housing construction policy no longer needs to support construction flow, and can now focus on qualitative improvement of living standards, including the residential environment, and the creation of a stock of quality housing for future generations.

These changes in the housing business environment represent a market shift toward the product quality that Sumitomo Forestry has been developing and opens doors for new business opportunities and growth for the company.

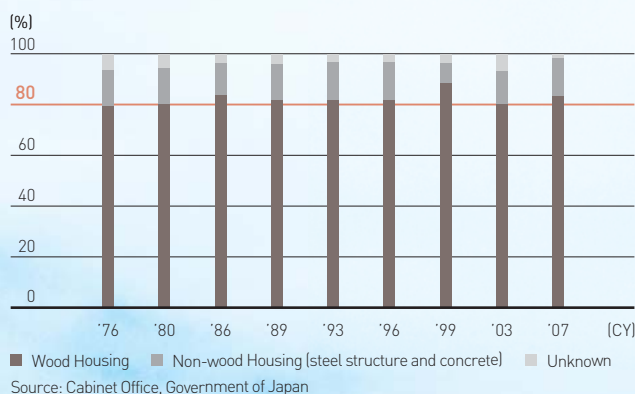
## BUT A PROMISING MARKET FOR US





## HOUSING MARKET

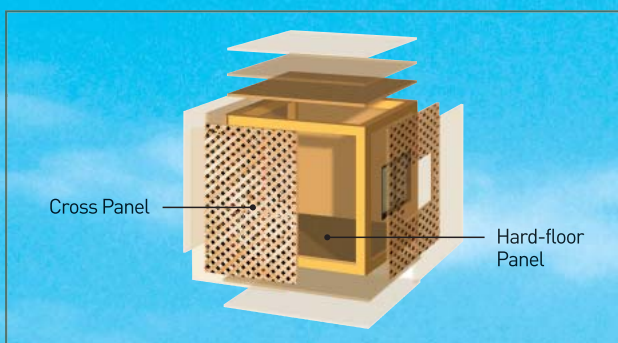
### Wood or Non-wood for Future Living?



**Preference for Wooden Housing:** A survey by the Cabinet Office of the Government of Japan found that over 80% of Japanese people desire wooden housing, a sign of strong support for wooden housing despite the recent boom in condominium demand. Sumitomo Forestry's focus on supplying wood materials and quality products has established us as Japan's leading\* supplier of wooden custom-built homes.

\* "Analysis of Housing Manufacturer Competitiveness, 2007" published by Jutaku Sangyo Kenkyujo Co., Ltd.

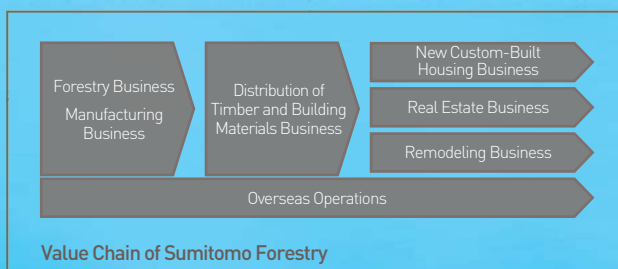
### Sumitomo Forestry's Multi-balance Construction



**Sumitomo Forestry's "Wooden Homes":** The in-house developed multi-balance construction method used to construct our "MyForest" series homes emphasizes our expertise in drawing out the unique features of wood and enables us to create wooden homes of unequalled durability and living comfort. In addition to the high quality of our products, we also offer extensive support services, such as the "60-year Support System" to assist customers in maintaining and improving the quality of their homes. These and other activities are designed to support and promote each customer in realizing his or her ideal home.

\* **Multi-balance Construction:** An integrated system of posts, beams, and panels prevents excessive stress from accumulating at joints and limits structural deformation or contortion caused by strong external forces, such as a large earthquake or destructive storm. The building structure is further strengthened by the panels themselves, which provide additional reinforcement if structural contortion were to occur.

### Sumitomo Forestry's Comprehensive Strength



**Comprehensive Strength:** The Sumitomo Forestry Group provides wood and housing lifestyle products at every stage of the process, from forest management to timber and building material manufacture and distribution, to new custom-built housing and remodeling. The comprehensive strength of the Sumitomo Forestry Group sets us apart from competitors and provides a foundation for developing the growth potential of the group. Our intracompany business activities across all stages of the operating chain are key components for raising the group's efficiency in business development and realizing other synergy advantages.



The all-encompassing reach of our value chain from upstream to downstream, beginning with timber cultivation through housing material production and distribution to housing construction, places the Sumitomo Forestry Group in a unique position in the housing industry.

This comprehensive strength of the Group, our emphasis on product quality, and our customer-first ethic to make us the industry's leading supplier of wooden custom-built homes.

We plan to optimize our management resources, including the technology and manpower capacity that are the primary sources for the Group's competitiveness, to continue expanding our global operations and generate additional synergies among our businesses.

This will further enhance our overall strength and establish sustainable business growth into the future.

## OUR ADVANTAGE IN THE MARKET



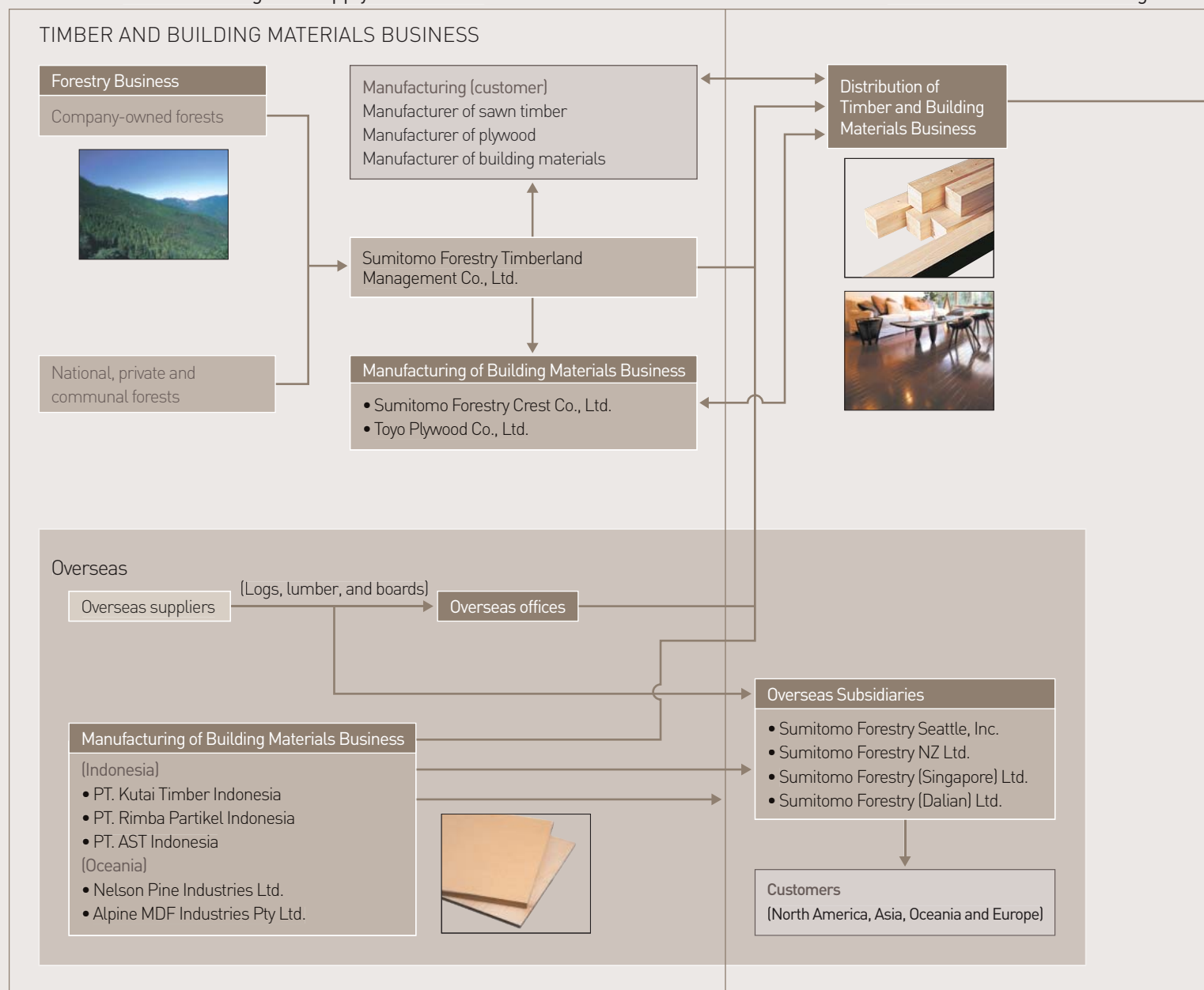
# OUR COMPREHENSIVE STRENGTH — VALUE CHAIN —

## BUSINESS STRUCTURE OF SUMITOMO FORESTRY

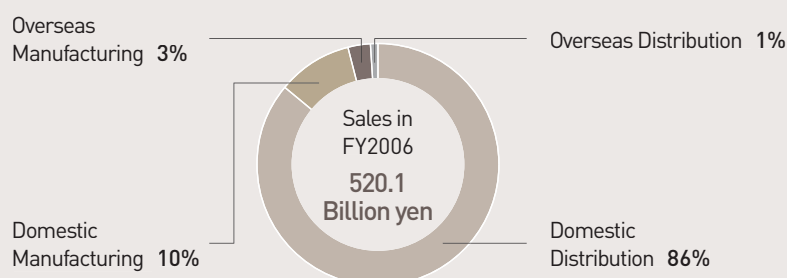
Based on our expertise in the profession related to the gift of nature “wood” and to providing customers with rich “living”, The Sumitomo Forestry Group is building a value chain that can meet all needs.

### UPSTREAM: Manufacturing and Supply of Materials

### MIDDLESTREAM: Distribution and Processing



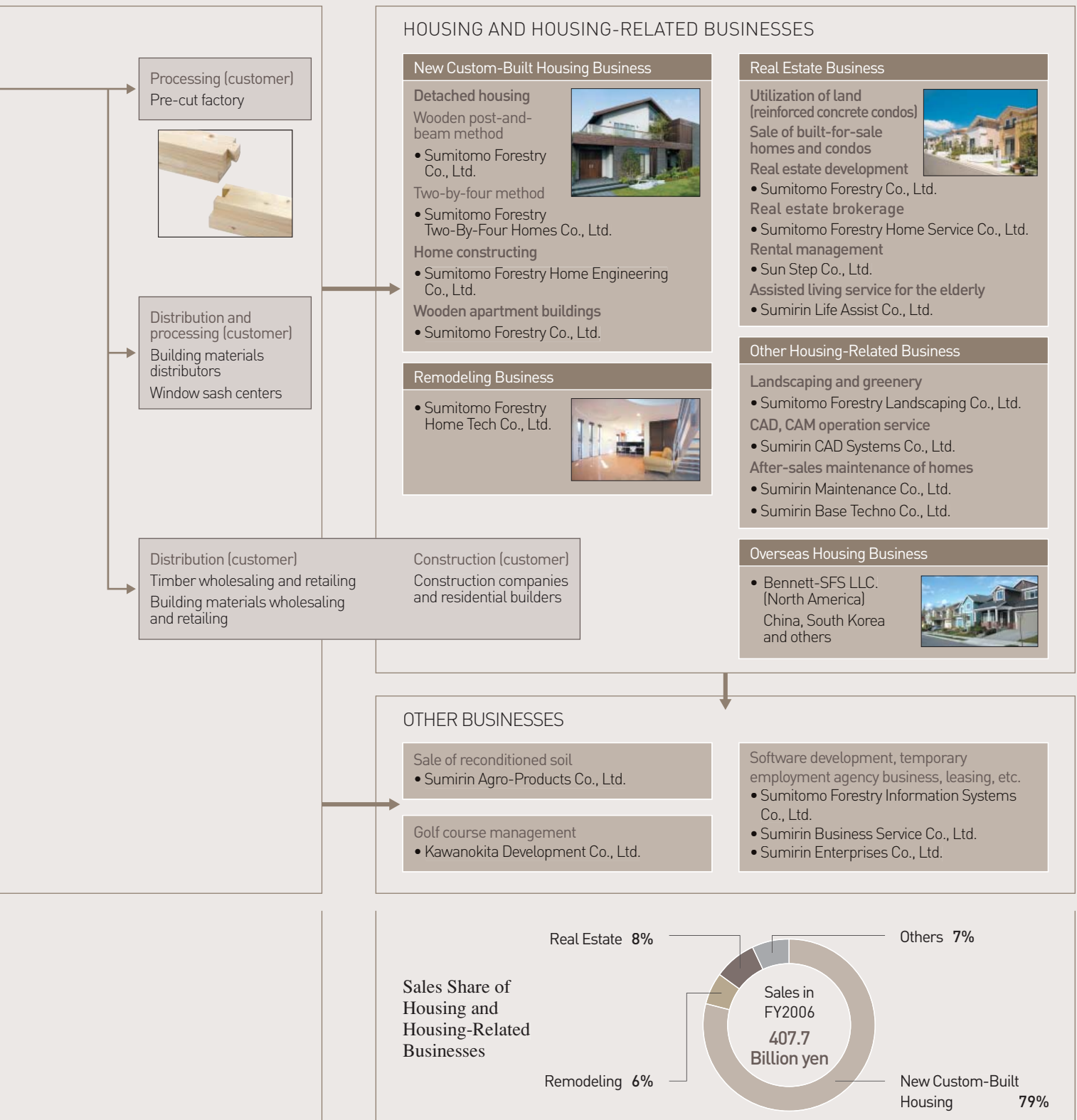
### Sales Share of Timber and Building Materials Business



Note: Figures for each segment include inter-segment transactions.

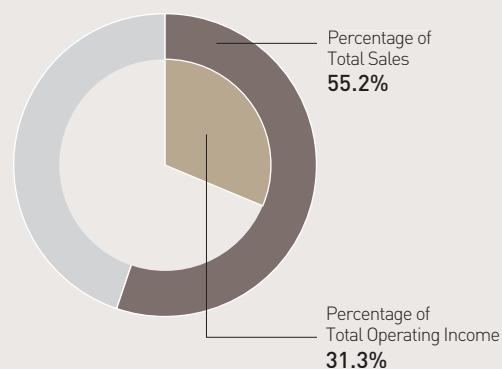


## DOWNSTREAM: Consumer Business

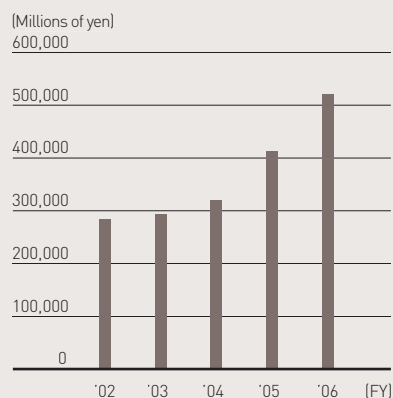


# AT A GLANCE

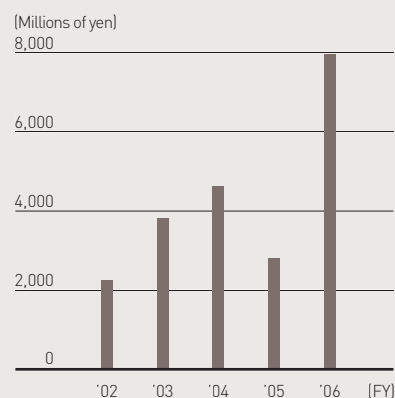
## TIMBER AND BUILDING MATERIALS BUSINESS



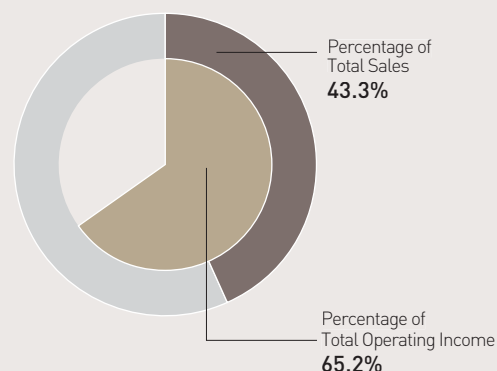
### Net Sales



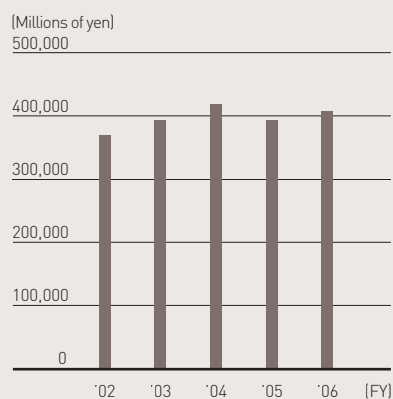
### Operating Income



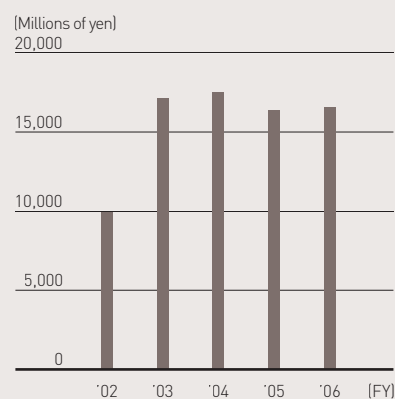
## HOUSING AND HOUSING-RELATED BUSINESSES



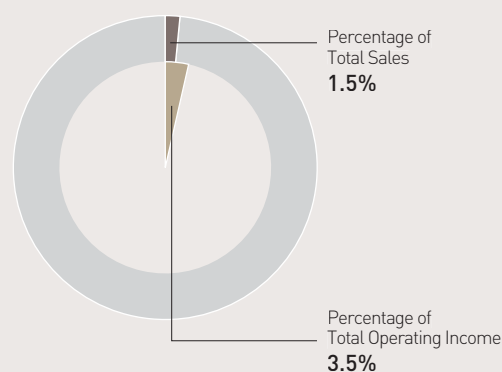
### Net Sales



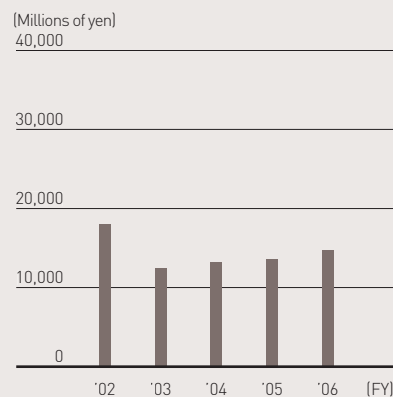
### Operating Income



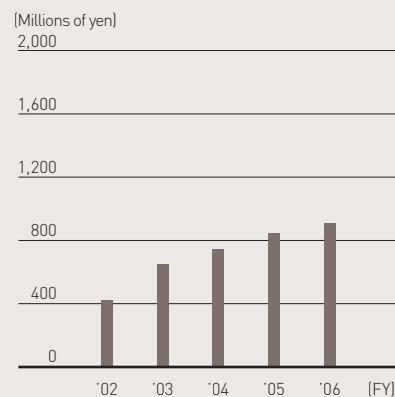
## OTHER BUSINESSES



### Net Sales



### Operating Income



Notes: 1. Business segment percentages include fiscal 2006 intersegment transactions.  
2. Business segment sales and operating income figures include intersegment transactions.



	Forestry Business (Domestic and Overseas Operations)	The Forestry Business efficiently manages some 40,000 hectares of company-owned forestland utilizing cyclical forest management based on a principle of “sustainable forestry” through a continuous cycle of harvesting and planting. Our overseas operations likewise follow management principles centered on planted timber and the promotion of sustainable timber resources.
	Manufacturing of Building Materials Business (Domestic and Overseas Operations)	The Manufacturing of Building Materials Business produces and processes a variety of building components focusing on wooden materials, such as boards and interior materials, and storage units. It does so using an integrated production system, extending from the selection of timber to the processing of products. Overseas operations manufacture and process panels such as medium density fiberboard (MDF), plywood, particleboard, and other wooden board materials from timber.
	Distribution of Timber and Building Materials Business (Domestic and Overseas Operations)	The Distribution of Timber and Building Materials Business's worldwide distribution network has made it Japan's leading trader of timber and building materials in terms of trading volume. The overseas business is expanding its operations in Asia in anticipation of a growing market in the region for timber and building materials.
	New Custom-Built Housing Business (Detached Housing and Collective Housing)	The New Custom-Built Housing Business's dedicated team system for marketing, design, production and interior refinement for each house provides a full-fledged custom-built house taking full advantage of the appeal of wooden materials and answering specific customer requirements.
	Remodeling Business	Sumitomo Forestry Home Tech Co., Ltd. applies its original in-house developed technology, along with technology honed in our Custom-Built Housing Business, to transform buildings and other structures into fresh and functional living spaces.
	Real Estate Business	The new Real Estate Business Division, created in April 2007, is focusing on five core operations: effective utilization of real estate holdings, real estate development, built-for-sale housing, real estate sales and brokerage, and real estate management. The new division applies its original planning capabilities, an extensive information network accumulated and cultivated over many years, and integrated activities with other business divisions with the objective of developing quality housing and facilities that meet the needs of society.
	Overseas Housing Business	The Overseas Housing Business provides high-quality wooden structure homes featuring the best characteristics of Japanese home designs adapted to local sensibilities. Currently focused on the Seattle region of the United States, operations are also being developed in China, Korea, and other regions.
	Other Housing-Related Businesses	Other operations include general exterior landscaping and urban environment improvement businesses, which support elegant housing environments using abundant natural greenery, flowers, and other outdoor ornamentation for terraces, gardens and other housing features.
	Lifestyle-Related Business	The Lifestyle-Related Business offers a diverse range of services, including the production and sales of farm and garden materials, insurance brokerage, and information systems and leasing services, which contribute to secure and fulfilling lives of our customers and society as a whole.

# FINANCIAL HIGHLIGHTS

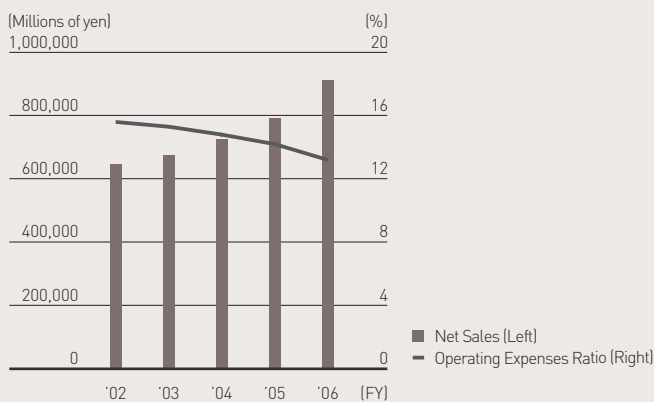
Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
Years ended March 31

	Millions of yen					Thousands of U.S. dollars*1
	2007	2006	2005	2004	2003	2007
<b>Operating Results:</b>						
Net sales and contract revenues	¥ 911,674	¥ 791,128	¥ 723,193	¥ 673,779	¥ 645,100	\$ 7,661,129
Gross profit	141,117	127,853	125,582	120,778	109,631	1,185,854
Selling, general and administrative expenses (SG&A expenses)	120,711	112,407	107,116	103,201	100,858	1,014,382
Capital investment	9,026	10,443	9,237	6,392	5,123	75,852
Operating income	20,405	15,446	18,466	17,577	8,772	171,472
Recurring income*2	21,259	16,800	18,692	17,074	9,721	178,649
Net income (loss)	11,954	10,842	8,014	9,870	(15,439)	100,452
<b>Financial Position:</b>						
Total assets	500,136	464,193	370,684	369,755	357,322	4,202,822
Interest-bearing debt	25,739	22,067	15,580	19,929	16,497	216,297
Total net assets*3	188,855	175,206	152,500	146,269	129,727	1,587,013
<b>Cash Flows:</b>						
Cash flows from operating activities	7,084	16,626	6,685	25,962	19,734	59,533
Cash flows from investment activities	(7,102)	(8,998)	(12,895)	(7,646)	2,026	(59,679)
Cash flows from financing activities	665	(14,039)	(7,087)	(735)	(8,171)	5,586

	Yen					U.S. dollars*1
	2007	2006	2005	2004	2003	2007
<b>Per Share Data:</b>						
Net income (loss)	¥ 67.43	¥ 61.28	¥ 45.28	¥ 55.81	¥ (87.53)	\$ 0.57
Net assets	1,059.20	996.03	866.47	830.50	736.42	8.90
Cash dividends	15.00	13.00	13.00	13.00	10.00	0.13

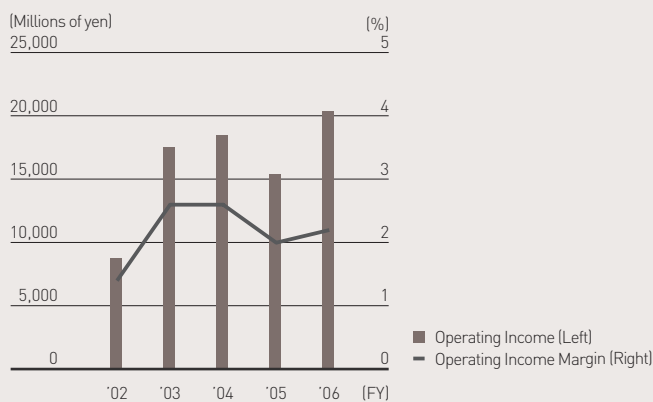
## Net Sales and Operating Expenses Ratio



Note: Operating Expenses Ratio=SG&A Expenses/Net Sales and Contract Revenues

**Net Sales:** Net sales for the Timber and Building Materials Business increased 26.2% year on year on higher product prices and increased business volume along with full-year contributions from newly incorporated subsidiaries acquired in the previous year. Net sales for the Housing and Housing-Related Businesses rose 3.5%, primarily on high-unit prices for completed units.

## Operating Income and Operating Income Margin



**Operating Income and Operating Income Margin:** Operating income increased 32.1% year on year and the operating income margin rose 0.2 percentage points as market conditions supported substantial earnings growth for the Timber and Building Materials segment.



	%				
	2007	2006	2005	2004	2003
<b>Financial Ratios:</b>					
Operating income margin	2.2	2.0	2.6	2.6	1.4
Return on assets (ROA)*4	4.4	4.0	5.0	4.7	2.7
Return on equity (ROE)*4	6.6	6.6	5.4	7.2	(11.1)
Equity ratio	37.5	37.7	41.1	39.6	36.3
Interest-bearing debt ratio*5	12.1	11.2	9.3	12.0	11.3
<b>State of Orders (on a unit basis):</b>					
Custom-built detached housing	9,751	9,251	10,076	10,529	10,538
Collective housing	1,455	1,288	1,776	1,655	1,227
<b>State of Sales (on a unit basis):</b>					
Detached housing	9,645	9,807	10,319	10,542	10,552
Collective housing	1,445	1,082	1,571	1,266	1,220
<b>Number of employees</b>					
	12,259	11,997	10,477	10,418	10,378
<b>Reference Market Data:</b>					
New housing starts (nationwide)	1,285,246	1,249,366	1,193,038	1,173,649	1,145,553
New housing starts (Tokyo metropolitan district)	431,200	432,005	419,088	422,750	393,296
Owner-occupied housing starts (nationwide)	355,700	352,577	367,233	373,015	365,507

Notes: 1. Japanese yen amounts have been translated into U.S. dollar amounts, for the reader's convenience only, at the rate of ¥119=US\$1, the approximate exchange rate prevailing in the Japanese foreign exchange market at March 31, 2007.

2. Recurring income = Operating income + Non-operating income – Non-operating expenses

Non-operating income includes interest income, purchase discounts, dividends income, foreign exchange gains, miscellaneous gains, and other income generated from normal business activities. Non-operating expenses include interest expense, sales discounts, loss on devaluation of property, plant and equipment, foreign exchange losses, miscellaneous expenses, and other expenses from normal business activities.

3. Total net assets are presented following enforcement of the new Japanese Corporate Law in 2006. Total net assets are comprised of the sum of shareholders' equity as previously defined and minority interest and gains (losses) on deferred hedges.

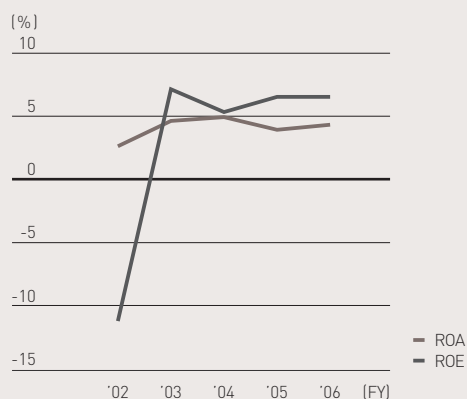
4. ROA and ROE are calculated using the simple average of beginning and end of term balance sheet figures.

ROA = Recurring income / Total assets

ROE = Net income (loss) / Shareholders' equity

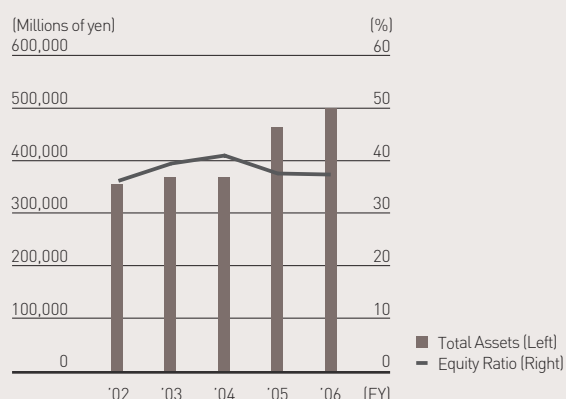
5. Interest-bearing debt ratio = Interest-bearing debt / (Interest-bearing debt + Shareholders' equity)

## ROA and ROE



**ROA and ROE:** Return on Assets increased 0.4 percentage points from the previous year on a 7.7% rise in total assets and 26.5% growth in recurring income. Return on Equity held steady at 6.6% as net income increased 10.3% and shareholder's equity rose 7.1%.

## Total Assets and Equity Ratio



**Total Assets and Equity Ratio:** Total assets rose by ¥35.9 billion on an increase in notes and accounts receivable accompanying the rise in sales and expanded acquisitions of real estate for resale. The Equity Ratio declined by 0.2 percentage points.

## TO OUR STAKEHOLDERS

The company achieved significant increases in sales and profits in all segments in fiscal 2006. The Timber and Building Materials Business continued to expand business in Japan and overseas, which along with improving business conditions helped raise segment operating income by roughly triple the previous year result. The promotion of high value-added housing in the Housing Business lead to a large increase in earnings for the overall company. In looking toward the future and in anticipation of the ongoing evolution of the business environment, during the year we launched the 10-year long-term management plan “Project SPEED” to guide our growth to the year 2016.

### REVIEW OF FISCAL 2006 RESULTS

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#### Owner-Occupied Housing Starts Rose for the First Time in Three Years

In the housing industry, rising land prices in metropolitan regions and expectations of higher housing loan interest rates spurred first-time homebuyer demand as overall new housing starts expanded 2.9% year on year to 1.28 million units. Among the most dynamic trends during the year was the 3.3% rise of built-for-sale houses as the condominium boom continued and the 3.9% growth of rental housing supported by the increase in real estate funds. Another important trend during the year was the first improvement in three years in Japan’s owner-occupied housing starts, highly related to our business, which rose 0.9% year on year to 350,000 units.

In the timber and building materials sector, the rapidly expanding economies of emerging nations are generating increasing demand for timber and tightening the supply and demand balance in the global market. In Japan, the increasing demand for timber paralleling the rise in new housing starts is stimulating the domestic market, including rises in product prices.

#### Profits Accelerated on Brisk Timber and Building Materials Business

In this overall environment, Sumitomo Forestry Group net sales and contract revenues increased ¥120.5 billion, or 15.2%, year on year to ¥911.6 billion. A substantial ¥72.0 billion of this growth is attributable to Toyo Plywood Co., Ltd., Ataka Kenzai Co., Ltd., and other recently consolidated companies in the Timber and Building Materials Business that provided a full-year of earnings contributions.

Operating income rose 32.1% year on year to ¥20.4 billion and recurring income rose 26.5% year on year to ¥21.2 billion. Profits were boosted by higher product prices in the Timber and Building Materials Business as well as the effects of the promotion of high value-added housing in the Housing Business. Net income in fiscal 2006 increased 10.3% year on year to ¥11.9 billion as taxes settled back to their normal level.



Ryu Yano  
President / Director



## Overview of Segment Results

### *Timber and Building Materials Business*

*Sales +26.2%, Operating Income +183.9%*

Net sales in the Timber and Building Materials segment grew 26.2% year on year to ¥520.1 billion and operating income rose 183.9% to ¥7.9 billion. Domestic Distribution sales volume expanded on the merger with Ataka Kenzai Co., Ltd. and from stronger collaborative ties with our business partners. The global market for timber was very active during the year and the tight supply and demand balance around the world supported higher prices for timber and wood panels, which pushed profits higher. The Manufacturing of Building Materials Business, primarily wood panels, posted substantial profit growth on steady production activity and the higher prices.

### *Housing and Housing-Related Businesses*

*Sales +3.5%, Operating Income +1.3%*

Net sales and contract revenues in the Housing and Housing-Related segment rose 3.5% year on year to ¥407.7 billion and operating income grew 1.3% year on year to ¥16.5 billion. Adjusted to reflect an actuarial difference from a revision to retirement benefit accounting methods, the growth in operating income was 9.3% year on year.

Promoting the innovative “passion for wood” concept together with design of the parent company’s high value added “MyForest” homes as marketing strategies in the Custom-Built Housing segment lead to total segment sales for completed construction of ¥285.2 billion, a 1.8% rise year on year, as rises in selling prices overcame a small drop in unit sales. In addition, our efforts in leading contracts into project starts and the marketing system centered on model showrooms designed meticulously to respond to the specific needs of each community contributed to an increase in orders of 5.5% year on year to 9,376 units. An increase in the percentage of orders for mid-level and higher priced homes raised the average order value per unit by 2.2% year on year to ¥31.6 million.

The Collective Housing Business introduced strategic products and stepped up marketing of wood apartment buildings, which generated 13.0% year on year growth in orders to 1,455 units and a 7.2% increase in order value to ¥14.7 billion. The Remodeling

Business posted a 2.4% year on year growth in orders to 8,670 units.

## RETURNS TO STOCKHOLDERS

### Dividend Raised ¥2 and

### Dividend Payout Ratio Elevated to 22%

Based on these performance results, we raised the annual dividend per share by ¥2 for fiscal 2006 to ¥15, representing a consolidated dividend payout ratio of 22.2%. We believe our foremost priorities at this point are to expand business through aggressive investment and create an operating structure that is flexible and resilient to changes in the business environment.

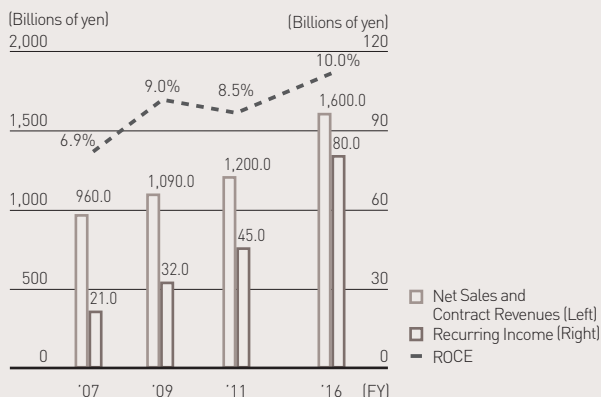
We regard providing our shareholders with stable and consistent dividends to be an important management responsibility and set dividends rate at a level that we believe represents a balanced consideration with our management base, financial standing, investment plans, and other factors. When profit levels for a fiscal year exceed our initial expectations, our policy is to review dividends and proactively raise them accordingly.

## OUTLOOK FOR FISCAL 2007

### An Expanding Housing Business and Higher Sales and Profits (excluding the effect of actuarial differences)

In fiscal year 2007, we anticipate nationwide owner-occupied housing starts reaching 360,000 units, representing 1.2% year on year growth, supported primarily by improving employment conditions. We also expect demand for timber and building materials to remain steady even as market conditions settle from the previous year’s activity. Based on these conditions, we forecast fiscal 2007 net sales and contract revenues rising 5.3% year on year to ¥960.0 billion, operating income declining 2.0% to ¥20.0 billion, recurring income declining 1.2% to ¥21.0 billion, and net income growing 0.4% to ¥12.0 billion. When factoring out the addition of ¥1.9 billion to fiscal 2006 profits attributable to the actuarial difference from the retirement benefit accounting, we anticipate operating income growth of ¥1.5 billion and recurring income growth of ¥1.6 billion.

### Targets for Net Sales and Contract Revenues, Recurring Income and ROCE



### Forecast by Segment

We aim to increase Timber and Building Materials Business sales 3.8% year on year to ¥540.0 billion and raise operating income 0.4% year on year to ¥8.0 billion in fiscal 2007. In the Distribution Business, profitability in the plywood business will fall, but we anticipate expanding sales of medium-density fiberboard (MDF) and other products along with growing profitability in overseas manufacturing operations to enable the expansion in operating income.

In the Housing and Housing-Related Businesses, while we anticipate rising materials prices to impact profits, the order backlog at the beginning of the year for custom-built detached houses was quantitatively higher than the previous year in terms of both value and the number of units. We forecast Housing and Housing-Related Businesses sales growing 7.9% year on year to ¥440.0 billion and operating income rising 2.5% to ¥17.0 billion.

## 10-YEAR LONG-TERM MANAGEMENT PLAN

“Project SPEED” (see the feature on page 18 for additional details)

### Changing Consciousness and Adopting an Aggressive Investment Stance to Achieve our 10-Year Vision

Looking back over the past decade, nationwide housing starts fell in a severe operating environment, but reform of the operating structure (fiscal 2002-2004) led to a recovery in profitability. Even though changes in the business environment such as diversifying lifestyles and the scarcity of timber resources will create new business opportunities going forward, with the population decline and our long term forecast for housing starts as assumptions we must revamp our business model.

With each employee playing a key role in actively and attentively advancing the development of the company, we have created a long-

term management plan with a clear roadmap to transform the Group over the next 10 years. We intend to immediately begin aggressive investment as called for under the plan to establish and develop new profit creating businesses. As a 10 year vision, maximizing our strength in providing housing related services both up and downstream we will advance global development related to “wood and housing”, and aim to be a business group with diverse revenue sources.

To undertake this business reform and bring about new growth, we will aggressively advance investment and introduce a new system to manage this investment. Specifically, we plan to implement a regimented capital allocation system utilizing return on capital employed (ROCE)\* as a measure of the profitability of the investment conducted in each business segment. We will set time-specific business targets as well as enforce strict criteria for withdrawal from unproductive businesses.

\* ROCE = business income / (interest-bearing debt + shareholder's equity);  
business income = (operating income + interest, dividends and other income) x (1 - effective tax rate)

### 10-Year Target: Sales of ¥1,600 Billion, Recurring Income of ¥80 Billion

Fiscal 2007 is the first year of the 10-year plan to reach targets in fiscal 2016 of sales of ¥1,600 Billion, recurring income of ¥80 Billion, and a 10% ROCE. The New Custom-Built Housing Business with its leading brand of new wood custom-built housing and the Distribution and Manufacturing of Timber and Building Materials Business with its market leasing share of the domestic market have been designated as the core businesses that will be essential to realizing the growth and profitability required to reach these targets. Also, with our technological capabilities in providing high quality wood products, gained over many years, and staff that conscientiously places top priority on the customer as key management resources, we will expand the business scope of the Overseas, Real Estate, and Remodeling Businesses.

## MEDIUM-TERM MANAGEMENT PLAN (FISCAL 2009 TARGETS)

### Recurring Income of ¥32.0 Billion on Aggressive Investment in the Real Estate and Overseas Operations

We have set three-year medium-term management targets as the first passage point for our long-term objective. For the three years to the end in fiscal 2009, our earning structure, which relies on the Housing Business for the majority of revenues, will not change significantly, but we will invest aggressively in key growth businesses to build a foundation to support future growth. Our targets for fiscal 2009 are sales of ¥1,090.0 billion, recurring income of ¥32.0 billion, and 9.0% ROCE.



## Income Plan by Business Segment

(Billions of yen)

		Net Sales and Contract Revenues				Recurring Income			
		FY2009 Plan	FY2006 Actual	Change	%	FY2009 Plan	FY2006 Actual	Change	%
Core Business	Distribution and Manufacturing of Timber and Building Materials Business	620.0	545.8	+74.2	+13.6%	6.8	6.5	+0.2	+3.4%
	New Custom-Built Housing Business	520.0	431.4	+88.6	+20.5%	24.2	16.7	+7.5	+45.3%
Priority Growth Business	Overseas Operations	49.0	32.9	+16.1	+48.8%	3.8	0.6	+3.2	+517.4%
	Real Estate Business	74.0	44.4	+29.6	+66.8%	2.2	0.8	+1.4	+178.6%
	Remodeling Business	33.0	25.8	+7.2	+27.7%	0.8	0.3	+0.5	+162.3%
	Elimination and/or Corporate	(206.0)	(168.7)	(37.3)	—	(5.8)	(3.7)	(2.1)	—
	Total	1,090.0	911.7	+178.3	+19.6%	32.0	21.3	+10.7	+50.5%

## Raise Core Business Recurring Income 33% to ¥31.0 Billion

We aim to raise recurring income in our core businesses by 33.6% from the fiscal 2006 level to ¥31.0 billion in fiscal 2009. In the Timber and Building Materials Business, while we anticipate temporary supply and demand imbalances to affect profit levels, we plan to strengthen our partnerships with leading distribution and construction companies to further substantiate our lead in the industry. This will expand our network and lead to more diverse revenue sources. Also, the new construction segment of the New Custom-Built Housing Business will focus on the mid and high-end housing markets in metropolitan areas and major regional cities. In fiscal 2009, the segment is aiming to attain growth in housing orders, including those for two-by-four constructed housing, of 14.9% over the fiscal 2006 level to 11,200 units and annual construction completions up 13.7% to 10,900 units. The segment is also implementing strategies to improve operating effectiveness and minimize costs, such as by leveling off the seasonal fluctuations in the numbers of construction starts and completions, to enhance its business competitiveness.

## Raise Recurring Income in the Priority Growth Businesses 400% to ¥6.8 Billion

The medium-term management plan sets a target of expanding recurring income in the priority growth business by 400% over fiscal 2006 to ¥6.8 billion. In our Overseas Operations, we aim to leverage our information network for market analysis and experience in each country to rapidly develop promising projects for commercialization. The Real Estate Business will focus on acquiring real estate and developing a wide array of solutions to create new value and meet the emerging

needs of Japan's changing society, including the aging population. The Remodeling Business will expand its scope beyond home maintenance and concentrate its wooden housing technology and experience on products designed to raise the asset value of homes.

## IN CLOSING

The foundation for our long-term management plan is the clear management philosophy of the Sumitomo Forestry Group: using the reusable resource wood we will provide all services related to housing lifestyles and be a truly useful company to society. Through these efforts we will draw out our strengths and offer high value products and services for our customers. In addition, going forward we will build sustainable relationships with our stakeholders. We aim to be a Group that provides “quality of our company” on par with leading companies in the world, raising not only economic value but also societal and environmental value.

As we set out on this path, I ask for your continued support and counsel.

August 2007

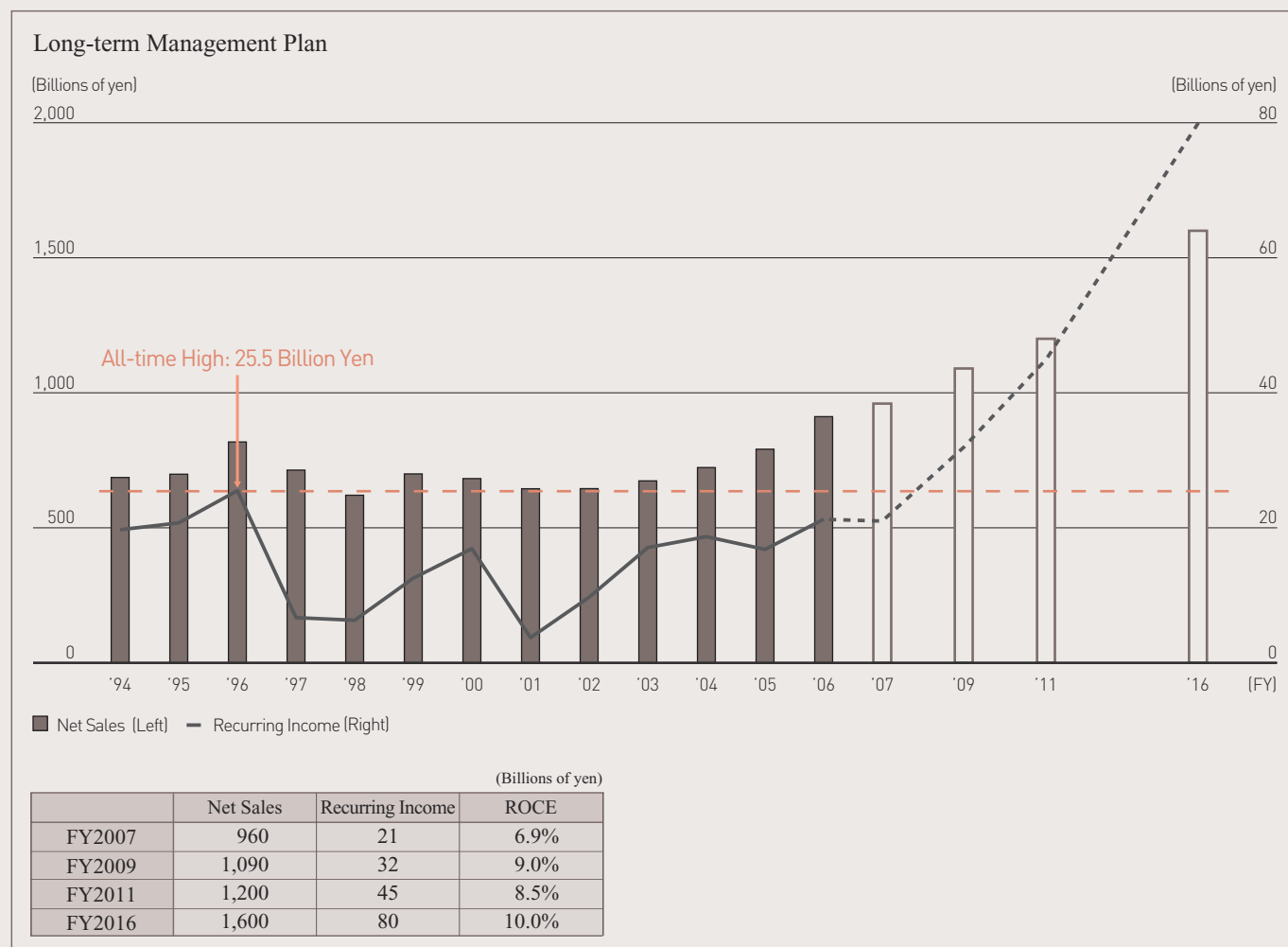
Ryu Yano

President / Director



## FEATURE: LONG-TERM MANAGEMENT PLAN

In fiscal 2007, the Sumitomo Forestry Group launched the long-term management plan “Project SPEED”<sup>\*</sup> with detailed guidelines for a strategy to attain specific performance targets in fiscal 2016. We are currently aiming to achieve the targets for the first three-year period to fiscal 2009.



### \*The Meaning of “Project SPEED”

**SPEED** denotes the swiftness with which we expect the plan to be implemented and produce results.

It serves as an acronym for:

“Strong Passion Enables us to become an Excellent company by implementing Detailed strategy.”



### PERSPECTIVE ON THE FUTURE BUSINESS ENVIRONMENT

- In the domestic housing market, which has the greatest influence on our Group results, the core owner-occupied housing market segment is expected to shrink gradually as the country undergoes a trend of decline in population and the number of households.
- The remodeling market is likely to expand as the stock of housing grows and housing structure durability improves. Business opportunities are also likely to increase in the real estate industry as new methods of offering value-added services and products emerge.
- We believe the global economy will remain healthy as the BRICs economies continue to rapidly expand and those of the United States and the European Union remain strong. We expect environmental issues to heighten demand for environmentally sound raw resources leading to growing global demand and increasingly diverse use for timber and construction materials.

## BACKGROUND OF THE LONG-TERM MANAGEMENT PLAN

### Creating a Business Structure with Diverse Income Sources

The Sumitomo Forestry Group's operations began with the forestry and timber business and have expanded outward to encompass a diverse range of business related to wood and housing. As we stand now, our income sources are strongly focused in our custom-built detached wooden housing and our distribution and manufacturing of timber and building materials businesses. Expanding the Group's income will require that we develop synergy effects among our current businesses and diversify income sources to create a business structure capable of producing and sustaining increased income flow.

After full consideration of the current and future conditions in our operating environment (the perspective described above), in fiscal 2007 we created our long-term management plan Project SPEED. This plan sets out a detailed guideline for the ongoing strengthening of our current core income businesses — the New Custom-Built Housing Business and the Distribution and Manufacturing of Timber and Building Materials Business — and allocating the income they produce as well as human resources and other management resources to concentrated investment in our priority growth businesses — the Overseas operations, Real Estate, and Remodeling businesses — to promptly create the new profit-earning operations that will become the future pillars of the Sumitomo Forestry Group.

## INCOME PLAN

### ROCE to Monitor Profitability Progress Toward ¥80 Billion in Recurring Income

In expanding our business scale and raising profitability by making aggressive investment, it is essential that we have a reliable management indicator capable of regularly monitoring our status

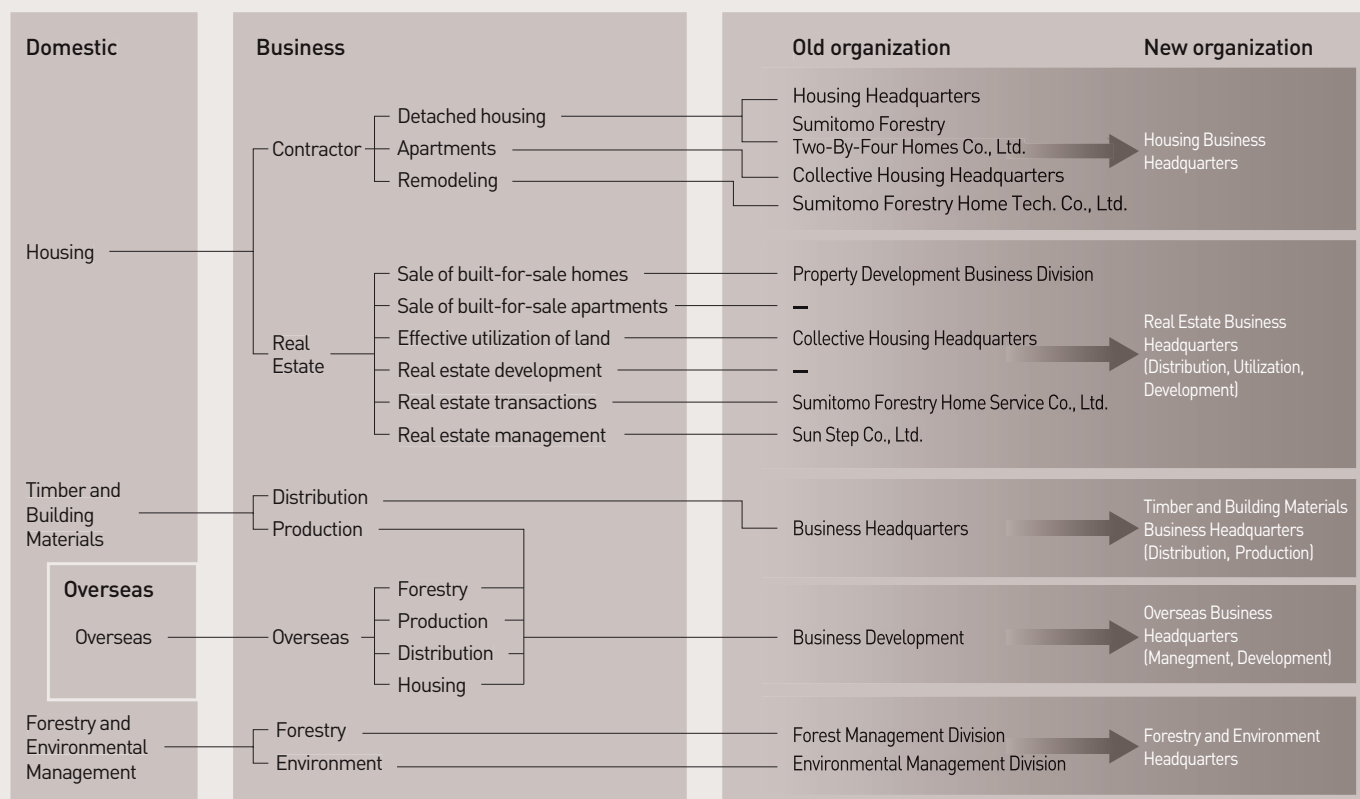
and progress. Therefore, return on capital employed (ROCE), an in-house developed management indicator, has been recently adopted and operating, administrative and executive departments are working together to monitor the effectiveness and profit-producing performance of our investments.

We have set three sets of net sales and recurring income targets to benchmark our progress to our 10-year objectives for fiscal 2016. In fiscal 2009, the end of the first three-year period, we are aiming for net sales of ¥1,090 billion and recurring income of ¥32 billion. After five years, fiscal 2011, we are targeting net sales of ¥1,200 billion and recurring income of ¥45 billion. Finally, in fiscal 2016 at the end of the 10-year plan, we intend to achieve net sales of ¥1,600 billion and recurring income of ¥80 billion. As we expand our business, we will also work to raise ROCE from the 7.4% in fiscal 2006 by establishing an operating structure capable of sustaining ROCE of 10% or higher.

For our strategic investment plan, to bring out new revenue sources, based on the assumption that we will continue to maintain a healthy financial standing and using free cash flow as our resource we will focus investment on the Timber and Building Materials Business, Overseas Operations, and Real Estate Business. In the Timber and Building Materials Business we will strengthen investment in and alliances with building materials and manufacturing companies as well as distribution companies. In Overseas Operations we will build a new factory, purchase forest land, and expand the housing business. In the Real Estate Business we will purchase real estate and invest in developers, real estate management firms, brokers, and service providers targeting the elderly. With these investments we are aiming for active strategic growth.

ROCE:  $\text{business income}^* / (\text{interest-bearing debt} + \text{shareholders' equity})$   
 $^* \text{business income: } (\text{operating income} + \text{interest, dividends and other income}) \times (1 - \text{the effective tax rate})$

## Reorganization



## STRATEGIES AND TARGETS FOR EACH BUSINESS DIVISION

### Core Businesses

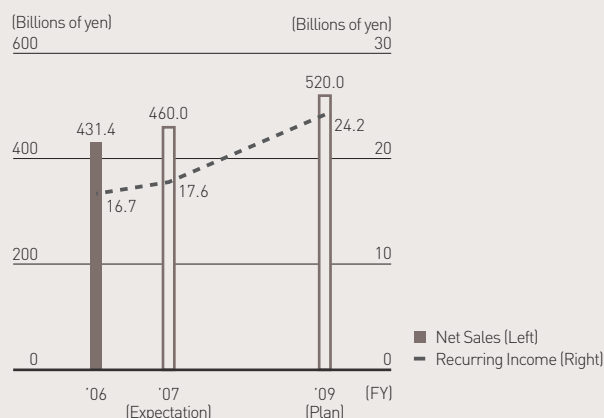
#### 1) New Custom-Built Housing Business

The core strategy of the Housing Business is to create a business structure for higher profits. The strategy goes beyond increasing orders by expanding the business scope and enhancing our staff, it calls for raising the overall operating efficiency of the organization as a whole. Specifically we aim to differentiate the distinct features of our products by emphasizing our strength in home design and the appeal of wood materials to a focused customer target in the mid and high-end housing markets in urban areas. Measures will include further raising product quality and integrating marketing and design operations to enhance the competitiveness of the sales division. We will also continue developing our regional operations to establish deeper ties to local areas focusing on model home exhibits that closely reflect specific local features.

In addition, in fiscal 2007 we radically modified the organizational structure enabling the division to become a total housing operation for custom-built detached housing, wooden apartment buildings,

remodeling, and all housing-related contract construction businesses. One key change is the establishment of wooden apartment sales centers within detached housing sales offices, which is greatly expanding our customer information gathering capabilities. Without increasing staff numbers more than necessary, the setup allows for faster response to customer inquiries concerning whether to rebuild or remodel and provides a palette of apartments and other housing outside of detached housing for sales staff to show. We aim to leverage this organizational structure change to expand the overall earnings of the Housing Business.

#### New Custom-Built Housing Business



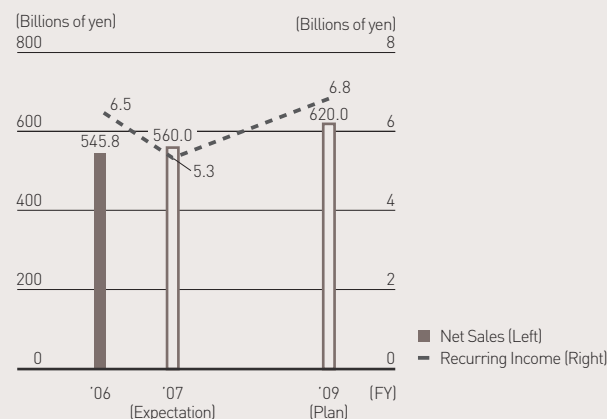
## 2) Distribution and Manufacturing of Timber and Building Materials Business

The Distribution of Timber and Building Materials Business has become the top timber and building materials operation in Japan in terms of timber transaction volume after Ataka Kenzai joined the Sumitomo Forestry Group in 2005. However, while we intend to maintain our leading position in the segment, we anticipate increasing industry restructuring activity as the domestic timber materials market shrinks in tandem with the housing market. To prepare for these changes in the business environment, we are advancing two main strategies.

The first strategy is to strengthen our business through alliances with other companies. Using these alliances we are further establishing and strengthening a housing business value chain encompassing all upstream and downstream processes and operations by leveraging our unparalleled strength in overseas procurement, information gathering via our business scale, wood materials technology, and our ability to offer solutions products in addition to sales of “goods”. The goal is to become a one-stop supplier, including via alliances with outside parties, of housing materials from raw materials to final products. The

integration of Ataka Kenzai vastly widened our business capabilities in the midstream area, and we aim to focus on strengthening and expanding the vertical aspects of our business structure. The second strategy is to revise and enhance our trading company capabilities. We plan to expand our management scope beyond strictly the commission-based business and into the investment field as we aim to establish a diverse income structure from both investment and commission operations.

### Distribution and Manufacturing of Timber and Building Materials Business



## Priority Growth Businesses

### 3) Remodeling Business

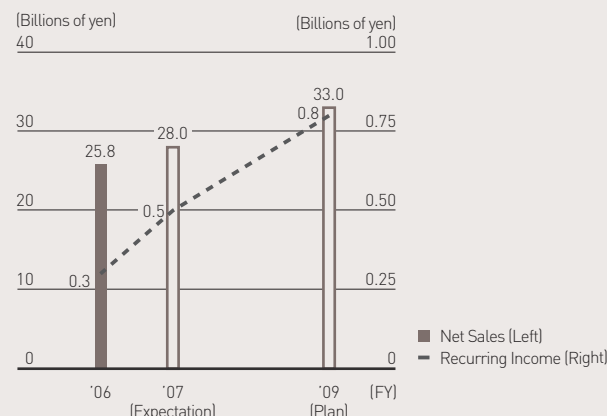
The long-term management plan designates the remodeling business as a priority growth business and places it under the aegis of the Housing Business to formulate an unhindered complementary relationship with the custom-built detached housing business. We are implementing two key strategies to advance this business.

The first strategy is to approach past housing clients. Our client base has reached roughly 200,000, and changing lifestyles and diversifying needs are core drivers of remodeling demand. We consider our satisfied clients to be a prime source of demand for a variety of services ranging from remodeling to selling existing homes and providing new homes. We will strengthen our strategy of offerings to maintain and enhance the asset value of homes, centering on the remodeling business. Specifically, we will increase the number of opportunities for contact with our customers through our program of scheduled inspections 10 years after construction, along with other activities. In addition to the increased order volume in the remodeling business, this will enhance our ability to improve customer satisfaction and enable us to meet all housing-related needs via Groupwide efforts. Through this we will develop new businesses and to be introduced to new customers.

The second key strategy is to attract general customers from outside our customer base. As Japan's leading custom-built detached wooden house builder in the remodeling segment, we have also made a strong showing in developing and marketing our leading capabilities in projects that require high technical expertise such as

reforming older private homes and buildings on small lots, as well as remodeling larger structures. Ministry of Internal Affairs and Communications data shows that of the 26 million existing detached houses in Japan, over 90% were built using wood, the conventional construction method. Some 11.5 million of these were built before the adoption of the Earthquake Resistance Building Standards of 1981 and are considered potentially unsafe in the case of an earthquake. We are leveraging the many connection points with our customers by using our infrastructure in the new custom-built detached housing market to aggressively promote our brand competitiveness, leading design capabilities, and cutting-edge earthquake reinforcement construction technology to be at the forefront of the market as the need to rebuild or remodel these homes grows each year.

### Remodeling Business





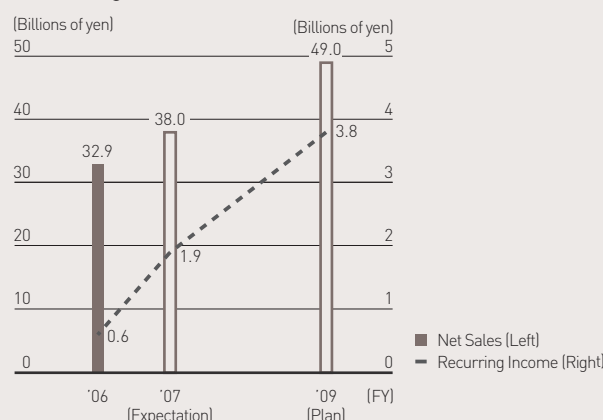
#### 4) Overseas Operations

We continue to improve the profit performance of our overseas operations while aggressively investing in four new business areas to optimize our capabilities in the current business environment.

First, in the overseas forestry business, we will establish a secure source of raw materials and invest in commercial forestry development to increase our presence in tree-based materials industries, which are expected to grow. Second, in the overseas manufacturing business, we plan to increase our overall production capacity by expanding our existing factories for medium-density fiberboard (MDF), particle board, and other wood-based products while also constructing new plants to maximize utilization of raw wood materials from timber plantations. The factory expansion and construction is planned to take place in Oceania and Indonesia as well as other strategic regions offering timber resources. Third, we plan to strengthen our overseas distribution operations by expanding our overseas sales networks, focusing on Singapore, Dalian (China) and other parts of Asian regions undergoing rapid economic growth, as well as expanding our distribution network in the United States and

Oceania. Forth, in the Housing Business, we plan to continue expanding the US business, whose business foundation is being strengthened and has posted home sales of 100 units annually after its first five years of operation in the mid to high-end housing range. We are also looking into starting operations in Korea and China, where living environment needs are increasing, as well as in other countries.

#### Overseas Operations



#### 5) Real Estate Business

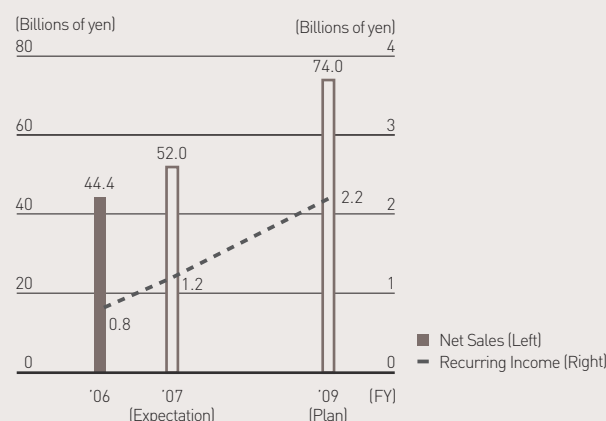
We will advance an aggressive plan to extend our real estate business operation beyond our current operations as a landholding asset manager to include the real estate development business encompassing land acquisition for the construction and sale of rental units, condominiums, nursing homes, and other structures. Taking a different approach than in the past, we have gathered all of our real estate functions into a dedicated real estate division.

The first step in this process will be to expand and diversify the scope of our real estate business activities and offer clients an expanded palette of value-added products for residential and urban communities, including built-for-sale housing, rental apartments, condominiums, and nursing homes. As part of this, in our non-wood structures, such as rental condominiums, while improving the profitability of these operations by introducing technological upgrades to reduce production costs, we plan to shift the real estate development activities to business areas that can provide more substantial and stable revenue sources. Sumitomo Forestry Home Service Co., Ltd., which carries out real estate sales, will play a major role in our development plans for the real estate business. Through strengthening sales agency functions and widening its office network outward from its core in the Tokyo, Osaka and Nagoya metropolitan areas, the business will increase its area specific property data collection ability and work closely with other

internal divisions to bring out synergies. The property development business, which was launched last fiscal year and constructs built-for-sale detached houses, has been steadily expanding its land acquisition activities over the last year. To quicken the development of this business, we are focusing efforts including actively incorporating outside expertise.

The real estate we purchase will bring a certain amount of risk and financial burden. Mindful of the axiom of “no risk, no reward”, we plan aggressive investment linked with the utilization of brokerage and real estate management functions within the Group, and linked with clear exit strategies.

#### Real Estate Business





## REVIEW OF OPERATIONS

### CONTENTS

- 24. Timber and Building Materials Business
- 28. Housing and Housing-Related Businesses
- 32. Other Businesses



# TIMBER AND BUILDING MATERIALS BUSINESS

## Segment Performance Highlights

	FY2004	FY2005	FY2006	FY2007 Plan
Sales	320,255	412,182	520,103	540,000
Operating income	4,615	2,806	7,967	8,000
Assets	157,840	237,265	269,610	—
Capital expenditures	2,949	5,701	5,281	—

Note: The sales figures given include intersegment transactions. Operating income figures include internal profit prior to the deduction of amounts such as intersegment transactions and headquarters expenses that are not apportionable.

## Operating Income of Main Subsidiaries

	FY2005	FY2006	FY2007 Expectation
Sumitomo Forestry Crest Co., Ltd.	251	943	980
Overseas Subsidiaries	FY2005	FY2006	FY2007 Expectation
PT. Kutai Timber Indonesia (Indonesia)*	(56)	256	400
Alpine MDF Industries Pty Ltd. (Australia)*	84	113	330
Nelson Pine Industries Ltd. (New Zealand)*	231	1,427	1,970

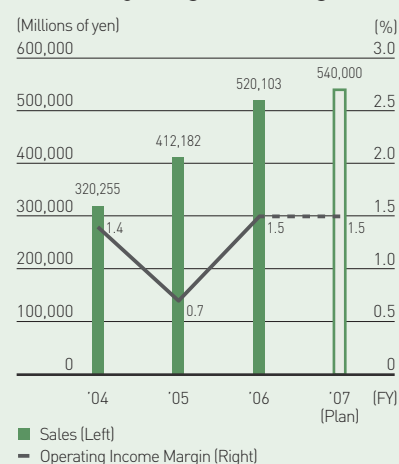
\* Calculations for overseas affiliated companies have been translated into Japanese yen at the following rates.

FY2005 US\$ = 110.17 / AU\$=83.91 / NZ\$=77.56

FY2006 US\$ = 116.31 / AU\$=87.62 / NZ\$=75.55

FY2007 (Expectation) US\$ = 118.00 / AU\$=88.00 / NZ\$=77.00

## Sales and Operating Income Margin



The Timber and Building Materials Business has securely established itself as the leading timber and building materials trading company in Japan through its wide ranging product lineup and global procurement capabilities. The business will advance a strategy of astute and aggressive investment in Japan and overseas to expand and diversify its profit base.

## BASIC STRATEGIES

### Distribution of Timber and Building Materials Business

- In Japan, expand market share by building a framework to become a one-stop comprehensive supplier of housing materials from raw materials to finished products.
- Overseas, expand sales in developing countries where demand for construction materials is growing and gather information to be used to develop new business opportunities.

### Manufacturing of Building Materials Business

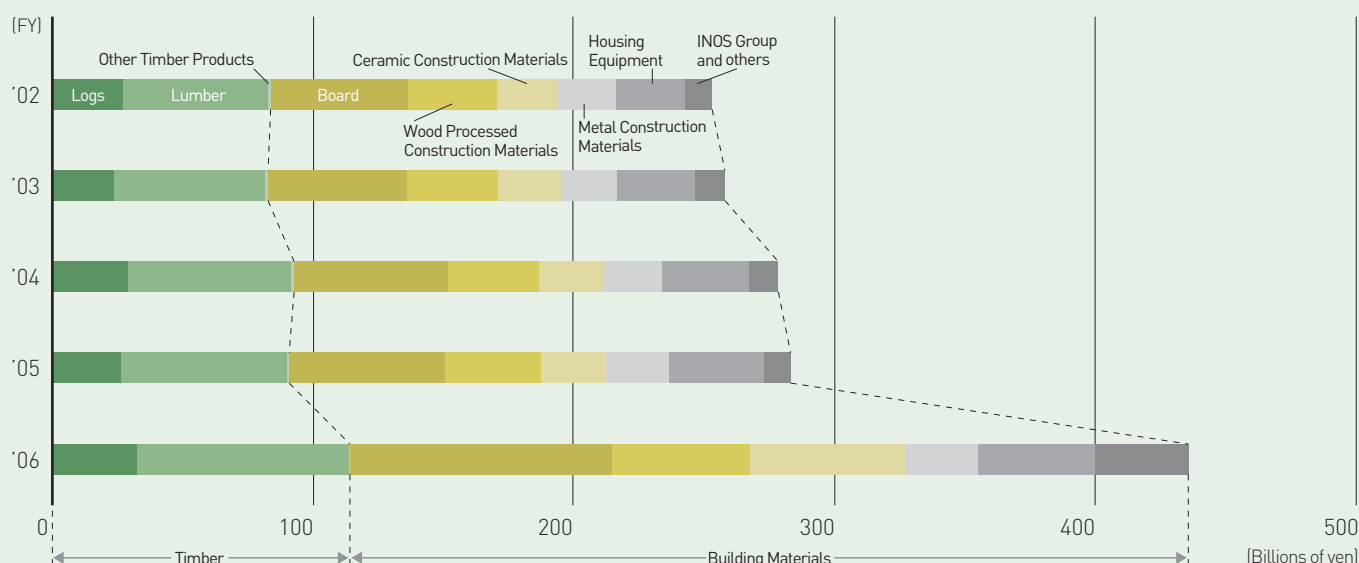
- Increase manufacture of products that make efficient use of timber resources.

### Forestry Business

- Expand land area in Japan and overseas covered by our forestry management business starting with forests supplying raw materials to the manufacturing business.



Sales by Product Category for the Distribution of Timber and Building Materials Business (non-consolidated)



## FISCAL 2006 PERFORMANCE REVIEW

### Business Environment and Results:

Sales +26.2%, Operating income +183.9%

The business environment for the Timber and Building Materials Business in fiscal 2006 included steeply rising prices for timber and wood materials in Japan and around the world as demand grew from the rapidly expanding economies of China and other emerging nations. In addition, increased sales from the larger customer base brought about by acquisitions resulted in Timber and Building Materials Business sales growing 26.2% year on year to ¥520.1 billion and operating income rising 183.9% to ¥7.9 billion in fiscal 2006.

### Review of Segment Results

#### *Distribution of Timber and Building Materials Business*

To fortify our leading position in the timber and building materials market, we merged with Ataka Kenzai Co., Ltd. (fiscal 2005 net sales ¥123.3 billion, operating income ¥600 million) on April 1, 2006. This merger has enabled us to strengthen relationships through the sharing of customer networks and expand our profit base.

Rising prices for timber and wooden board such as glue-laminated timber produced in Europe and plywood produced in Southeast Asia supported 25.7% year on year growth in timber sales to ¥114.1 billion and a 67.1% increase in building materials sales to ¥321.7 billion. Also, in anticipation of rapid growth in demand for timber and

building materials in China, we established a subsidiary in Dalian, China, to expand our local trading volume and increase revenue. The subsidiary will also to be a base for future new business expansion in forest management, manufacturing, and other areas.

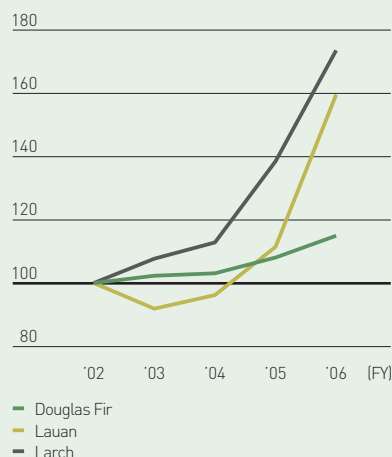
#### *Manufacturing of Building Materials Business*

Our ongoing efforts to develop the Manufacturing of Building Materials Business in Japan and overseas included implementing measures to improve productivity and lower costs to offset the growing manufacturing costs accompanying the steep rises in raw materials prices as well as passing the higher costs on to our product prices. Our overall volume of sales increased during the year on strong demand for plywood, particleboard, medium density fiberboard (MDF) and other wooden board products.

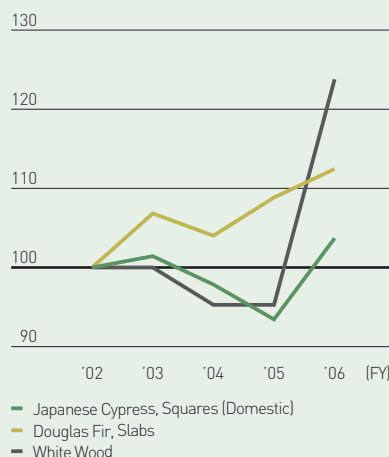
In our overseas operations, we responded to the growing concern about environmental issues around the world by expanding the use of raw materials drawn from plantation forests in our manufactured products. We invested aggressively during the year in anticipation of growing demand for wood board materials from the rapidly growing economies in the Asia region. Specifically, at subsidiary PT. Kutai Timber Indonesia we expanded our specialized rotary lathe facilities to increase our plywood production capacity using raw materials from plantation forests. In addition, we are also constructing a new particleboard manufacturing plant, which is scheduled to commence operation during fiscal 2007.

# Market Conditions for Timber and Building Materials (using FY2002 as the base year)

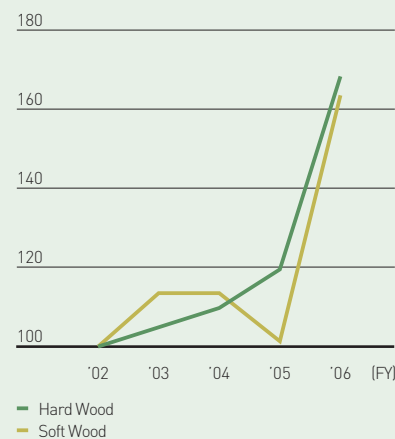
Log Price Indices



Lumber Price Indices



Board Price Indices



## Forestry Business

Management of the Forestry Business is conducted from a long-term perspective based on sustainable forest management activities and with full consideration of environmental issues. We are seeking to further increase our use of domestic timber to reflect the recovering self-sufficiency ratio of the domestic timber market amid the changing worldwide supply and demand balance.

In select areas of our company-owned forests, the company plans to initiate small area clearcutting techniques to reduce logging costs, and we also plan to increase the usage efficiency of logged timber. In addition, Sumitomo Forestry Timberland Management Co., Ltd. expanded its transaction volume of domestic cedar logs used for plywood by increasing its participation in the National Forest Timber Supply and Sales System to acquire timber from national forest thinning operations, which is then used to produce Japanese cedar plywood and other products.

## OUTLOOK AND STRATEGIES FOR FISCAL 2007

Sales +3.8%, Operating Income +0.4%

Continuing strong global demand for wood materials is expected to hold timber prices at high levels in fiscal 2007. We expect a drop in plywood sales prices, but strong sales of MDF and other manufacturing materials will somewhat offset this drop. We also plan to increase timber transaction volume by providing new products that meet the emerging needs of our expanding client base. In this environment we forecast Timber and Building Materials Business sales growing 3.8% year on year to ¥540.0 billion and operating income rising 0.4% to ¥8.0 billion.

## SUPERIORITY OF THE TIMBER AND BUILDING MATERIALS BUSINESS



Merger Ceremony for Sumitomo Forestry and Ataka Kenzai



Cedar Plywood



Processed MDF

**Synergies with Ataka Kenzai's Development Promotion Division**

As part of the April 2006 merger with Ataka Kenzai Co., Ltd., customer base and staff of that company's Development Promotion Division were transferred to Sumitomo Forestry. This meant that a new customer network of housing construction companies was gained for sales of building frames, concrete and other building materials. A strength of the Development Promotion Division is its abilities in aiding architectural design for houses that raises functionality of housing such as earthquake resistance capabilities, based on the know-how of its connections.

Through the synergies gained via the merger, sales and product development abilities of this group will be strengthened. Specifically, products to meet customer needs that the Department was not able to offer before will now be made available, and for Sumitomo Forestry our abilities in offering solutions to customers downstream is being strengthened. We are putting in place the ability for the Development Promotion Division to be a one-stop solutions provider for a wide range of customers.

**Domestic Cedar Plywood Contributing to Higher Efficiency**

Our cedar plywood is produced at the Komatsushima branch of Sumitomo Forestry Crest Co., Ltd. using 100% domestic-grown Japanese cedar, which are notoriously difficult to process. Demand for cedar and structural plywood for use in housing frame materials has been growing as it is used as a primary element to increase structural durability to enhance the earthquake resistance capabilities of wooden housing. The Japanese government is promoting the use of cedar as a means of advancing the forestry industry and the use of forests. Cedar plywood is 35% lighter than the softwood generally used in construction-use plywood, making it advantageous for both transport and at the time of construction. In addition, the Komatsushima branch sources almost all of its Japanese cedar from the area within 100km of its location, shortening transport distance and thus lower CO<sub>2</sub> emissions. In this way the branch is contributing to the prevention of global warming.

**Global Sales of Medium Density Fiberboard (MDF\*)**

Our expansion into global markets for the manufacture and sales of medium density fiberboard is a key strength of the Sumitomo Forestry Group. Subsidiaries Nelson Pine Industries Ltd. in New Zealand and Alpine MDF Industries Ltd. in Australia use fast-growing Radiata pine, which reaches maturity in about 30 years, in the MDF they manufacture. Using their superior technology, these companies produce high quality MDF with smooth and easy-to-process-with surfaces for furniture and home interior applications. Receiving praise from users, the products are sold in Japan, China, and other Asia Pacific region markets.

\* MDF: A wood particle material formed by fibrillating wood into fine wood fibers, similar to cotton, adding an adhesive agent and applying high temperature and pressure.

## INTERVIEW



Sumitomo Forestry  
Timberland Management Co., Ltd.  
Director Forestry Division General Manager  
**Kaori Hasegawa**

The current business environment is providing a supportive backdrop for our efforts to expand the operations of the forestry and forestry related business. The sharp rise in timber prices worldwide in particular has made domestic timber prices more competitive. In these favorable conditions, we are developing operations in a wide range of fields, from forest management to domestic timber sales. Our strength is rooted in our experience and business network. Our know-how is cultivated from over 300 years of forest management. Our network of forestry operations enables us to maintain active cooperative relations with entities related to forestry operations, giving us a clear understanding of the evolving needs and demands of our customers and enabling us to stably supply domestic timber and implement an effective reforestation system. The integrity of our supply chain, which is directly connected with our timber resources, supports the overall revenue growth of the Sumitomo Forestry Group on several levels, such as raising the competitiveness of the Timber and Building Materials Business by supporting new product development and strengthening our brand in the housing industry through the provision of high-quality materials. In the future, we plan to introduce a new timber distribution system and expand our non-timber distribution business to create a new operating structure and ensure stable revenue inflow. We also plan to develop our unique capabilities through an expanded use of domestic timber as we continue to extend our sustainable forestry management activities.



# HOUSING AND HOUSING-RELATED BUSINESSES

## Segment Performance Highlights

	(Millions of yen)			
	FY2004	FY2005	FY2006	FY2007 Plan
Sales	418,313	393,868	407,780	440,000
Operating income	17,530	16,370	16,586	17,000
Assets	108,705	105,579	113,276	—
Capital expenditures	4,403	3,737	3,481	—

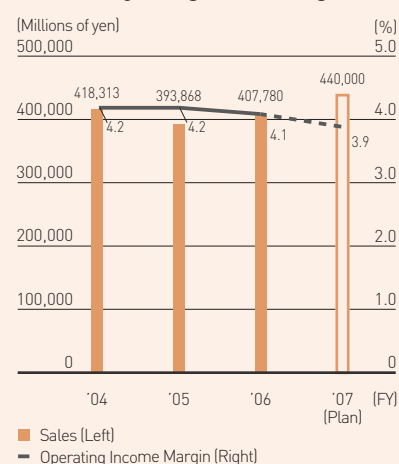
Note: The sales figures given include intersegment transactions. Operating income figures include internal profit prior to the deduction of amounts such as intersegment transactions and headquarters expenses that are not apportionable.

## Operating Income of Main Subsidiaries

	(Millions of yen)		
	FY2005	FY2006	FY2007 Expectation
Sumitomo Forestry Two-By-Four Homes Co., Ltd.	(487)	46	40
Sumitomo Forestry Home Service Co., Ltd.	423	241	550
Sumitomo Forestry Home Tech Co., Ltd.	195	264	450
Sumitomo Forestry Home Engineering Co., Ltd.*	515	647	680
Sun Step Co., Ltd.	281	415	470

\* On October 1, 2006, Sumirin Construction Co., Ltd. changed its name to Sumitomo Forestry Home Engineering Co., Ltd.

## Sales and Operating Income Margin



The Housing and Housing-Related Businesses aim to market distinct products emphasizing our strengths in product design and featuring the appeal of wood materials, concentrating on a consumer base of mid to high-end customers in urban areas. To further raise operating efficiency and customer satisfaction, we have reorganized the segment into the contract construction business, including custom-built detached houses, and the real estate business, focusing on a close-knit network, comprising the development and offering of products with multilayered value-added features.

## BASIC STRATEGIES

### New Custom-Built Housing Business

- Emphasize strengths in product design and wood products concentrating on a consumer base of mid to high-end customers in urban areas
- Improve business efficiency by utilizing the detached home model home exhibit sites as integrated contact points between the company and consumers for apartment and remodeling operations as well.

### Remodeling Business

- Offer comprehensive products and services to stimulate demand from current Sumitomo Forestry homeowners and highlight our accumulated technical skills in the new housing business to stimulate demand from new customers.

### Overseas Housing Business

- Expand our overseas business from the current base in Seattle, United States, by rapidly developing operations in Korea and China followed by other regions and supplying quality housing products matched to local market needs.

### Real Estate Business

- In addition to continuing our traditional effective land use business of building revenue generating structures for land owners, develop and offer rental housing, built-for-sale homes, residential care facilities, and other structures on company-bought land and offer a wide range of value-added products and services.
- In the built-for-sale detached housing business, offer living environments featuring attractive outdoor layouts, security systems, and designs matched to the appearance and character of the local community.

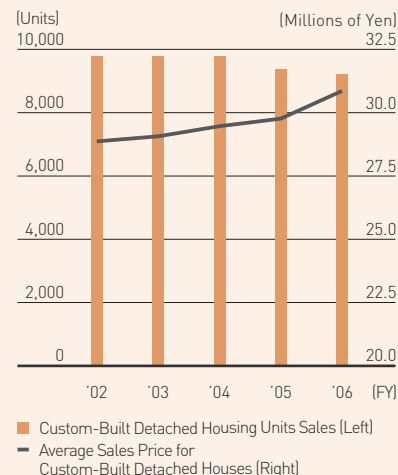


MyForest-WARAKU



MyForest-GRAND LIFE

Unit Sales and Average Sales Price  
in the Custom-Built Detached Housing  
(wooden post-and-beam construction method houses only)



## FISCAL 2006 PERFORMANCE REVIEW

### Business Environment and Results:

Sales +3.5%, Operating income +1.3%

New housing starts grew 2.9% year on year to 1.28 million units in fiscal 2006 on brisk first time buyer demand in anticipation of higher housing loan interest rates and rising land prices in major metropolises. The number of owner-occupied housing starts, which is a key factor supporting performance in our housing business, rose 0.9% year on year to 0.35 million units, marking the first growth in three years.

The Housing Business responded to this business environment by strengthening its organization to facilitate business activities fine-tuned to the market and by fortifying its product lineup to meet emerging consumer needs. These efforts resulted in sales growth of 3.5% year on year to ¥407.7 billion and operating income up 1.3% to ¥16.5 billion.

### Review of Segment Results

#### New Custom-Built Housing Business

##### • Detached-Housing

As our key product in the segment, the wooden post-and-beam construction method detached-housing business promoted the unique features of our MyForest series, which actively utilizes domestic timber and provides a lifestyle of natural breezes and lighting reminiscent of Japan's traditional wooden houses. The MyForest line offers a diverse palette of designs, such as the MyForest-Super Natural Walnut featuring the rich environment provided by black walnut imported from

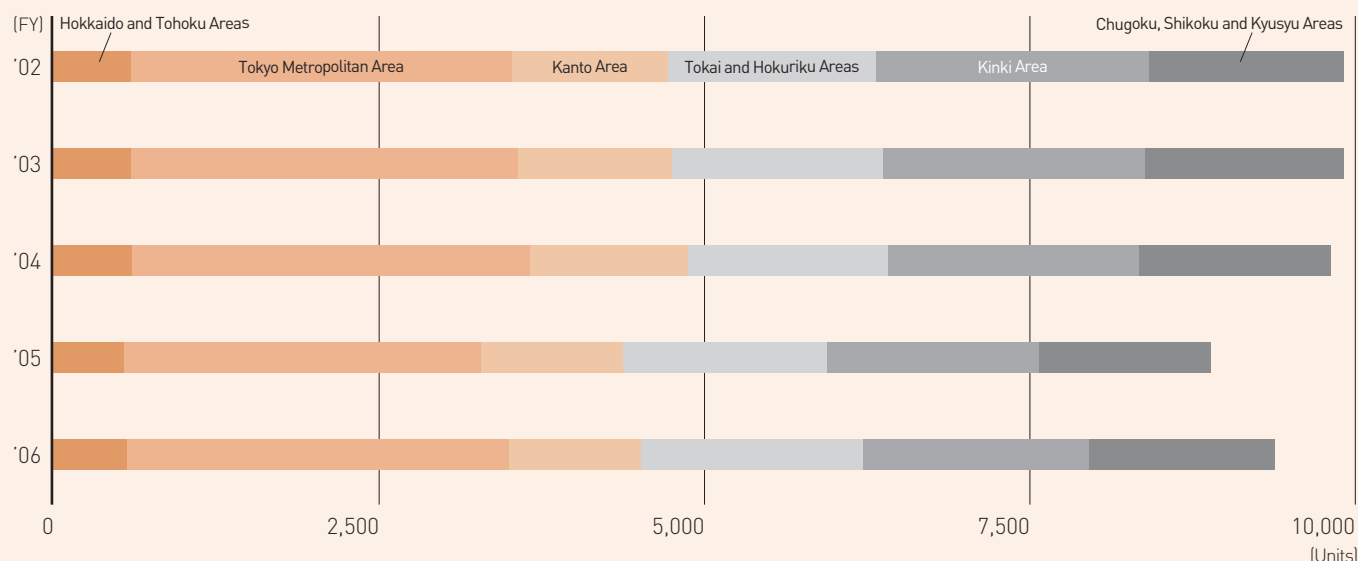
North America, MyForest-Waraku providing a blend of Japanese style elements and functionality, and MyForest-GRAND LIFE single-story homes designed to complement the simple lifestyles preferred by the baby-boomer generation. The segment also introduced housing features focused on specific consumer needs, such as a fire-resistant construction method that allows urban homeowners to maximize the use of limited land space. The business also revised its organizational framework to facilitate management that is more capable of responding to the specific needs of local environments. Sales promotion activities were augmented with Housing Specialist events focusing on the three major metropolitan areas of Tokyo, Osaka and Nagoya, providing consumers with opportunities to deepen their understanding of building construction layouts and interior and exterior materials, which are hard to picture at model home exhibits. These efforts led to an increase in construction orders of 5.5% year on year to 9,376 units. Promotion of our high value-added housing products integrating our design capabilities contributed to growth in unit order value of 2.2% to ¥31.6 million while the value of completed units utilizing our wooden post-and-beam construction method increased 1.8% to ¥285.2 billion.

The value of completed units of two-by-four construction method homes constructed by Sumitomo Forestry Two-By-Four Homes Co., Ltd. rose 8.5% to ¥11.0 billion as the strategy centering on a marketing shift toward mid and high-end products progressed favorably.

##### • Collective Housing

The collective housing business expanded its product lineup with the Succeed M-trust Inno wooden apartment building series and continued

### Orders by Region for Custom-Built Detached Houses (wooden post-and-beam construction method houses only)



to reinforce its staff. These efforts produced solid results with order value rising 7.2% year on year to ¥14.7 billion and the value of completed housing surging 21.1% to ¥13.9 billion in fiscal 2006.

#### • Overseas Housing Business

In operations overseas, property acquisitions in the greater Seattle area based on meticulous market analysis led to an increase of 43 units in sales year on year to 99 units in fiscal 2006. The detached housing market in Korea is believed to be on the threshold of significant growth, and we are actively positioning the segment to provide high-quality products in the region by creating alliances with local companies and opening model home exhibits.

#### Remodeling Business

The Remodeling Business implemented a strategy to stimulate remodeling demand from homeowners outside of our existing customer base, including expanding marketing of the Sumirin REP method quake-resistant remodeling technology jointly developed with Sumitomo Forestry Home Tech Co., Ltd. The strategy successfully raised the number of remodeling orders by 2.4% year on year to 8,670 units and raised sales 9.0% to ¥25.8 billion.

#### Real Estate Business

Sumitomo Forestry Home Service Co., Ltd. continued to roll out the infrastructure for its real estate brokerage business during the year by expanding its office network, particularly focusing on the Tokyo metropolitan area, and expanding the functions available on its website. These

efforts helped boost sales 5.0% year on year to ¥7.2 billion in fiscal 2006.

The built-for-sale detached housing business launched the new Forest Garden Kamishidami (with 10 units available initially) in Nagoya, designed for families comprised of parents in their thirties and based on a concept of creating a community with high asset value that will be lived in for a long time.

### OUTLOOK AND STRATEGIES FOR FISCAL 2007

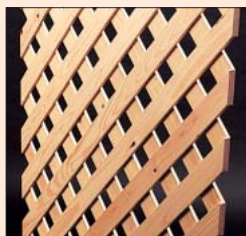
Sales +7.9%, Operating Income +2.5%

We anticipate new housing construction starts to maintain their underlying strength in fiscal 2007 supported by improving employment levels and other factors. The new housing construction business plans to introduce new products reflecting emerging consumer needs, which will lead to improving customer satisfaction. The Real Estate Business will advance its land acquisition activities while maintaining an appropriate risk balance. We will continue to construct nursing home facilities through subsidiaries set up in 2006 amid the accelerating trend in Japan of a declining birthrate and growing population of the elderly. We will focus on developing a business model capable of gaining solid profitability through the rents collected from these facilities.

Based on the above measures, we aim to achieve Housing and Housing-Related Businesses sales growth of 7.9% year on year to ¥440.0 billion and an operating income increase of 2.5% to ¥17.0 billion in fiscal 2007. We expect custom-built detached housing orders to grow 6.1% year on year to 10,350 units.



## SUPERIORITY OF THE HOUSING AND HOUSING-RELATED BUSINESSES



Cross Panel

### Outstanding Earthquake Resistance Cross Panel Technology

Our cross panels are an original earthquake resistant material made using domestically grown Japanese cypress. Compared with other plywood building materials of the same size, our cross panels are 1.3 times harder, and feature superior earthquake energy absorbing capability. They enable the structure to experience smaller sway during a seismic incident and thus prevent damage. The panels also enable more freedom in building design. The structural stability they offer allows special demands to be met such as the window being placed on the south side of the building, a feature popular among Japanese consumers due to the sunlight access it brings. Also, the effective use of domestic materials contributes to the formation of environmentally friendly forests in Japan.



Sumitomo Forestry School of Professional Building Techniques

### Human Capital Development System Capable of Training Traditional Construction Methods through to Cutting Edge Techniques

Sumitomo Forestry established the specialty training program Sumitomo Forestry School of professional Building Techniques in 1988 to develop construction craftsmen and ensure continuous and stable productivity and high quality in our construction. Through one year of training, participants are taught knowledge and skills needed as a construction carpenter, and based on that taught our original cutting edge construction techniques and the manner expected of them as professional craftsmen. As basic skills, participants are taught traditional Japanese construction methods ranging from tool construction, to tool use, to stereotomy\*. This original training system has been highly praised, as seen by the selection of graduates as national representatives for Japan in the carpentry category for the 39th World Skills Competition, where they joined other Japanese craftsmen to showcase Japan as a leader in "monozukuri" (manufacturing).

\* Stereotomy: A method for designing building layouts based on component materials via imagining the structure and parts of the building geometrically, using rings, rulers and compasses.



### An IT System that Supports Customer Service and the Lowering of Operation Costs

At Sumitomo Forestry, we actively use IT to lower operating costs and improve our ability to quickly meet all customer needs. Specifically, we introduced a presentation system capable of quickly showing customers images of their home to strengthen our ability to speedily incorporate all customer preferences into designs. In addition, our NACCS system centrally manages contract and materials procurement data with an easy-to-use interface for outside business partners, making even lower operation costs possible. The system also aids in ensuring quality, thus bringing about productivity improvements.

## INTERVIEW



Real Estate Business Headquarters  
Real Estate Solution Business Division  
Tokyo Business Division General Manager  
**Hideki Iida**

Up until the end of last fiscal year, we positioned our real estate effective use business as a business partner for landowners with a business development strategy of assisting landowners make effective use of their real estate assets by creating solutions that leverage our marketing and information network strengths. Beginning in April of this year, we adopted a new business strategy placing land acquisition for our own use at the forefront of our business development activities.

While we previously combined our housing and land use know-how to develop business oriented to regional and market needs, our new strategy places us as the leader of business development (i.e. the landowner) and enables us to provide the high-quality living environments that society and communities are seeking. In particular, through our long tradition and experience in creating living environments, in response to the rapid aging of Japanese society we are aggressively preparing and offering housing and nursing care facilities for elderly people.

## OTHER BUSINESSES

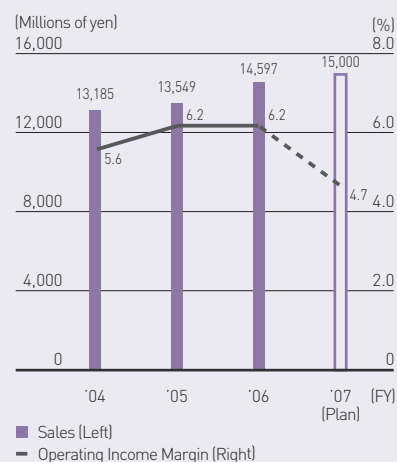
### Segment Performance Highlights

	FY2004	FY2005	FY2006	FY2007 Plan
Sales	13,185	13,549	14,597	15,000
Operating income	738	841	903	700
Assets	8,650	9,139	9,067	—
Capital expenditures	754	980	811	—

Note: The sales figures given include intersegment transactions. Operating income figures include internal profit prior to the deduction of amounts such as intersegment transactions and headquarters expenses that are not apportionable.

(Millions of yen)

### Sales and Operating Income Margin



The business of the Sumitomo Forestry Group extends beyond its core business of providing comfortable living and includes offering a wide range of services to support fulfilling lifestyles for customers as well as support for the surrounding communities and environment. These services include the production and sale of farm and garden materials, insurance brokerage, information systems development and leasing services.

### FISCAL 2006 PERFORMANCE REVIEW

Sales +7.7%, Operating Income +7.4%

Other Businesses segment sales increased 7.7% year on year to ¥14.5 billion. Insurance brokerage and leasing subsidiary Sumirin Enterprises Co., Ltd., was the primary contributor to the sales growth backed by strong sales of property insurance to our housing customers. Operating income rose 7.4% to ¥0.9 billion.

### STRATEGIES FOR FISCAL 2007

Operations in the Other Businesses segment are primarily oriented to providing services to the Group and focus on developing systems to promote the ongoing smooth implementation of business activities within the Group and enhancement of the Group's profitability. With regard to Sumirin Enterprises Co., Ltd., we aim to increase profitability by expanding its share of the property insurance sold to Sumitomo Forestry housing customers. We aim to raise the percentage of our customers purchasing insurance from Sumirin to about 50% by offering services matched to specific needs of local communities.

# CORPORATE SOCIAL RESPONSIBILITY

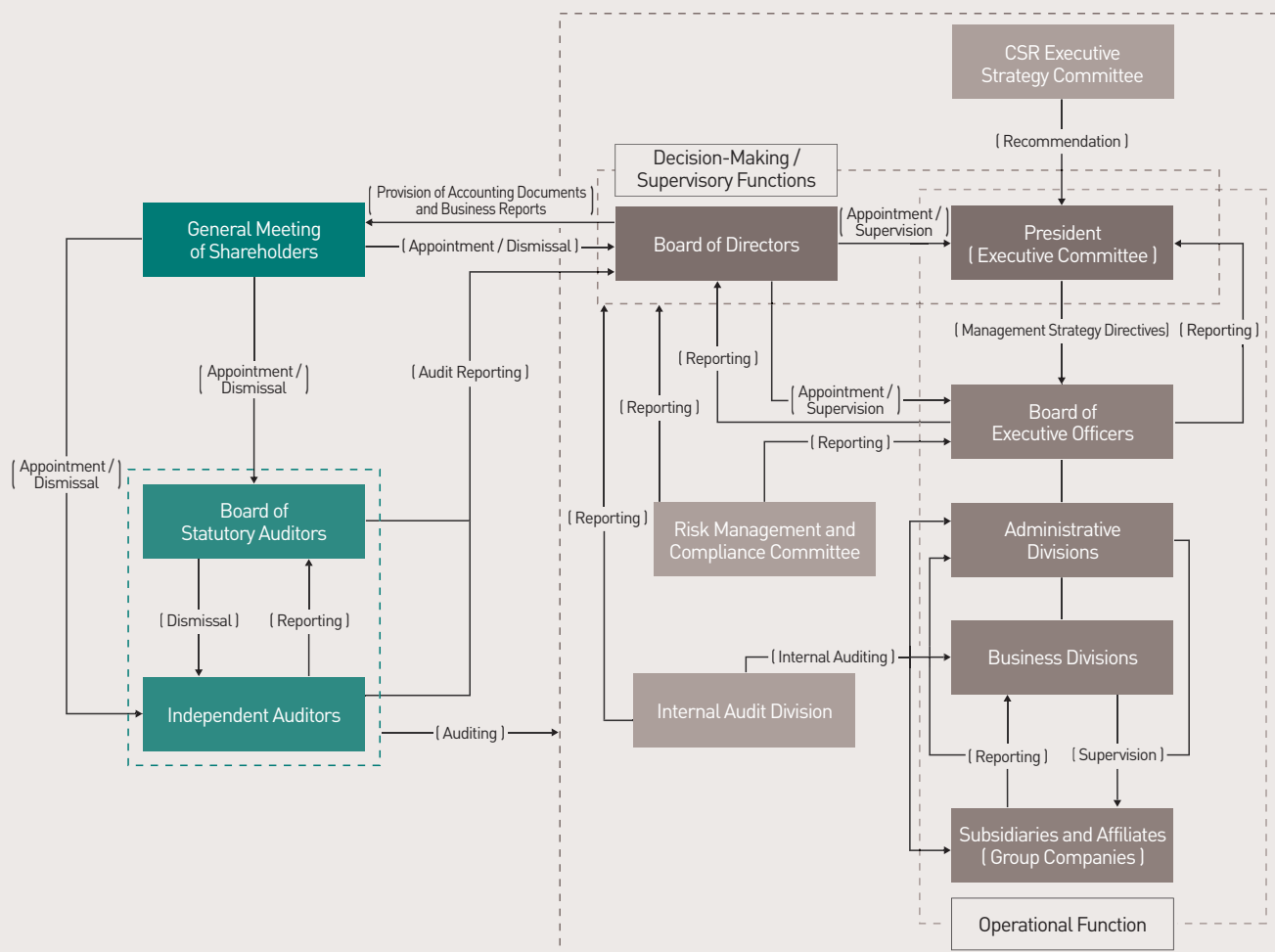
## CONTENTS

- 34. Our Management System
- 37. Directors
- 38. Our Corporate Social Responsibility



# OUR MANAGEMENT SYSTEM

## Business Execution and Management Supervision Mechanism



## CORPORATE PHILOSOPHY

The Sumitomo Forestry Group utilizes timber as a renewable, healthy, and environmentally friendly natural resource, and contributes to a prosperous society through all types of housing-related services.

## ACTION GUIDELINES

### Sumitomo Spirit

- We conduct business based on principles of integrity and sound management.

### Respect for Humanity

- We create an open and inclusive corporate culture that instills a strong sense of pride and motivation in employees.

### Environmental Protection

- We contribute to the protection of the environment and our fellow beings through responsible business practices.

### Putting Customers First

- We act with customer satisfaction first and foremost in mind.

## THE MANAGEMENT SYSTEM FUNDAMENTAL STANCE

The Sumitomo Forestry Group regards and makes efforts in enhancing and strengthening our system of corporate governance as one of our top priorities for management, including maintaining management transparency, conducting proper and lawful operations, and promoting swift decision-making and action. To promote and maintain an open-minded corporate culture in which each employee works with motivation and pride, we have adopted a management philosophy and code of conduct emphasizing the Sumitomo Spirit, respect for humanity, environmental protection, and putting customers first. We continuously promote the importance of this philosophy to all employees through public relations channels.

## CORPORATE GOVERNANCE

### Board of Directors and Executive Committee

In principle, the Board of Directors meets once a month to address decision-making and supervisory functions and specifically addresses decisions regarding important management matters, the review business performance, and determination of measures to fortify supervisory functions related to business execution. The Executive Committee, in principle, meets twice a month to ensure complete preparation for discussion of issues at the Board of Directors meetings.

At present, directors are not provided non-performance related bonus incentives. The retirement benefit system for directors was abolished in June 2005 and replaced by a remuneration and bonus system closely linked to business performance.

### Executive Officer System

In June 2002, we introduced an executive officer system and separated the decision-making and supervisory functions from business execution functions to improve the speed of management, enhance the business execution supervisory function, and clarify responsibility for business execution.

### Board of Auditors

The group's Board of Auditors consists of four statutory auditors, including two external auditors. In addition to attending important company meetings, auditors meet once every three months to exchange views with representative directors regarding business issues and improvements to the auditing environment, and meet

periodically to exchange information with the auditors of Group companies to support the overall appropriateness group operations. The Internal Auditing Department works in concert with the statutory auditors by performing internal audits of the appropriateness and lawfulness of the daily operations of the group.

### External Statutory Auditors

The two external statutory auditors are Mr. Hiroshi Miki and Mr. Satohiko Sasaki. Hiroshi Miki is an attorney and legal expert focusing on providing an objective evaluation of the appropriateness of the group's business operations. Satohiko Sasaki, who is deeply versed in forest administration, focuses on providing an objective evaluation of the appropriateness of the company's environmental operations and business development activities in Southeast Asia. To enable the external statutory auditors to best perform their supervisory function and ensure smooth progress in meetings, the external auditors attend meetings of the Board of Directors and keep an administrative office in the General Administrative Division. They are advised of meeting schedules and provided preparatory materials to ensure they are fully informed about the issues to be discussed.

### Strengthening Disclosure and Accountability

We at Sumitomo Forestry realize that raising transparency in our management in a very important issue in corporate governance. To meet this responsibility we disclose at appropriate times not only business decision related information but also corporate and financial information to shareholders and other stakeholders. Also, we work to communicate the feedback received from stakeholders to management.

## BASIC POLICY FOR INTERNAL CONTROL SYSTEM DEVELOPMENT AND IMPLEMENTATION

At a meeting of the board of directors in May 2006, the group established the “Basic Policy for Internal Control System Development and Implementation” to identify current and future issues associated with the group’s internal control systems with the aim of further enhancing corporate governance and constructing a more effective risk management system. In addition, in July 2006 we established a dedicated project team to work with the group’s auditing firm to construct an internal control system to ensure the appropriateness of financial reporting with the aim of introducing the system in April 2008.

## COMPLIANCE AND RISK MANAGEMENT

The Sumitomo Forestry Group is committed to compliance and is fully aware that, as a member of society, compliance is essential to continuing our business activities. The group considers its compliance activities to be among its most important management issues.

In July 2006, the Compliance Group was established in the General Administrative Division to strengthen the compliance administrative system and to promote and coordinate compliance management throughout the group. The Compliance Group’s main activities include identifying and developing response measures to potential compliance risk in the group’s business. In this way we are working to strengthen our compliance framework.

The group’s risk management activities include monitoring and supervision by the board of directors and risk management on a corporate governance level by the statutory auditors. For risk management within each business division, each division handles management of the risk that inevitably exists in their business promotion activities, such as the credit status of trading partners, inventory management, market conditions, occupational safety, product quality, and the environmental impact.

In addition, the General Administrative Division oversees risk management regarding important risk issues that affect the whole group, such as disaster response, compliance, and information security.

### EXAMPLES OF ACTIVITIES IN COMPLIANCE AND RISK MANAGEMENT

#### Establishment of the “Compliance Counter”

With the aim of activating a self-policing function in our operations, the group has established the Compliance Counter consultation system to receive information from employees and quickly identify and resolve compliance issues, such as illegal activities or actions opposing our corporate ethic, which could be easy to overlook within regular operating processes. The Compliance Counter features the General Manager of the General Administrative Division and legal advisors as communication representatives.

#### Establishment of the Emergency Hotline

In preparation for an emergency situation, the group has set up an around-the-clock, 7-days-a-week dedicated emergency hotline and response mechanism for use by all group personnel for swift and effective response in the case of an emergency. The response system includes a “two-hour rule” for reporting emergency situations to top management enabling them to swiftly provide guidance and directives for addressing the situation.

#### Information Security

Due to the character of our business, the group maintains a large volume of detailed customer information over long periods, and ongoing enhancement of our information security to protect private information as well as other data is a top priority. The group’s proactive stance on data protection includes raising employee awareness of security issues through special training and online courses on the Personal Information Protection Act and strict in-house rules regarding the use of digital memory media.



# DIRECTORS



First row, from the left

**Ryu Yano**  
President and Executive Officer

**Shoichi Takahashi**  
Vice president and Executive Officer

Second row, from the left

**Hitoshi Hayano**  
Managing Executive Officer

**Mamoru Inoue**  
Managing Executive Officer

**Hideki Nose**  
Managing Executive Officer

**Hideyuki Kamiyama**  
Managing Executive Officer

**Shigehiko Shiozaki**  
Managing Executive Officer

## DIRECTORS

* President/Director	Ryu Yano
* Director	Shoichi Takahashi
Director	Hideki Nose
Director	Hideyuki Kamiyama
Director	Mamoru Inoue
Director	Shigehiko Shiozaki
Director	Hitoshi Hayano

(\* Representative Director)

## STATUTORY AUDITORS

Senior Statutory Auditor	Shuji Kitamura
Statutory Auditor	Toshio Kohigashi
* Statutory Auditor	Hiroshi Miki
* Statutory Auditor	Satohiko Sasaki

(\* Outside Corporate Auditors as stipulated by the Commercial Code)

## EXECUTIVE OFFICERS

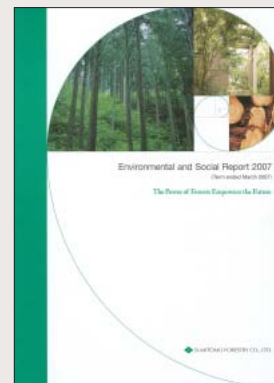
* President and Executive Officer	Ryu Yano	
* Vice President and Executive Officer	Shoichi Takahashi	Responsible for Personnel, Executive Manager of Timber and Building Materials Business Headquarters
* Managing Executive Officer	Hideki Nose	Responsible for Intellectual Property, Tsukuba Research Institute, Executive Manager of Forestry and Environmental Headquarters
* Managing Executive Officer	Hideyuki Kamiyama	Responsible for Corporate Planning, General Administrative, Finance, Information Systems, Internal Audit
* Managing Executive Officer	Mamoru Inoue	Executive Manager of Overseas Business Headquarters
* Managing Executive Officer	Shigehiko Shiozaki	Executive Manager of Housing Business Headquarters
* Managing Executive Officer	Hitoshi Hayano	Executive Manager of Real Estate Business Headquarters
Managing Executive Officer	Hiroshi Ando	Assistant Executive Manager of Timber and Building Materials Business Headquarters
Executive Officer	Masahiro Nishimura	President and Director of Sumitomo Forestry Home Tech Co., Ltd.
Executive Officer	Josuke Toyoda	General Manager of Information Systems Division
Executive Officer	Kaoru Takeshita	President and Director of Sumitomo Forestry Two-By-Four Homes Co., Ltd.
Executive Officer	Koji Takata	President and Director of Sumitomo Forestry Crest Co., Ltd.
Executive Officer	Hideo Watabe	Assistant Executive Manager of Real Estate Business Headquarters and General Manager of Real Estate Solution Business Division of the same headquarters
Executive Officer	Yasuyuki Yamamoto	Assistant Executive Manager of Housing Business Headquarters, General Manager of Product Development Division of the same headquarters and General Manager of Technology Division of the same headquarters
Executive Officer	Jiro Kuramitsu	Assistant Executive Manager of Overseas Business Headquarters and General Manager of Overseas Development Division of the same headquarters
Executive Officer	Akira Ichikawa	General Manager of Corporate Planning Division

(\* Doubles as Director and Executive Officer)

(As of June 22, 2007)

# OUR CORPORATE SOCIAL RESPONSIBILITY

Sustainability is the very core of the Sumitomo Forestry Group's corporate philosophy as the group has been practicing "sustainable forestry" since its founding over 300 years ago. We regard corporate social responsibility (CSR) as "returning to our starting point and reexamining our corporate philosophy of sustainability" and we continue to uphold and raise our corporate stature as a company essential to society.



For further details regarding Sumitomo Forestry's corporate social responsibility efforts, please refer to the Environmental and Social Report 2007.

## ENVIRONMENTAL VISION

In December 2005, the Group established the Medium-Term Environmental Management Policy placing "environmental coexistence" as a management cornerstone for achieving a viable balance of economical and environmental factors in our business operations. The policy focuses on four themes: 1) engaging in comprehensive environmental management, 2) strengthening and promoting environmental education, 3) providing thorough environmental reporting, and 4) promoting activities that contribute to society.

(Further details, please see our Environmental and Social Report website: <http://sfc.jp/english/information/ir/library/#environmental>)

## ENVIRONMENTAL COEXISTENCE THROUGH BUSINESS ACTIVITIES

### "MyForest" and Environmental Coexistence (New Custom-Built Housing Business)

A fundamental design of our MyForest detached-housing product line launched in October 2005 is the harnessing of natural shading, heat resistance and storage, air circulation, and other elements to provide a naturally comfortable living environment without over-reliance on heating and cooling. The energy efficiency of these units meets the strict specifications of the government's Next Generation Energy Conservation Standards\*. Also, at the design stage of each of these custom-built units, a lighting simulation test is conducted to evaluate the impact from adjacent buildings. Our meticulous approach to enhancing the energy saving capabilities of the MyForest products has enabled us to lower the CO<sub>2</sub> footprint of these homes by about 20% over other units that also meet the Next Generation Energy Standards.

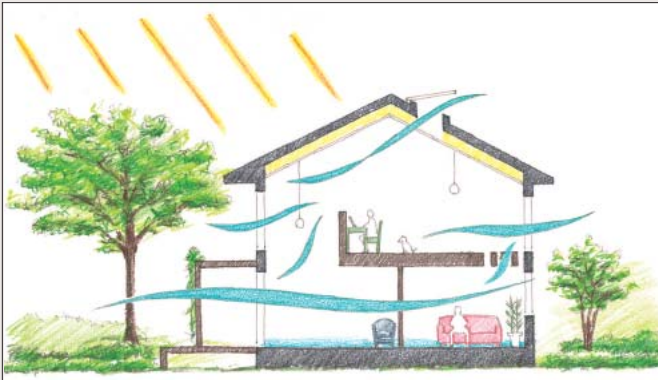
\* Next Generation Energy Conservation Standards: Adopted in Japan in 1999 to promote improved insulation and reduction of energy consumption in housing units.

### Environmental Coexistence through Use of Domestic Materials (New Custom-Built Housing Business, Distribution of Timber and Building Materials Business)

About 70% of Japan's land area is forest, and the Sumitomo Forestry Group maintains about 40,000 hectares, representing approximately 1/1,000 of the total. Nevertheless, about 80% of the timber material used in Japan is imported. This reliance on imported timber has led to reduced thinning, pruning and other efforts to maintain domestic forests, and the amount of forest in Japan that can effectively contribute to absorbing CO<sub>2</sub> and the future common good is rapidly dwindling. To promote environmental coexistence through the use of domestic timber resources, the Custom-Built Housing Business constructs its MyForest homes using materials such as the high-performance glue-laminated "Super Cypress" made from 100% domestic-grown Japanese cypress. We have achieved 51% usage of domestic timber materials in our principal structural members and are ambitiously aiming to raise this percentage to 70%. In addition, in fiscal year 2007, the Distribution of Timber and Building Materials Business successfully increased the volume of high-precision dry timber MIZDAS using our new drying technology by 67% year on year to 22,459m<sup>3</sup>.

## ENVIRONMENTAL MANAGEMENT

In fiscal year 1997, our housing division became the first company in the housing industry to earn ISO 14001 certification, and in fiscal year 2002 we renewed the certification for all of the parent company's operations. We are also making solid progress in earning certification for our group companies. PT. AST Indonesia received ISO 14001 certification in fiscal year 2006, and four domestic group companies were added to of the overall ISO-certification. In addition, we introduced environmental budgets in all of our domestic and overseas operations in fiscal year 2006 to make environmental management an active element in everyday operations.



“**Ryo-on-bo**”: To allow people to spend each day in health and comfort, this type of housing skillfully incorporates the power and rhythm of nature. The approach toward homes that the Japanese have developed and built over centuries is realized through modern technology.

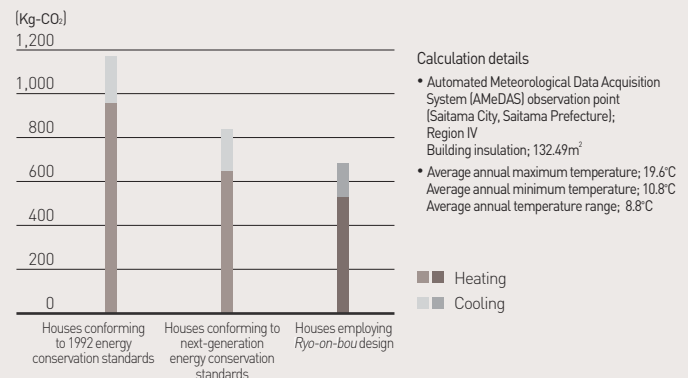
## ENVIRONMENTAL RISK MANAGEMENT

We are seeking to rid our operations of activities with potential or known environmental risk, such as waste treatment, the use of asbestos, illegal logging and soil pollution and developing specific countermeasures for related business departments. Thanks to these efforts, we found no significant infractions of environmental regulations and there were no environmental accidents at any of our group companies in fiscal year 2006. Our efforts to further strengthen and improve our environmental risk management include close examination and action in the following areas of concern for the future.

### Preventing Illegal Waste Disposal

In fiscal year 2006, we conducted an exhaustive examination of the industrial waste treatment conditions at all of the companies in the Sumitomo Forestry Group and immediately corrected all consignment contracts and manifests that were found to be inadequate in their waste treatment processes. In addition, we conducted 24 study sessions attended by 506 staff from across the country to enhance knowledge about proper industrial waste treatment processes. At the parent company and all of our affiliated companies, we have established strict regulations regarding industrial waste management and a management system with clearly defined management roles and responsibilities. We have begun transitioning all group companies to an electronic manifest system and are concentrating our business transactions with waste treatment operators onto companies with superior efforts in compliance to waste treatment policies. We will continue to conduct internal audits and inspections of waste treatment facilities to be fully informed of our industrial waste treatment management conditions and to further enhance our abilities to implement the most appropriate waste treatment in each business operation at all companies in the group.

### Comparison of CO<sub>2</sub> Emissions from Houses Using Eco Assessment Charts\*



Eco Assessment Charts: Assessment record of CO<sub>2</sub> emissions and air-conditioning expenses for each house plan calculated based on the insulation specification used and others assumptions, and on regional AMeDAS climate data for the house location. Environmental design is carried out based on this assessment record.

## Measures to Prevent Global Warming

Residential housing is the source of about 13% of all CO<sub>2</sub> emissions in Japan, and this percentage rises with each passing year. As a housing provider, we believe our group bears a strong responsibility in this matter. Our group efforts therefore go beyond actions to reduce the CO<sub>2</sub> emissions of our operations and work to enhance nature's ability to absorb CO<sub>2</sub> from the environment by promoting the use of locally grown domestic timber and proper forest management.

Overseas, upgrades to the timber chip fiber processing equipment at Nelson Pine Industries Ltd. in New Zealand resulted in a 10% reduction in electricity consumption and a 5% decrease in CO<sub>2</sub> emissions from the previous fiscal year. Overall, however, our expanding business operations led to a 7.2% year on year increase in CO<sub>2</sub> emissions to 199,576 tons in fiscal year 2006. We are steadfastly determined to reduce our CO<sub>2</sub> output and are continuing to promote and amplify our CO<sub>2</sub> reduction measures.

## WORKING WITH OUR STAKEHOLDERS

### Working with Business Partners

In line with our Green Procurement Guidelines, our purchase transactions prioritize products and services with low environmental impact from business partners that share our dedication to reducing the environmental burden of their operations. We also set strict Safety and Sanitation Control Regulations in our operations with builders to reduce labor accidents at construction sites.

### Working with our Customers

The Sumitomo Forestry Group has earned a reputation among its customers as the leader in the custom-built wooden housing field as the “wood” and “living” specialist. To continue providing the high quality, high performance housing that backs this reputation, we conduct inten-





Students gain full understanding through the study comic "Mori-to-ki-no-Himitsu" [The Secrets of the Forest and Trees]



"Kikorin"  
Created in 2006, the tree spirit "Kikorin" is our new character to symbolize our commitment to sustainability. In a friendly way, Kikorin conveys the Spirit of Sumitomo Forestry for the creation of a future where people and nature co-exist.

sive testing and verification at the Tsukuba Research Institute in order to identify potential issues with our existing housing products and introduce materials that will further raise our product quality and performance. Recognizing that purchasing a home is a major investment for our customers, we are promoting a housing performance reporting system to provide customers a greater sense of security when they purchase our products. This indication system provides data from careful evaluations by third-party specialists of the performance of each of our housing products. We provided Housing Performance Evaluation at Design Stage on 95.9% of our housing products in fiscal year 2006.

### Working with Society

As a good corporate citizen, we operate as an open company inviting students to tour our company and hold public seminars and other activities to present our corporate position and share our vision. Among our activities are the Forest of Learning events we have held in the national forests on the slopes of Mount Fuji to support the restoration of natural forest after typhoons. Since 1997 large numbers of people from Sumitomo Forestry and our business partners joined with volunteers to carry out large-scale forest replanting, and these events have progressed to thinning and other forest sustainability activities as we work to regenerate the forest.

In fiscal year 2006, we participated in the publication of the study comic "The Secrets of the Forests and Trees" and donated approximately 26,000 copies to elementary schools and public libraries across the country. We believe this publication provides an opportunity for a wide range of children in Japan to learn about the current conditions surrounding forests in their environmental studies and encourages understanding of the relevance of environmental issues. In addition, in January 2007 we opened the Sustainable Forest Gallery in the popular Omotesando Hills shopping center in Tokyo to provide an access point for appreciation of the uses of domestic timber for an audience of jun-

ior high and high school students, who would not ordinarily have the opportunity to consider the importance of forests.

Among our social contributions overseas, our affiliated company PT. Kutai Timber Indonesia established the KTI Educational Foundation in 2000 to provide scholarships primarily to elementary school children. The company also provides donations, living assistance and emergency supplies.

### Working with our Employees

The Sumitomo Forestry Group views each of its employees as a treasured company asset and aims to provide a safe work environment that can accommodate the full range of human diversity. As a housing company, we also take great interest in being a company that supports the home lifestyles of our employees and their families and actively endeavor to facilitate a healthy balance of career and family life. In fiscal year 2006, we revised our child and nursing care program to provide an extra off day each week for employees raising children or providing special care for a family member. We also expanded such programs as that to provide full remuneration for the first five days of parental leave to fathers, and expanded our shortened work day program to parents of children up to the fourth grade.

### Working with our Shareholders

We constantly seek to improve the quality of management by increasing transparency through appropriate information disclosure and active publicity and IR activities to continue to build on our relationship of trust with our shareholders and investors. We have been selected from among 2,500 companies globally for the third consecutive year for inclusion in the Dow Jones Sustainability World Index (DJSI World) for being in the top 10% in terms of economy, environment and social aspects. Recognition of our efforts to fulfill our social responsibility has also led to annual inclusion in the FTSE 4 Good Global Index.

## FINANCIAL SECTION

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52.	Consolidated Statements of Cash Flows
53.	Notes to Consolidated Financial Statements
65.	Report of Independent Auditors

## TEN-YEAR SUMMARY

Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
Years ended March 31

	Millions of yen (unless otherwise specified)		
	2007	2006	2005
Operating Results:			
Net sales and contract revenues	¥ 911,674	¥ 791,128	¥ 723,193
Timber and Building Materials Business* <sup>1</sup>	520,103	412,182	320,255
Housing and Housing-Related Businesses* <sup>1</sup>	407,780	393,868	418,313
Other Businesses	14,597	13,549	13,185
Elimination and/or corporate	(30,806)	(28,471)	(28,560)
Gross profit	141,117	127,853	125,582
Selling, general and administrative expenses	120,711	112,407	107,116
Operating income	20,405	15,446	18,466
Timber and Building Materials Business* <sup>1</sup>	7,967	2,806	4,615
Housing and Housing-Related Businesses* <sup>1</sup>	16,586	16,370	17,530
Other Businesses	903	841	738
Elimination and/or corporate	(5,051)	(4,571)	(4,418)
Recurring income* <sup>2</sup>	21,259	16,800	18,692
Net income (loss)	11,954	10,842	8,014
Financial Position:			
Total assets	¥ 500,136	¥ 464,193	¥ 370,684
Working capital* <sup>3</sup>	76,453	68,037	67,579
Interest-bearing debt	25,739	22,067	15,580
Total net assets* <sup>4</sup>	188,855	175,206	152,500
Cash Flows:			
Cash flows from operating activities	¥ 7,084	¥ 16,626	¥ 6,685
Cash flows from investment activities	(7,102)	(8,998)	(12,895)
Cash flows from financing activities	665	(14,039)	(7,087)
Cash and cash equivalents at the end of the year	50,311	49,628	55,928
Capital Investment* <sup>5</sup>			
Tangible fixed assets	¥ 6,724	¥ 8,132	¥ 7,016
Software	1,581	1,857	1,673
Others	721	454	549
Total	9,026	10,443	9,237
Depreciation and amortization	6,476	6,403	6,452
Per Share Data:	Yen		
Net income (loss)	¥ 67.4	¥ 61.3	¥ 45.3
Net assets	1,059.2	996.0	866.5
Cash dividends	15.00	13.00	13.00
Financial Ratios:	%		
Gross income margin	15.5	16.2	17.4
Operating income margin	2.2	2.0	2.6
Recurring income margin	2.3	2.1	2.6
Return on asset (ROA)* <sup>6</sup>	4.4	4.0	5.0
Return on equity (ROE)* <sup>6</sup>	6.6	6.6	5.4
Equity ratio	37.5	37.7	41.1
Interest-bearing ratio* <sup>7</sup>	12.1	11.2	9.3
Current ratio	129.3	129.3	137.4
Interest coverage ratio [times]	11.2	10.8	18.6

Notes: 1. Starting in fiscal 2001, the profits from transactions in housing materials have been included in the Housing and Housing-Related segment; they were previously included in the Timber and Building Materials segment.

2. Recurring income = Operating income + Non-operating income – Non-operating expenses

Non-operating income includes interest income, purchase discounts, dividends income, foreign exchange gains, miscellaneous gains, and other income generated from normal business activities. Non-operating expenses include interest expense, sales discounts, loss on devaluation of property, plant and equipment, foreign exchange losses, miscellaneous expenses, and other expenses from normal business activities.

3. Working capital = Current assets – Current liabilities



Millions of yen (unless otherwise specified)						
2004	2003	2002	2001	2000	1999	1998
¥ 673,779	¥ 645,100	¥ 644,730	¥ 682,375	¥ 699,594	¥ 620,615	¥ 713,728
293,220	283,517	270,856	279,811	340,988	294,411	333,941
393,616	370,421	381,978	405,150	370,692	335,782	380,781
12,350	17,882	18,050	16,978	15,481	13,900	10,818
(25,408)	(26,721)	(26,154)	(19,565)	(27,568)	(23,480)	(11,812)
120,778	109,631	109,437	118,064	112,269	99,692	107,877
103,201	100,858	106,397	102,065	98,720	93,481	102,072
17,577	8,772	3,040	15,999	13,549	6,210	5,805
3,813	2,238	1,882	5,128	14,770	11,341	6,870
17,150	9,920	4,961	16,631	5,141	942	1,832
644	415	579	519	569	1,315	985
(4,030)	(3,802)	(4,384)	(6,279)	(6,933)	(7,388)	(3,882)
17,074	9,721	3,731	16,908	12,541	6,305	6,694
9,870	(15,439)	465	6,994	5,708	134	2,145
¥ 369,755	¥ 357,322	¥ 365,531	¥ 371,102	¥ 360,935	¥ 346,293	¥ 341,325
66,377	60,260	60,477	61,319	68,892	71,746	62,992
19,929	16,497	18,124	24,517	35,720	40,059	47,188
146,269	129,727	147,440	150,979	144,914	139,301	140,357
¥ 25,962	¥ 19,734	¥ 17,332	¥ 3,468	¥ (3,281)	¥ 26,715	¥ 9,561
(7,646)	2,026	(16,439)	(1,960)	(3,330)	2,068	(6,200)
(735)	(8,171)	(9,716)	(13,873)	(5,351)	(8,257)	(9,100)
69,312	52,029	38,873	47,476	59,916	71,971	51,302
¥ 4,040	¥ 2,761	¥ 7,705	¥ 4,448	¥ 4,373	¥ —	¥ —
1,468	2,077	2,194	1,889	1,264	—	—
883	283	225	252	303	—	—
6,392	5,123	10,124	6,590	5,941	4,556	13,172
6,447	5,985	5,289	4,551	4,756	5,060	5,057
Yen						
¥ 55.8	¥ (87.5)	¥ 2.6	¥ 39.6	¥ 32.4	¥ 0.8	¥ 12.2
830.5	736.4	835.1	854.9	821.6	789.8	795.8
13.00	10.00	10.00	10.00	10.00	10.00	10.00
%						
17.9	17.0	17.0	17.3	16.0	16.1	15.1
2.6	1.4	0.5	2.3	1.9	1.0	0.8
2.5	1.5	0.6	2.5	1.8	1.0	0.9
4.7	2.7	1.0	4.6	3.5	1.8	1.7
7.2	(11.1)	0.3	4.7	4.0	0.1	1.5
39.6	36.3	40.3	40.7	40.1	40.2	41.1
12.0	11.3	10.9	14.0	19.8	22.3	25.2
135.7	132.6	131.8	131.1	137.7	141.6	137.4
21.9	18.3	7.8	22.6	18.6	5.8	4.3

4. Total net assets are presented following enforcement of the new Japanese Corporate Law in 2006. Total net assets are comprised of the sum of shareholders' equity as previously defined and minority interest and gains (losses) on deferred hedges.

5. Disclosure of capital investment was not institutionalized prior to fiscal 2000, thus data prior to fiscal 2000 is only partially available.

6. ROA and ROE are calculated using the simple average of beginning and end of term balance sheet figures.

ROA = Recurring income / Total assets

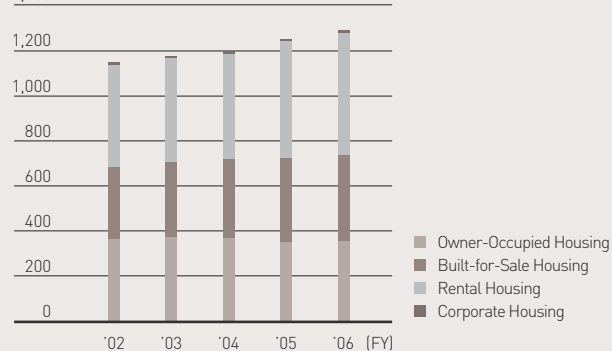
ROE = Net income (loss) / Shareholders' equity

7. Interest-bearing debt ratio = Interest-bearing debt / (Interest-bearing debt + Shareholders' equity)

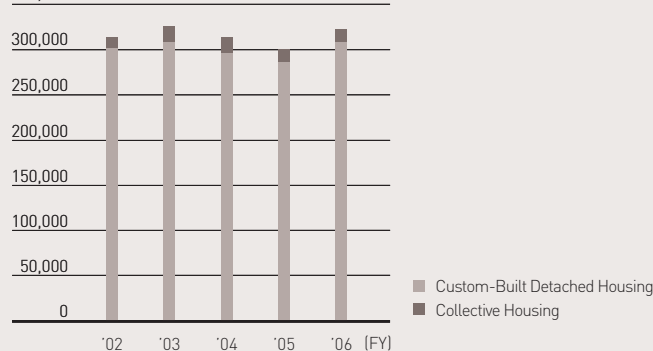
# MANAGEMENT DISCUSSION AND ANALYSIS

## (INCLUDING BUSINESS RISK DISCLOSURE)

Number of New Housing Starts in Japan

(Thousands units)  
1,400

Amount of Orders Received

(Millions of yen)  
350,000

## MARKET OVERVIEW

The Japanese economy remained in a general recovery trend in the term ended March 2007. The expanding economies in Europe, the United States, and Asia supported continued brisk exports and domestic production, and growth in corporate earnings led to increasing capital investment and improving employment conditions. In the household sector, however, uncertainty about future trends persisted as the growth in employee income levels and consumer spending remained flat.

In the housing sector, expectation of higher housing loan interest rates and rising land prices in metropolitan areas stimulated first-time home buyer demand, supporting growth in new housing starts of 2.9% year on year to 1.28 million units. Owner-occupied housing starts turned upward for the first time in three years, rising 0.9% year on year to 0.35 million units.

In the timber and building materials sector, the global supply and demand balance tightened as worldwide demand for timber increased. The domestic market was also brisk as the growth in new housing starts stimulated demand and led to increased product prices.

## CONSOLIDATED OPERATING RESULTS

### 1. Orders Received and Net Sales

Sales increased 15.2% year on year to ¥911.674 billion. Timber and Building Materials Business sales rose 26.2% year on year (this figure and all figures herein include intersegment transactions) on the first full-year contributions of subsidiaries that became subject to consolidation in the previous fiscal year along with expanded trading volume and higher unit prices. Housing and Housing-Related Business sales grew 3.5% supported by strong sales of its high value-added housing products highlighting the appeal of wood. The

order value for custom-built detached housing rose 7.5% year on year to ¥308.019 billion and the number of units increased 5.4% year on year to 9,751 units, supported by an expanded product line and the building of a fine-tuned sales system.

### 2. Selling, General and Administrative Expenses

Selling, general and administrative expenses increased 7.4% year on year to ¥120.711 billion. The increase was largely due to expense increases associated with the new consolidated subsidiaries, retirement benefit accounting methods, more staff added for business expansion, and enhanced marketing promotions.

### 3. Operating Income

As a result of the above developments, operating income increased 32.1% year on year to ¥20.405 billion. The growth in operating income was primarily attributable to increased sales of the Timber and Building Materials Business and improved profitability in the Housing and Housing-Related Business.

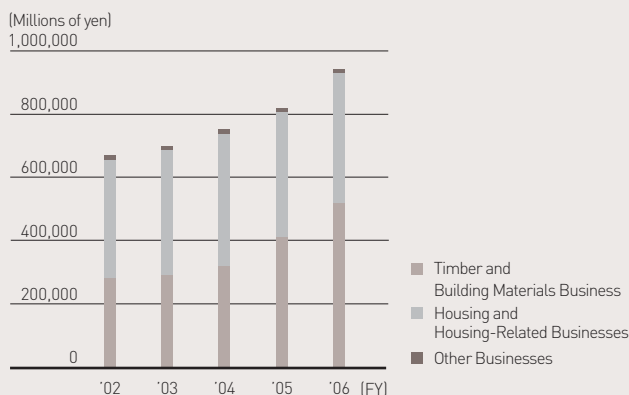
### 4. Other Income and Expenses

Other income minus other expenses declined 51.8% year on year to an income of ¥284 million. Interest and dividend income received increased ¥518 million over the previous term. However, the decline reflected the non-reoccurrence of ¥419 million in insurance gains booked as extraordinary income in the previous fiscal year as well as a ¥663 million provision for losses associated with business reorganization, a ¥352 million expense from office relocations, and other factors.

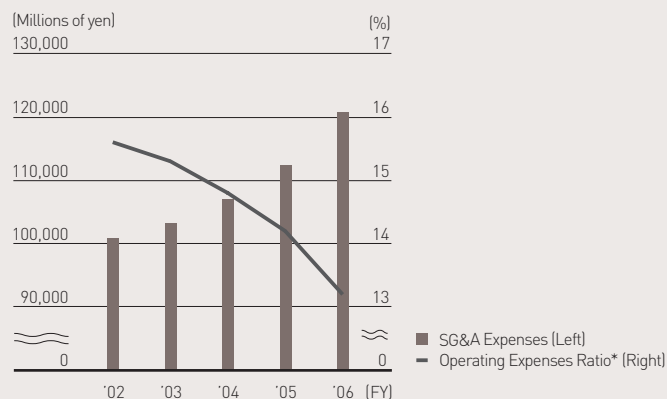
### 5. Net Income

Income taxes returned to the normal level after declining in the previous fiscal year owing to the end of operations at a subsidiary. Therefore, income taxes for fiscal 2006 increased ¥3.602 billion, or

### Net Sales and Contract Revenues



### SG&A Expenses and Operating Expenses Ratio



\* Operating Expenses Ratio = SG&A Expenses / Net Sales and Contract Revenues

72.6%, year on year to ¥8.561 billion. Net income rose 10.3% year on year to ¥11.954 billion. Net income per share rose ¥6 to ¥67.43 while return on equity (ROE) remained flat at 6.6%.

## SEGMENT RESULTS

(INCLUDING INTERSEGMENT TRANSACTIONS)

### 1. Timber and Building Materials Business

Net sales in Timber and Building Materials Business increased 26.2% over the previous fiscal year to ¥520.103 billion and operating income surged 183.9% to ¥7.967 billion. This steep sales and income growth was primarily due to the expanded revenue base from the merger with Ataka Kenzai Co., Ltd., and the increasing worldwide demand for wood and timber products that was accompanied by higher selling prices, particularly for timber and wood board, and expanded sales volume. The manufacturing of building materials business also provided a substantial contribution from higher sales prices and improved productivity.

### 2. Housing and Housing-Related Businesses

Net sales for the Housing and Housing-Related Businesses grew 3.5% over the previous fiscal year to ¥407.780 billion and operating income increased 1.3% to ¥16.586 billion. The carefully constructed sales system that enhanced competitiveness and improved heat-insulating performance and design expertise, along with mar-

keting strategies that boosted sales of high value-added housing, supported the sales and income growth.

## FINANCIAL POSITION AND CASH FLOW

### 1. Financial Position

During fiscal 2006, total assets had increased ¥35.943 billion over the previous fiscal year to ¥500.136 billion. Current assets increased ¥36.641 billion year on year to ¥337.072 billion on increases in accounts receivable and inventories accompanying the growth in sales. Tangible fixed assets increased ¥118 million to ¥74.050 billion, intangible assets declined ¥794 million to ¥6.313 billion, and investments and other assets decreased ¥21 million to ¥82.7 billion.

Total liabilities increased ¥25.419 billion to ¥311.281 billion. Current liabilities rose ¥28.225 billion to ¥260.619 billion owing to an increase in operating payables accompanying the growth in sales and in accounts payable on construction arising from the number of construction projects in progress. Long-term liabilities declined ¥2.806 billion to ¥50.662 billion and the balance of interest-bearing debt rose ¥3.672 billion to ¥25.739 billion.

Total net assets increased ¥10.524 billion\* to ¥188.855 billion year on year, primarily due to a ¥9.6 billion increase in retained earnings.

\* Due to changes in accounting methods, minority interest has been added to the total shareholders' equity of the previous fiscal year to facilitate comparison with the fiscal 2006 total shareholders' equity.

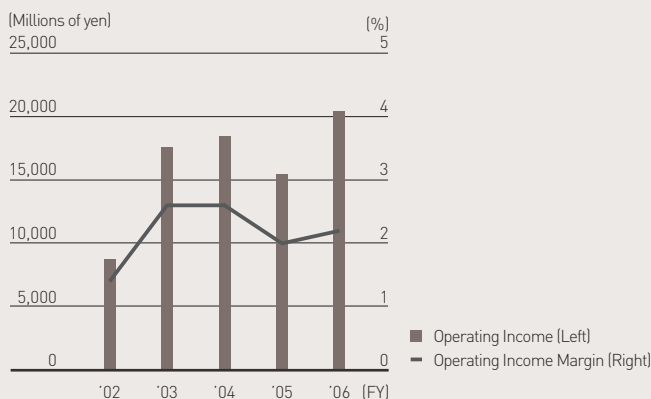
## Business Results by Segment

	Timber and Building Materials Business		Housing and Housing-Related Businesses		Other Businesses	
	FY2006	FY2005	FY2006	FY2005	FY2006	FY2005
Net sales	520,103	412,182	407,780	393,868	14,597	13,549
Operating income	7,967	2,806	16,586	16,370	903	841
Operating income margin	1.5%	0.7%	4.1%	4.2%	6.2%	6.2%

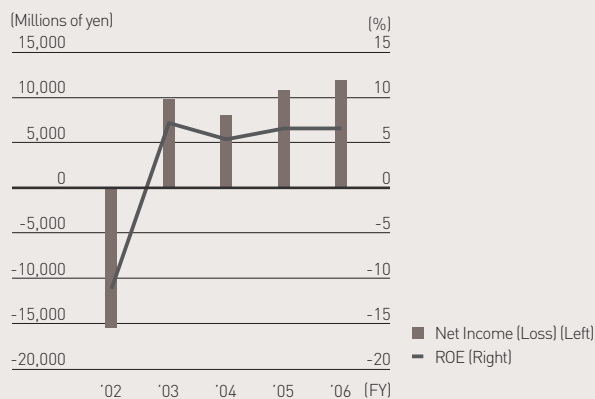
Note: The sales figures given above include intersegment transactions. Operating income figures include internal profit prior to the deduction of amounts such as intersegment transactions and headquarters expenses that are not apportionable.



## Operating Income and Operating Income Margin



## Net Income (Loss) and ROE



## 2. Cash Flow

Net cash provided by operating activities decreased ¥9.542 billion year on year to ¥7.084 billion. The decline was due to the increased notes and accounts receivables, as well as inventories associated with the sales growth in the Timber and Building Materials Business. Net cash used in investment activities declined ¥1.896 billion year on year to ¥7.102 billion, primarily from capital investment in factories of overseas subsidiaries and expenses incurred from the factory relocation of a domestic subsidiary. Net cash used in financing activities reversed from a ¥14.039 billion outflow in the previous fiscal year to a ¥665 million inflow as fund procurement by the parent company and subsidiaries exceeded repayment of interest-bearing debt, dividend payments and other expenses. The balance of cash and cash equivalents at the end of fiscal 2006 totaled ¥50.311 million, a ¥683 million increase over the previous fiscal year.

## BUSINESS RISK

The following risk factors involved in the business of the Sumitomo Forestry Group may have a large influence on the investment decisions of investors. Potential risk may include, but is not necessarily limited to, the following.

### 1. Housing Market Trends

The Sumitomo Forestry Group business results are heavily reliant on the trends in the housing market. Changes in the following business conditions may cause significant declines in housing orders that could negatively impact the group's business results.

#### 1) Interest Rate Fluctuation

Interest rate increases, particularly rises in long-term interest rates, can have an adverse effect on demand as they cause an increase in

total payments for customers purchasing detached housing, many of whom take out loans for the purchase, and for customers who build collective housing for the effective use of their land. The anticipation of rises in interest rates can induce a temporary surge in home purchases however as consumers seek to avoid high loan costs.

#### 2) Land Price Fluctuation

A sharp rise in land prices can have a negative effect on consumer inclination to purchase land on which to build housing. Conversely, a steep drop in land price is a form of asset deflation and can reduce demand for home reconstruction. Consequently, substantial rises or drops in land prices both have the potential to negatively impact the group's business results.

#### 3) Tax Systems Changes

An increase in the consumption tax rate that would directly apply to housing purchase amounts would potentially significantly reduce housing demand and could negatively impact the group's business results.

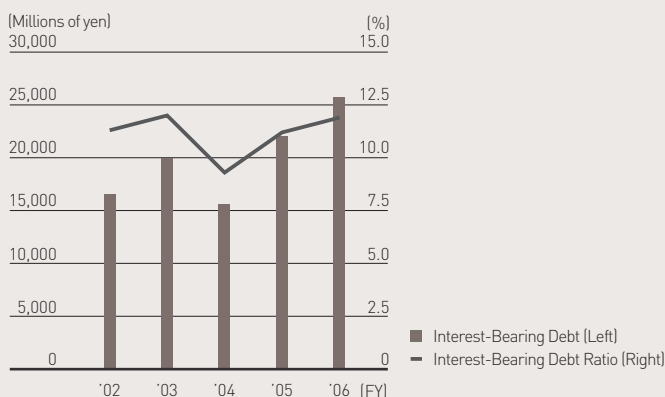
### 2. Statutory Changes

Laws and regulations surrounding the housing business include the Personal Information Protection Act in addition to the Building Standards Law, Construction Industry Law, Building Lots and Building Transaction Business Law, Urban Planning Law, National Land Use Planning Law, Housing Quality Assurance Law, and Waste Disposal and Public Cleaning Law (law concerning procedures for waste disposal and site clean-up). The Sumitomo Forestry Group diligently conforms to all laws and regulations while recognizing that the abolition, revision, or adoption of laws and regulations can substantially influence the group's business results.

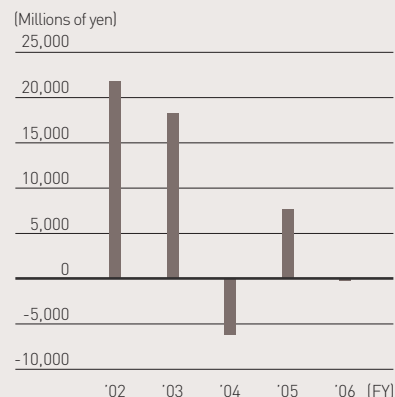
### 3. Timber and Construction Material Market Conditions

Declines in prices for timber and construction material reduce the profitability of the timber and construction material business. On

## Interest-Bearing Debt and Interest-Bearing Debt Ratio



## Free Cash Flows



the other hand, steep increases in prices for timber and construction material, as well as rises in prices for other housing materials, can lead to higher materials costs for the housing business which could negatively impact group results. Price fluctuations for other raw materials, such as oil, can directly or indirectly affect raw materials prices and influence the group's business results.

## 4. Exchange Rate Fluctuations

The group's import and export transactions are often conducted in foreign currencies, and fluctuations in exchange rates affect transaction value when converted in yen. The group endeavors to minimize the risk of significant impact through hedges using foreign exchange contracts; however, exchange rate fluctuations can influence the group's business results and financial position.

## 5. Product Quality Assurance

The group endeavors to implement complete quality control of its products, housing, and in all aspects of its operations. However, unforeseen circumstances can potentially lead to a significant quality issue that could influence the group's business results.

## 6. Overseas Business Activities

The group conducts various business activities overseas and engages in business transactions, such as product transactions, with various business partners overseas. Consequently, as is the case with domestic Japanese operations, laws and regulations, economic and social conditions, and consumer trends in the foreign countries in which the group conducts business can influence the group's business results.

## 7. Retirement Allowance Accounting

A significant deterioration in the operating environment for the group's pension assets, such as substantial fluctuations in the domes-

tic stock market or the necessity to revise the assumptions for pension actuarial calculations, can require an increase in pension assets or can increase the costs associated with the pension accounts, and could influence the group's business results and financial position.

## 8. Natural Disasters

Damage from a major earthquake, wind, flood, or other destructive natural element could result in cost increases from operating interruptions at facilities, safety verification of our housing products, completion delays for construction contracts, or other actions. A significant increase in costs caused by a natural disaster could influence group business results.

## 9. Information Security

The group maintains a large volume of customer information and makes every effort to ensure proper and secure information management through extensive training of executives and employees regarding regulations, systems maintenance, and other important aspects of information management. Despite these precautions, a leak of this customer information due to a computer system breach by a malicious third party, theft, human error by an employee or contracted individual, accident, or other cause could lead to customer claims for compensatory damages and destroy customer and market trust in the company, which could influence the group's business results.

## 10. Environmental Risk

Environmental protection is a top priority for the group and is one of the four action guidelines of the group's corporate philosophy. Changes to environmental regulations in Japan or overseas or the occurrence of major environmental issues could lead to fines, compensation payments, costs associated with resolving environmental problems, or other expenses that could influence the group's business results.

# CONSOLIDATED BALANCE SHEETS

Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
As of March 31, 2007 and 2006

ASSETS	Millions of yen		Thousands of U.S. dollars (Note 4)
	2007	2006	2007
Current assets:			
Cash and time deposits (Note 11)	¥ 47,385	¥ 44,720	\$ 398,194
Marketable securities (Note 5, 11)	3,000	5,000	25,208
Receivables-			
Notes and accounts, trade	167,404	138,260	1,406,757
Loans and other	50,138	51,226	421,327
Inventories-			
Finished goods, logs and lumber	30,087	22,413	252,831
Developed land and housing for sale	12,128	10,071	101,917
Land and housing projects in progress	16,698	15,628	140,320
Deferred income taxes (Note 8)	6,179	7,597	51,923
Other current assets	4,710	6,429	39,582
Allowance for doubtful accounts	(657)	(913)	(5,522)
Total current assets	337,072	300,431	2,832,537
Property, plant and equipment, at cost less accumulated depreciation (Note 7):			
Land	19,812	19,973	166,491
Buildings and structures	37,665	36,882	316,511
Machinery and equipment	62,587	60,054	525,942
Timberland (Note 6)	10,741	11,136	90,257
Construction in progress	3,867	4,426	32,495
	134,672	132,470	1,131,696
Less accumulated depreciation	(60,622)	(58,538)	(509,425)
Net property, plant and equipment	74,050	73,933	622,271
Intangible assets, net of amortization:			
Goodwill	927	1,532	7,790
Other intangible assets	5,386	5,575	45,264
Total intangible assets	6,313	7,107	53,054
Investments and other assets:			
Investment securities (Note 5)	71,584	71,413	601,550
Long-term loans and receivables	2,258	2,436	18,971
Deferred income taxes (Note 8)	1,101	1,242	9,248
Other assets	9,595	9,727	80,630
Allowance for doubtful accounts	(1,837)	(2,097)	(15,439)
Total investments and other assets	82,700	82,722	694,960
Total assets	¥ 500,136	¥ 464,193	\$ 4,202,822

See accompanying notes to consolidated financial statements.

LIABILITIES AND NET ASSETS	Millions of yen		Thousands of U.S. dollars (Note 4)
	2007	2006	2007
Current liabilities:			
Payables-			
Notes and accounts, trade	¥ 167,140	¥ 154,024	\$ 1,404,535
Other	8,297	6,679	69,727
Short-term debt (Note 7)	14,355	11,106	120,633
Current portion of long-term debt (Note 7)	2,621	2,113	22,025
Advances received from customers	44,446	37,920	373,499
Accrued income taxes	4,602	1,596	38,675
Accrued employees' bonuses	8,566	8,078	71,986
Accrued directors and corporate auditors' bonuses	83	—	698
Other current liabilities (Note 8)	10,507	10,877	88,297
Total current liabilities	260,619	232,394	2,190,075
Long-term liabilities:			
Long-term debt (Note 7)	8,763	8,848	73,640
Deferred income taxes (Note 8)	15,400	15,136	129,413
Accrued employees' retirement benefits (Note 16)	12,383	15,875	104,061
Other long-term liabilities	14,116	13,610	118,620
Total long-term liabilities	50,662	53,469	425,734
Contingent liabilities (Note 14)			
Net assets:			
Shareholders' equity (Note 12)			
Common stock-			
Authorized: 400,000,000 shares			
Issued and outstanding: 177,410,239 shares in 2007 and 176,603,881 shares in 2006	27,672	27,672	232,538
Capital surplus	26,882	25,655	225,898
Retained earnings	108,919	99,319	915,282
Treasury stock: 174,188 shares in 2007 and 761,629 shares in 2006	(184)	(617)	(1,549)
Total shareholders' equity	163,288	152,029	1,372,169
Valuation and translation adjustments:			
Unrealized gain on available-for-sale securities	22,482	22,125	188,923
Deferred gains or losses on hedges	155	—	1,304
Foreign currency translation adjustments	1,804	1,052	15,160
Total valuation and translation adjustments	24,441	23,177	205,387
Minority interests in consolidated subsidiaries	1,125	3,124	9,457
Total net assets	188,855	178,330	1,587,013
Total liabilities and net assets	¥ 500,136	¥ 464,193	\$ 4,202,822



# CONSOLIDATED STATEMENTS OF INCOME

Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
For the years ended March 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 4)
	2007	2006	2007
Sales:			
Net sales	¥ 545,735	¥ 439,516	\$ 4,586,004
Contract revenues	365,940	351,612	3,075,125
Total	911,674	791,128	7,661,129
Cost of sales:			
Cost of sales	504,152	408,124	4,236,575
Cost of contracts completed	266,405	255,151	2,238,700
Total	770,558	663,275	6,475,275
Gross profit	141,117	127,853	1,185,854
Selling, general and administrative expenses (Note 10)	120,711	112,407	1,014,382
Operating income	20,405	15,446	171,472
Other income (expenses):			
Interest and dividends income	1,299	781	10,917
Interest expense	(1,284)	(1,094)	(10,787)
Equity in earnings of affiliates	228	327	1,919
Loss on devaluation of investment securities	(9)	(15)	(77)
Loss on devaluation of real estate for sale and other assets	(137)	(19)	(1,152)
Loss on the move of business establishment	(352)	—	(2,956)
Loss on business restructuring	(663)	—	(5,570)
Loss on retirement allowance by merger	(145)	—	(1,217)
Insurance income	—	419	—
Income on transfer of business by spin-off	—	229	—
Integration costs	—	(455)	—
Other gains, net (Note 9)	1,346	416	11,312
Total	284	589	2,389
Income before income taxes and minority interests	20,689	16,035	173,861
Income taxes (Note 8):			
Current	5,381	2,254	45,219
Deferred	3,180	2,705	26,725
Total	8,561	4,959	71,944
Minority interests	174	235	1,465
Net Income	¥ 11,954	¥ 10,842	\$ 100,452
Per share of common stock:	Yen		U.S. dollars (Note 4)
Net Income (Note 18)	¥ 67.43	¥ 61.28	\$ 0.57
Cash dividends	15.00	13.00	0.13

See accompanying notes to consolidated financial statements.

# CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
For the years ended March 31, 2007 and 2006

	Number of Shares of Common Stock	Millions of yen								
		Common Stock	Capital Surplus	Retained Earnings	Treasury Stock at Cost	Unrealized Gain on Available-for- Sale Securities	Deferred Gains or Losses on Hedges	Foreign Currency Translation Adjustments	Minority Interests	Total Net Assets
Balance as of March 31, 2005	176,603,881	¥ 27,672	¥ 25,654	¥ 90,807	¥ (496)	¥ 9,243	¥ —	¥ (380)	¥ 521	¥ 153,021
Net income		—	—	10,842	—	—	—	—	—	10,842
Changes in unrealized gain on available-for-sale securities, less applicable tax		—	—	—	—	12,882	—	—	—	12,882
Changes in foreign currency translation		—	—	—	—	—	—	1,432	—	1,432
Cash dividends (¥13.00 per share)		—	—	(2,287)	—	—	—	—	—	(2,287)
Bonuses to directors and corporate auditors		—	—	(43)	—	—	—	—	—	(43)
Gain on sale of treasury stock		—	1	—	—	—	—	—	—	1
Treasury stock acquired, net (108,341 shares)		—	—	—	(121)	—	—	—	—	(121)
Other changes		—	—	—	—	—	—	—	2,603	2,603
Balance as of March 31, 2006	176,603,881	¥ 27,672	¥ 25,655	¥ 99,319	¥ (617)	¥ 22,125	¥ —	¥ 1,052	¥ 3,124	¥ 178,330
Cash dividends (¥13.00 per share)		—	—	(2,295)	—	—	—	—	—	(2,295)
Bonuses to directors and corporate auditors		—	—	(59)	—	—	—	—	—	(59)
Net income		—	—	11,954	—	—	—	—	—	11,954
Purchases of treasury stock		—	—	—	(130)	—	—	—	—	(130)
Disposal of treasury stock		—	1	—	5	—	—	—	—	6
Increase or decrease by merger	806,358	—	1,226	—	557	—	—	—	—	1,783
Other changes		—	—	—	—	357	155	752	(1,999)	(735)
Balance as of March 31, 2007	177,410,239	¥ 27,672	¥ 26,882	¥ 108,919	¥ (184)	¥ 22,482	¥ 155	¥ 1,804	¥ 1,125	¥ 188,855

	Thousands of U.S. dollars (Note 4)									
	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock at Cost	Unrealized Gain on Available-for- Sale Securities	Deferred Gains or Losses on Hedges	Foreign Currency Translation Adjustments	Minority Interests	Total Net Assets	
Balance as of March 31, 2006	\$ 232,538	\$ 215,588	\$ 834,614	\$ (5,183)	\$ 185,924	\$ —	\$ 8,840	\$ 26,255	\$ 1,498,576	
Cash dividends (\$0.11 per share)	—	—	(19,289)	—	—	—	—	—	(19,289)	
Bonuses to directors and corporate auditors	—	—	(495)	—	—	—	—	—	(495)	
Net income	—	—	100,452	—	—	—	—	—	100,452	
Purchases of treasury stock	—	—	—	(1,091)	—	—	—	—	(1,091)	
Disposal of treasury stock	—	11	—	40	—	—	—	—	51	
Increase or decrease by merger	—	10,299	—	4,685	—	—	—	—	14,984	
Other changes	—	—	—	—	2,999	1,304	6,320	(16,798)	(6,175)	
Balance as of March 31, 2007	\$ 232,538	\$ 225,898	\$ 915,282	\$ (1,549)	\$ 188,923	\$ 1,304	\$ 15,160	\$ 9,457	\$ 1,587,013	

See accompanying notes to consolidated financial statements.

# CONSOLIDATED STATEMENTS OF CASH FLOWS

Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
For the years ended March 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 4)
	2007	2006	2007
Cash flows from operating activities:			
Income before income taxes and minority interests	¥ 20,689	¥ 16,035	\$ 173,861
Adjustments —			
Depreciation and amortization	6,476	6,403	54,421
Amortization of goodwill	576	566	4,841
Provision for (reversal of) doubtful accounts	(517)	15	(4,343)
Provision for (reversal of) employee's retirement benefits, less payments	(3,495)	(1,044)	(29,373)
Interest and dividend income	(1,299)	(781)	(10,917)
Interest expense	1,284	1,094	10,787
Equity in earnings of affiliates	(228)	(327)	(1,919)
Losses on devaluation of marketable securities and investment securities	9	15	77
Losses (gains) on sales of marketable securities and investment securities, net	(273)	(53)	(2,293)
Losses (gains) on disposal of fixed assets, net	(326)	575	(2,738)
Income on transfer of business by spin-off	—	(229)	—
Change in assets and liabilities:			
Notes and accounts receivable, trade	(23,440)	1,165	(196,971)
Inventories	(10,671)	1,590	(89,674)
Other current assets	(3,672)	(5,051)	(30,861)
Notes and accounts payable, trade	14,188	2,929	119,229
Advances received from customers	6,914	2,067	58,097
Other current liabilities	549	(222)	4,616
Other	878	(261)	7,380
Total	7,642	24,487	64,220
Interest and dividend income received	1,448	1,008	12,169
Interest paid	(1,275)	(1,008)	(10,715)
Income taxes paid, net	(731)	(7,861)	(6,141)
Net cash provided by operating activities	7,084	16,626	59,533
Cash flows from investment activities:			
Proceeds from sales of marketable securities	—	247	—
Decrease (increase) in short-term loans receivable	(445)	801	(3,741)
Payments for purchases of fixed assets	(11,613)	(12,554)	(97,591)
Proceeds from sales of fixed assets	7,676	7,496	64,507
Payments for purchases of intangible assets	(1,586)	(1,872)	(13,329)
Payments for purchases of investment securities	(2,143)	(3,569)	(18,009)
Proceeds from sales of investment securities	1,294	93	10,873
Payments for purchase of stock in subsidiary newly consolidated	—	(1,921)	—
Proceeds from purchase of stock in subsidiary newly consolidated	—	1,316	—
Payments for long-term loans receivable	(186)	(50)	(1,561)
Repayments of long-term loans receivable	106	589	887
Other	(204)	425	(1,715)
Net cash used in investment activities	(7,102)	(8,998)	(59,679)
Cash flows from financing activities:			
Increase (decrease) in short-term borrowings	3,031	(5,770)	25,474
Proceeds from long-term debt	3,632	842	30,517
Repayments of long-term debt	(3,522)	(6,700)	(29,599)
Dividends paid	(2,295)	(2,287)	(19,289)
Other	(180)	(124)	(1,517)
Net cash used in financing activities	665	(14,039)	5,586
Effect of exchange rate changes on cash and cash equivalents	35	111	295
Net increase (decrease) in cash and cash equivalents	682	(6,300)	5,735
Cash and cash equivalents at the beginning of the year	49,628	55,928	417,044
Cash and cash equivalents at the end of the year (Note 11)	¥ 50,311	¥ 49,628	\$ 422,779

See accompanying notes to consolidated financial statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Sumitomo Forestry Co., Ltd. and Consolidated Subsidiaries  
As of March 31, 2007 and 2006

## 1. NATURE OF OPERATIONS

Sumitomo Forestry Co., Ltd. (the “Company”) and its Group companies are involved in various business activities related to wood and houses, with timberland operations serving as the foundation of its business. Specifically, the Company’s operations encompass forest management as well as timber and building materials related operations, including the procurement, manufacture and sale of timber and building materials; housing-related operations, including the construction, sale, after-sales maintenance and landscaping of custom-built and other homes and sale and brokerage of real estate; and other lifestyle related businesses, including the leasing and golf course management.

## 2. BASIS OF PRESENTING CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements of the Company and consolidated subsidiaries (together, the “Companies”) are prepared on the basis of accounting principles generally accepted in Japan (“Japanese GAAP”), which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and are compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan.

On December 27, 2005, the Accounting Standards Board of Japan (the “ASBJ”) published a new accounting standard for the statements of changes in net assets, which is effective for fiscal years ending on or after May 1, 2006. The consolidated statement of net assets, which was previously voluntarily prepared in line with the international accounting practices, is now required under Japanese GAAP and has been renamed “the consolidated statement of changes in net assets” in the current fiscal year.

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The accompanying consolidated financial statements incorporate certain reclassifications and rearrangements in order to present these statements in a form which is more familiar to the readers of these statements outside Japan. In addition, the notes to consolidated financial statements include information which is not required under Japanese GAAP but is presented herein as additional information.

As permitted, amount of less than one million yen are rounded in this annual report.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### (a) Basis of consolidation and investments in affiliates

The consolidated financial statements include the accounts of the Company and, with exceptions that are not material, those of its subsidiaries. All significant intercompany transactions and accounts and unrealized intercompany profits are eliminated on consolidation.

The material difference between the cost and underlying net equity of investments in consolidated subsidiaries is deferred and amortized over a five-year period. Immaterial difference are expensed when incurred.

Investments in affiliates (15 to 50 percent-owned companies except subsidiaries) in which the ability to exercise significant influence exists are stated at cost plus equity in undistributed earnings (losses). Net consolidated income includes the Company’s share of the current net earnings (losses) of such companies, after elimination of unrealized intercompany profits.

### (b) Translation of foreign currency transactions and accounts

Current and long-term receivables and payables in foreign currencies are translated into Japanese yen at the exchange rates at the balance sheet date.

The Company translates the revenue and expense accounts of the foreign consolidated subsidiaries at the average rates of exchange in effect during the year. The balance sheet accounts, except for the components of net assets, are also translated into yen at the rates of exchange in effect at the balance sheet date. The components of net assets are translated at their historical rates.

### (c) Statements of cash flows

Cash and cash equivalents include all highly liquid investments, generally with original maturities of three months or less, that are readily convertible to known amounts of cash and are near enough to maturity that they present only an insignificant risk of changes in value.

### (d) Allowance for doubtful accounts

The allowance for doubtful accounts is stated based on the default ratio sustained over a specific period in the past and the estimated uncollectible amount based on the analysis of certain individual accounts, including probable bad debts and claims in bankruptcy.



This amount is considered sufficient to cover possible losses on collection.

(e) Accrued employees' bonuses

Accrued employees' bonuses are provided based on estimated bonuses to be paid to employees, which are charged to income in the current year.

(f) Warranty reserve for completed construction

A warranty reserve is provided for repair costs which may be required for completed construction. The reserve is estimated based on past experience and future estimates.

The warranty reserve for completed construction is included in other current liabilities.

(g) Accrued employees' retirement benefits

Accrued employees' retirement benefits are provided based on the projected retirement benefit obligation and the plan assets at year-end.

Unrecognized actuarial gains (losses) are amortized in the fiscal year in which they arise.

(h) Accrued retirement benefits to directors and corporate auditors

Accrued retirement benefits to directors and corporate auditors of some subsidiaries are provided based on the amount required for at year-end in accordance with established internal regulations.

(i) Reserve for restructuring costs

The allowance for restructuring costs is stated at the estimated losses on restructuring of discontinued operation and on readjustment of town lots of land, at the end of the fiscal year.

The balance of these reserves at March 31, 2007, which were included in other current liabilities and other long-term liabilities in the accompanying consolidated balance sheets, were ¥9 million (US\$76 thousand) and ¥888 million (US\$7,459 thousand).

(j) Presentation of net assets

On December 9, 2005, the ASBJ published a new accounting standard for presentation of net assets. Under this accounting standard, certain items which were previously presented as liabilities are now presented as components of net assets. Such items include stock acquisition rights, minority interests, and any deferred gain or loss on derivatives accounted for under hedge accounting. This standard is effective for fiscal years ending on or after May 1, 2006. The consolidated balance sheet as of March 31, 2007 is presented in line with this new accounting standard.

(k) Marketable securities and investments

Marketable securities and investments are classified and accounted for, depending on management's intent, as follows: i) held-to-maturity debt securities, which are expected to be held to maturity with the positive intent and ability to hold to maturity, are reported at amortized cost; and ii) available-for-sale securities, which are not classified as the aforementioned securities, are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of net assets.

The Company determines cost of securities sold by the moving average method.

(l) Inventories

Inventories other than finished goods are stated at cost, which is determined by the specific identification method.

Finished goods are stated at moving average cost.

(m) Property, plant and equipment

Property, plant and equipment, including significant renewals and additions, are capitalized at cost. Maintenance, repairs, minor renewals and improvements are charged to income. Depreciation is computed, with minor exceptions, by the declining balance method at rates based on the estimated useful lives of the assets according to general class, type of construction and use. In the case of retirement or disposal, the difference between the net book value and salvage or sales proceeds is charged or credited to income.

(n) Timberland

Timberland consists of standing timber and related land. Standing timber, consisting of timber stock in natural forests, purchased forests and planted forests, is classified either as mature timber or growing timber. Mature timber represents costs related to trees that are 21 or more years old, of which costs have been transferred from growing timber. Growing timber represents costs of trees less than 21 years old (see Note 6).

The timber stock from both natural forests and purchased forests is carried at the specific acquisition cost.

The timber stock from planted forests is stated at cost, which consists of sowing, seeding and planting.

Intensive forest management generally practiced in Japan results in high yields of quality logs. Such management, implemented by the Company, includes the following procedures:

Age in Years	Procedures
0	Sowing, seeding at nursery
1	Planting after land preparation
1-6	Weeding
8	Vine cutting
10-14	Salvage cutting
14	Pruning
16-25	Thinning and debranching
Over 50	Final cutting

The charges for weeding, vine cutting, salvage cutting, pruning and thinning and debranching are charged to selling, general and administrative expenses as incurred.

When finally harvested from timberland for sale, the harvested timber has its cost calculated based on the proportion of metric volume of the timber harvested to that of the particular area, applied to the book value of the area. The calculated cost is the cost of sales.

#### (o) Revenue recognition

Sales are generally recognized at the time the goods are delivered to the customers.

Sales of precut timber, building materials and certain housing equipment, such as system kitchens, system furniture, bathtubs, sinks and other, which are purchased by the Company and sold to building contractors for use in house building projects specifically subcontracted from the Company, are recognized upon completion and acceptance of the completed houses by the customers, with the related cost being included in cost of contracts completed.

Contract revenues, representing revenues from custombuilt houses, are recorded when the completed houses are accepted by customers.

#### (p) Finance leases

Finance leases of the Companies, other than those where ownership of the lease assets is transferred to the lessee, are accounted for as operating leases.

#### (q) Bonuses to directors and corporate auditors

On November 29, 2005, the ASBJ replaced an accounting standard for bonuses to directors and corporate auditors. Under the new accounting standard, bonuses to directors and corporate auditors must be expensed and are no longer allowed to be directly charged

to retained earnings. This accounting standard is effective for fiscal years ending on or after May 1, 2006. Companies must accrue bonuses to directors and corporate auditors at the year end to which such bonuses are attributable.

The company and certain consolidated subsidiaries adopted this new accounting standard beginning in the year ended March 31, 2007. The effect was to decrease income before income taxes and minority interests for the year ended March 31, 2007 by ¥83 million (\$698 thousand).

#### (r) Income taxes

The Companies accrue income taxes based on taxable income. The Companies include many items for financial reporting purposes which, in the case of expenses, are not currently deductible and, in the case of income, are not currently taxable.

Income taxes based on temporary differences between tax and financial reporting purposes are reflected as deferred income taxes in the consolidated financial statements using the asset and liability method.

#### (s) Appropriations of retained earnings

Appropriations of retained earnings reflected in the accompanying consolidated financial statements are recorded upon approval by shareholders as required under Japanese law.

#### (t) Earnings per share of common stock

The computation of net income and cash dividends per share is based on the average number of shares outstanding during each period.

#### (u) Reclassifications

Certain accounts in the consolidated financial statements for the year ended March 31, 2006 have been reclassified to conform to presentation in 2007.

## 4. U.S. DOLLAR AMOUNTS

The U.S. dollar amounts are included solely for convenience and have been translated, as a matter of arithmetical computation only, at the rate of ¥119=US\$1, the approximate exchange rate prevailing in the Japanese foreign exchange market at March 31, 2007. This translation should not be construed as a representation that the yen amounts actually represent, or have been or could be converted into, U.S. dollars.

## 5. SECURITIES

The carrying amount and aggregate fair value of the securities classified as available-for-sale and held-to-maturity at March 31, 2007 and 2006 were as follows:

	Millions of yen			
	2007			
	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Securities classified as:				
Available-for-sale:				
Equity securities	¥ 31,715	¥ 37,397	¥ (1,069)	¥ 68,043
Debt securities	—	—	—	—
Held-to-maturity:				
Debt securities	¥ 3,397	—	—	¥ 3,397

	Millions of yen			
	2006			
	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Securities classified as:				
Available-for-sale:				
Equity securities	¥ 26,053	¥ 41,718	¥ (92)	¥ 67,679
Debt securities	—	—	—	—
Held-to-maturity:				
Debt securities	¥ 5,290	¥ —	¥ —	¥ 5,290

	Thousands of U.S. dollars			
	2007			
	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Securities classified as:				
Available-for-sale:				
Equity securities	\$ 266,514	\$ 314,258	\$ (8,983)	\$ 571,789
Debt securities	—	—	—	—
Held-to-maturity:				
Debt securities	\$ 28,548	—	—	\$ 28,548

Proceeds from sales of available-for-sale securities and the corresponding gross gains and losses, which are included in other gains (losses), net in the accompanying consolidated statements of income for the year ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Proceeds	¥ 1,294	¥ 93	\$ 10,873
Gross gains	273	53	2,297
Gross losses	—	—	—

The carrying values of debt securities by contractual maturities for securities classified as available-for-sale and held-to-maturity at March 31, 2007 were as follows:

	Millions of yen		Thousands of U.S. dollars	
	2007			
	Available-for-Sale	Held-to-Maturity	Available-for-Sale	Held-to-Maturity
Due within one year	—	¥ 3,000	—	\$ 25,208
Due after one year				
through five years	—	291	—	2,449
Due after five years				
through ten years	—	106	—	891
	—	¥ 3,397	—	\$ 28,548

The difference between the above cost and the amounts shown in the accompanying consolidated balance sheets principally consisted of non-marketable securities and equity securities of unconsolidated subsidiaries and affiliates.

## 6. TIMBERLAND

The investment in timberland at March 31, 2007 and 2006 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Standing timber:			
Mature timber	¥ 10,401	¥ 10,723	\$ 87,400
Growing timber	340	413	2,857
	10,741	11,136	90,257
Land	477	477	4,006
	¥ 11,217	¥ 11,613	\$ 94,263

The timberland accounts at March 31, 2007 and 2006 were reduced by ¥268 million (US \$2,255 thousand) and ¥268 million in aggregate, representing the accumulated deferred gains from disposals of timberland.

## 7. SHORT-TERM AND LONG-TERM DEBT

Short-term debt at March 31, 2007 and 2006 generally represented short-term borrowings which bore interest of 4.76% and 4.37% per annum, respectively. Long-term debt at March 31, 2007 and 2006 were summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Loans, principally from banks and insurance companies, due 2008 to 2012 with interest of 6.09%:			
Secured	¥ 3,220	¥ 7,560	\$ 27,055
Unsecured	8,004	3,181	67,265
Debenture bonds:			
0.35 basis points	60	120	504
0.64 basis points	100	100	840
	11,384	10,961	95,664
Portion due within one year	2,621	2,113	22,024
	¥ 8,763	¥ 8,848	\$ 73,640

The following assets were pledged to secure bank loans and long-term debt at March 31, 2007 and 2006:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Receivables-			
Notes and accounts, trade	¥ 457	¥ 523	\$ 3,844
Finished goods, logs and lumber	1,407	1,246	11,823
Land	334	269	2,805
Buildings and structures	3,774	3,765	31,713
Machinery and equipment	9,614	8,141	80,790
Timberland	2,000	2,309	16,806
Investment securities	—	3,344	—
Other	—	27	—
	¥ 17,586	¥ 19,624	\$ 147,781

The aggregate annual maturities of long-term debt at March 31, 2007 were as follows:

YEARS ENDING MARCH 31	Millions of yen	Thousands of U.S. dollars
2008	¥ 2,621	\$ 22,025
2009	5,340	44,871
2010	251	2,106
2011	194	1,629
2012	2,037	17,119
Thereafter	942	7,914
	¥ 11,384	\$ 95,664

## 8. INCOME TAXES

Income taxes in Japan applicable to the Companies generally comprise Corporation Tax, Enterprise Tax and Prefectural and Municipal Inhabitants Taxes. The effective statutory tax rate for fiscal 2007 was 40.0%.

The chart below shows the differences in the statutory tax rate and effective income tax rate.

	2007	2006
Statutory tax rate	—	40.0%
Non-deductible expense for purposes	—	1.5
Per capita portion of Inhabitant Tax	—	1.6
Amortization of consolidation differences	—	1.4
Valuation allowance	—	(14.5)
Other	—	0.9
	—	30.9%

For the year ended March 31, 2007, the difference is not disclosed because the difference is less than 5% of the normal effective statutory tax rate.



The significant components of deferred tax assets and liabilities at March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Deferred tax assets:			
Accrued employees' bonuses	¥ 3,691	¥ 3,484	\$ 31,020
Devaluation of real estate for sale and other assets	4,019	4,160	33,771
Pension and severance costs	4,870	6,293	40,924
Tax loss carryforwards	984	3,186	8,270
Impairment loss	1,397	1,693	11,738
Other	5,289	4,622	44,448
Gross deferred tax assets	20,250	23,438	170,171
Valuation allowance	(8,471)	(8,802)	(71,183)
Total deferred tax assets	11,780	14,636	98,988
Deferred tax liabilities:			
Deferred gains on sales of property	(1,033)	(966)	(8,681)
Gain on securities contributed to employee retirement benefit trusts	(1,590)	(1,590)	(13,365)
Unrealized gain on available-for-sale securities	(13,615)	(16,604)	(114,410)
Land revaluation differences	(1,309)	(1,230)	(11,001)
Other	(2,412)	(543)	(20,268)
Gross deferred tax liabilities	(19,959)	(20,933)	(167,725)
Net deferred tax assets	¥ (8,180)	¥ (6,297)	\$ (68,737)

Net deferred tax assets were included in the consolidated balance sheets at March 31, 2007 and 2006 as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Current assets-			
Deferred income taxes	¥ 6,179	¥ 7,597	\$ 51,923
Investment and other assets-			
Deferred income taxes	1,101	1,242	9,248
Current liabilities-			
Other	(59)	(0)	(495)
Long-term liabilities-			
Deferred income taxes	(15,400)	(15,136)	(129,413)
Net deferred tax assets	¥ (8,180)	¥ (6,297)	\$ (68,737)

## 9. OTHER GAINS (LOSSES), NET

Other gains (losses), net, for the years ended March 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Gain on sales of property, plant and equipment	¥ 696	¥ 82	\$ 5,848
Gain on sales of investment securities	273	53	2,293
Loss on sales of property, plant and equipment	(168)	(492)	(1,410)
Loss on disposal of property, plant and equipment	(202)	(165)	(1,700)
Other, net	747	939	6,281
	¥ 1,346	¥ 416	\$ 11,312

## 10. RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses charged to selling, general and administrative expenses for the year ended March 31, 2007 and 2006 were ¥912 million (US \$7,663 thousand) and ¥993 million, respectively.

## 11. CASH AND CASH EQUIVALENTS

Cash and cash equivalents at March 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Cash and time deposits	¥ 47,385	¥ 44,720	\$ 398,194
Short-term investments	3,000	5,000	25,208
Less: Cash deposits and short-term investments which mature or become due over three months after the date of acquisition	(74)	(92)	(623)
Cash and cash equivalents	¥ 50,311	¥ 49,628	\$ 422,779

## 12. SHAREHOLDERS' EQUITY

On and after May 1, 2006, Japanese companies are subject to a new corporation law of Japan (the "Company Law"), which reformed and replaced part of the Commercial Code of Japan (the "Code").

The Company Law provides that an amount equivalent to 10% of cash dividends must be appropriate as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus) depending on the equity account charged upon the payment of such dividends. Legal reserve and additional paid-in capital may be reversed without limitation and no further appropriation is required when the sum of legal reserve and additional paid-in capital equals 25% of the common stock.

The Company Law also provides that the common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts under certain conditions upon resolution of shareholders.

The balance of the legal reserve of the Company at March 31, 2007 and 2006, which were included in retained earnings in the accompanying consolidated balance sheets, were ¥2,857 million (US\$24,009 thousand) and ¥2,857 million, respectively.

Year-end dividends are approved by shareholders at a meeting held subsequent to the fiscal year to which the dividends are applicable. In addition, semi-annual interim dividends may be paid upon resolution of Board of Directors, subject to limitations imposed by the Company Law.

## 13. FINANCE LEASES

(Lessee)

Finance leased charges to the Companies for the years ended March 31, 2007 and 2006 were ¥4,618 million (US \$38,810 thousand) and ¥4,366 million, respectively.

The leased assets and related expenses of the Companies' finance leases, other than those where the ownership of the lease assets is transferred to the lessee, are being accounted for as operating leases. If capitalized, the following amounts would be recorded in the financial statements (in equivalent amounts):

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Buildings and structures	¥ 11,894	¥ 11,318	\$ 99,948
Machinery and equipment	6,334	5,823	53,230
Other	171	188	1,436
Accumulated depreciation	(8,028)	(7,898)	(67,465)
Accumulated impairment loss	(4)	(4)	(35)
	¥ 10,367	¥ 9,427	\$ 87,114

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Depreciation	¥ 4,466	¥ 4,224	\$ 37,533
Interest expenses	152	142	1,277

Depreciation costs are calculated based on the straightline method over the lease periods of the leased assets, with no residual value of the assets at the end of the lease periods.

Interest expenses are calculated by subtracting the amount equivalent to the acquisition cost from the total lease fee. The resulting differences, which are of an amount equivalent to the total interest payments over the lease periods, are allocated to each period by the interest method. The present values of future lease payments of the Companies as at March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Current obligation	¥ 4,091	¥ 3,768	\$ 34,378
Long-term obligation	6,380	5,754	53,614
Present value of lease payments	¥ 10,471	¥ 9,522	\$ 87,992
Impairment loss on leased assets	¥ 1	¥ 2	\$ 9

(Lessor)

Finance lease fee income of the Companies credited to income for the years ended March 31, 2007 and 2006 were ¥118 million (US \$989 thousand) and ¥131 million, respectively. The leased assets and related expenses of the Companies' finance leases other than those where the ownership of the leased assets is transferred to the lessee and are being accounted for as operating leases at March 31, 2007 and 2006 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Machinery and equipment	¥ 466	¥ 469	\$ 3,917
Other	25	36	214
Accumulated depreciation	(235)	(249)	(1,978)
	¥ 256	¥ 257	\$ 2,153

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Depreciation	¥ 104	¥ 111	\$ 873
Interest expenses	14	16	116

Interest income is calculated by subtracting the amount equivalent to the acquisition cost from the total lease fee. The resulting differences, which are of an amount equivalent to the total interest receipts over the lease periods, are allocated to each period by the interest method. The present values of future lease receipts for the Companies at March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Current obligation	¥ 86	¥ 87	\$ 721
Long-term obligation	166	167	1,393
Present value of lease receipts	¥ 252	¥ 253	\$ 2,114

## 14. CONTINGENT LIABILITIES

Contingent liabilities as at March 31, 2007 and 2006, for loans guaranteed amounted to ¥21,800 million (US \$183,189 thousand) and ¥20,880 million, and for notes discounted and endorsed in the ordinary course of business amounted to ¥159 million (US \$1,336 thousand) and ¥363 million, respectively.

## 15. DERIVATIVES AND HEDGING ACTIVITIES

The Companies use derivative financial instruments to manage their exposure to fluctuations in foreign exchange and interest rates. Foreign exchange forward contracts, foreign currency swaps, and interest rate swaps are utilized by the Companies to reduce foreign currency exchange and interest rate risks. The Companies do not enter into derivatives for trading or speculative purposes.

## 16. EMPLOYEE'S RETIREMENT BENEFITS AND PENSION PLANS

The Company and some of its consolidated subsidiaries offer their employees both a lump-sum benefit at retirement and a non-contributory funded defined benefit pension plan. Others offer a lump-sum benefit at retirement only.

These systems are open to employees who meet set conditions, but substantially all employees are eligible.

Retirement benefits are calculated based on the employees basic rate of pay, length of service, termination circumstance and other factors. The employees of the companies that adopt defined-benefit pension plan may opt for either a lump-sum payment or annuity payments.

The liability for employee's retirement benefits at March 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Projected benefit obligation	¥ (49,376)	¥ (48,162)	\$ (414,921)
Fair value of plan assets	36,992	32,286	310,860
Unrecognized actuarial loss	—	—	—
Unrecognized prior service cost	—	—	—
Prepaid pension cost	—	—	—
Net liability for retirement benefits	¥ (12,383)	¥ (15,875)	\$ (104,061)

The components of net periodic benefit costs for the year ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Service cost	¥ 3,140	¥ 2,930	\$ 26,384
Interest cost	863	830	7,255
Expected return on plan assets	(1,156)	(167)	(9,714)
Recognized actuarial loss	(1,899)	(2,973)	(15,958)
Amortization of prior service cost	—	—	—
Net periodic benefit costs	¥ 948	¥ 619	\$ 7,967

Certain consolidated subsidiaries have adopted the conventional method in calculating their projected benefit obligation.

Assumptions used for the year ended March 31, 2007 and 2006 were set forth as follows:

	2007	2006
Discount rate	2.0%	1.9%
Expected rate of return on plan assets	3.7%	0.7%
Recognition period of actuarial gain/loss	1 year	1 year



## 17. SEGMENT INFORMATION

## a) Industry segment information—

The Companies' business is classified into the following three segments based on the similarities of the types and nature of business:

Timber and building materials: manufacturing or purchasing and sale of timber and building materials

Housing: construction of houses, buildings and their exteriors, gardening, planting, sale of interiors and brokerage of real estate

Other: leasing, golf course management and other

The tables below present sales, operating expenses and operating income information by segment.

YEAR ENDED MARCH 31, 2007	Millions of yen					
	Timber and Building Materials	Housing	Other	Total	Elimination and / or Corporate	Consolidated
Sales and contract revenues:						
Unaffiliated customers	¥ 500,843	¥ 407,187	¥ 3,643	¥ 911,674	¥ —	¥ 911,674
Intersegment transfers	19,259	593	10,954	30,806	(30,806)	—
Total	520,103	407,780	14,597	942,480	(30,806)	911,674
Operating expenses	512,136	391,194	13,694	917,024	(25,755)	891,269
Operating income	¥ 7,967	¥ 16,586	¥ 903	¥ 25,456	¥ (5,051)	¥ 20,405
Identifiable assets, depreciation and capital investment:						
Identifiable assets	¥ 269,610	¥ 113,276	¥ 9,067	¥ 391,954	¥ 108,182	¥ 500,136
Depreciation and amortization	3,003	2,332	751	6,085	391	6,476
Capital investment	5,281	3,481	811	9,573	(546)	9,026

YEAR ENDED MARCH 31, 2006	Millions of yen					
	Timber and Building Materials	Housing	Other	Total	Elimination and / or Corporate	Consolidated
Sales and contract revenues:						
Unaffiliated customers	¥ 395,650	¥ 392,131	¥ 3,347	¥ 791,128	¥ —	¥ 791,128
Intersegment transfers	16,532	1,737	10,202	28,471	(28,471)	—
Total	412,182	393,868	13,549	819,600	(28,471)	791,128
Operating expenses	409,376	377,498	12,708	799,582	(23,900)	775,682
Operating income	¥ 2,806	¥ 16,370	¥ 841	¥ 20,018	¥ (4,571)	¥ 15,446
Identifiable assets, depreciation and capital investment:						
Identifiable assets	¥ 237,265	¥ 105,579	¥ 9,139	¥ 351,982	¥ 112,210	¥ 464,193
Depreciation and amortization	2,906	2,336	686	5,928	475	6,403
Capital investment	5,701	3,737	980	10,418	25	10,443

YEAR ENDED MARCH 31, 2007	Thousands of U.S. dollars					
	Timber and Building Materials	Housing	Other	Total	Elimination and / or Corporate	Consolidated
Sales and contract revenues:						
Unaffiliated customers	\$ 4,208,769	\$ 3,421,743	\$ 30,617	\$ 7,661,129	\$ —	\$ 7,661,129
Intersegment transfers	161,842	4,983	92,049	258,874	(258,874)	—
Total	4,370,611	3,426,726	122,666	7,920,003	(258,874)	7,661,129
Operating expenses	4,303,663	3,287,346	115,078	7,706,087	(216,430)	7,489,657
Operating income	\$ 66,948	\$ 139,380	\$ 7,588	\$ 213,916	\$ (42,444)	\$ 171,472
Identifiable assets, depreciation and capital investment:						
Identifiable assets	\$ 2,265,629	\$ 951,903	\$ 76,197	\$ 3,293,729	\$ 909,093	\$ 4,202,822
Depreciation and amortization	25,236	19,595	6,307	51,138	3,283	54,421
Capital investment	44,381	29,249	6,813	80,443	(4,591)	75,852

Notes: (Year ended March 31, 2007)

As stated in Note 3 (q), the accounting standard for bonuses to directors and corporate auditors (Principle 4 of the Business Accounting Standards-November 29, 2005) can be applied to consolidated financial statements from the fiscal year that ended on or after May 1, 2006. This accounting standard was applied during the fiscal year. The effect of this change on the segment information was to increase operating expenses and to decrease operating income in the "Elimination and/or Corporate" category by ¥83 million (\$698 thousand).

b) Geographical segment information—

The Companies' business is classified into two segments based on geographic proximity. Other includes Asia, North America and Oceania.

YEAR ENDED MARCH 31, 2007	Millions of yen				
	Domestic	Other	Total	Elimination and / or Corporate	Consolidated
Sales and contract revenues:					
Unaffiliated customers	¥ 891,289	¥ 20,386	¥ 911,674	—	¥ 911,674
Intersegment transfers	2,454	9,945	12,399	(12,399)	—
Total	893,743	30,330	924,073	(12,399)	911,674
Operating expenses	869,954	28,904	898,858	(7,589)	891,269
Operating income	¥ 23,788	¥ 1,427	¥ 25,215	¥ (4,810)	20,405
Identifiable assets, depreciation and capital investment:					
Identifiable assets	¥ 354,837	¥ 41,420	¥ 396,257	¥ 103,879	¥ 500,136

YEAR ENDED MARCH 31, 2006	Millions of yen				
	Domestic	Other	Total	Elimination and / or Corporate	Consolidated
Sales and contract revenues:					
Unaffiliated customers	¥ 773,221	¥ 17,907	¥ 791,128	¥ —	¥ 791,128
Intersegment transfers	2,276	8,005	10,280	(10,280)	—
Total	775,497	25,912	801,409	(10,280)	791,128
Operating expenses	755,595	25,960	781,556	(5,874)	775,682
Operating income	19,901	(48)	19,853	(4,407)	15,446
Identifiable assets, depreciation and capital investment:					
Identifiable assets	¥ 318,973	¥ 38,212	¥ 357,184	¥ 107,008	¥ 464,193

YEAR ENDED MARCH 31, 2007	Thousands of U.S. dollars				
	Domestic	Other	Total	Elimination and / or Corporate	Consolidated
Sales and contract revenues:					
Unaffiliated customers	\$ 7,489,822	\$ 171,307	\$ 7,661,129	\$ —	\$ 7,661,129
Intersegment transfers	20,620	83,570	104,190	(104,190)	—
Total	7,510,442	254,877	7,765,319	(104,190)	7,661,129
Operating expenses	7,310,541	242,887	7,553,428	(63,771)	7,489,657
Operating income	\$ 199,901	\$ 11,990	\$ 211,891	\$ (40,419)	171,472
Identifiable assets, depreciation and capital investment:					
Identifiable assets	\$ 2,981,827	\$ 348,063	\$ 3,329,890	\$ 872,932	\$ 4,202,822

Notes: (Year ended March 31, 2007)

As stated in Note 3 (q), the accounting standard for bonuses to directors and corporate auditors (Principle 4 of the Business Accounting Standards-November 29, 2005) can be applied to consolidated financial statements from the fiscal year that ended on or after May 1, 2006. This accounting standard was applied during the current fiscal year. The effect of this change on segment information was to increase operating expenses and to decrease operating income in the "Elimination and/or Corporate" category by ¥83 million (\$698 thousand).

#### c) Overseas sales information—

As the total overseas sales were less than 10% of consolidated net sales, overseas sales information has been omitted.

## 18. NET INCOME PER SHARE

The computation of net income per share for the year ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Numerator for net income per share:			
Net Income	¥ 11,954	¥ 10,842	\$ 100,452
Income not available to common stockholders	—	(62)	—
Income available to common stockholders	11,954	10,779	100,452
Denominator for net income per share:			
Weighted average number of shares issued	177,287,939	175,891,228	

# REPORT OF INDEPENDENT AUDITORS



## Report of Independent Auditors

The Board of Directors  
Sumitomo Forestry Co., Ltd.

We have audited the accompanying consolidated balance sheets of Sumitomo Forestry Co., Ltd. (the “Company”) and consolidated subsidiaries as of March 31, 2007 and 2006, and the related consolidated statements of income, changes in net assets, and cash flows for the years then ended, all expressed in yen. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Sumitomo Forestry Co., Ltd. and consolidated subsidiaries at March 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

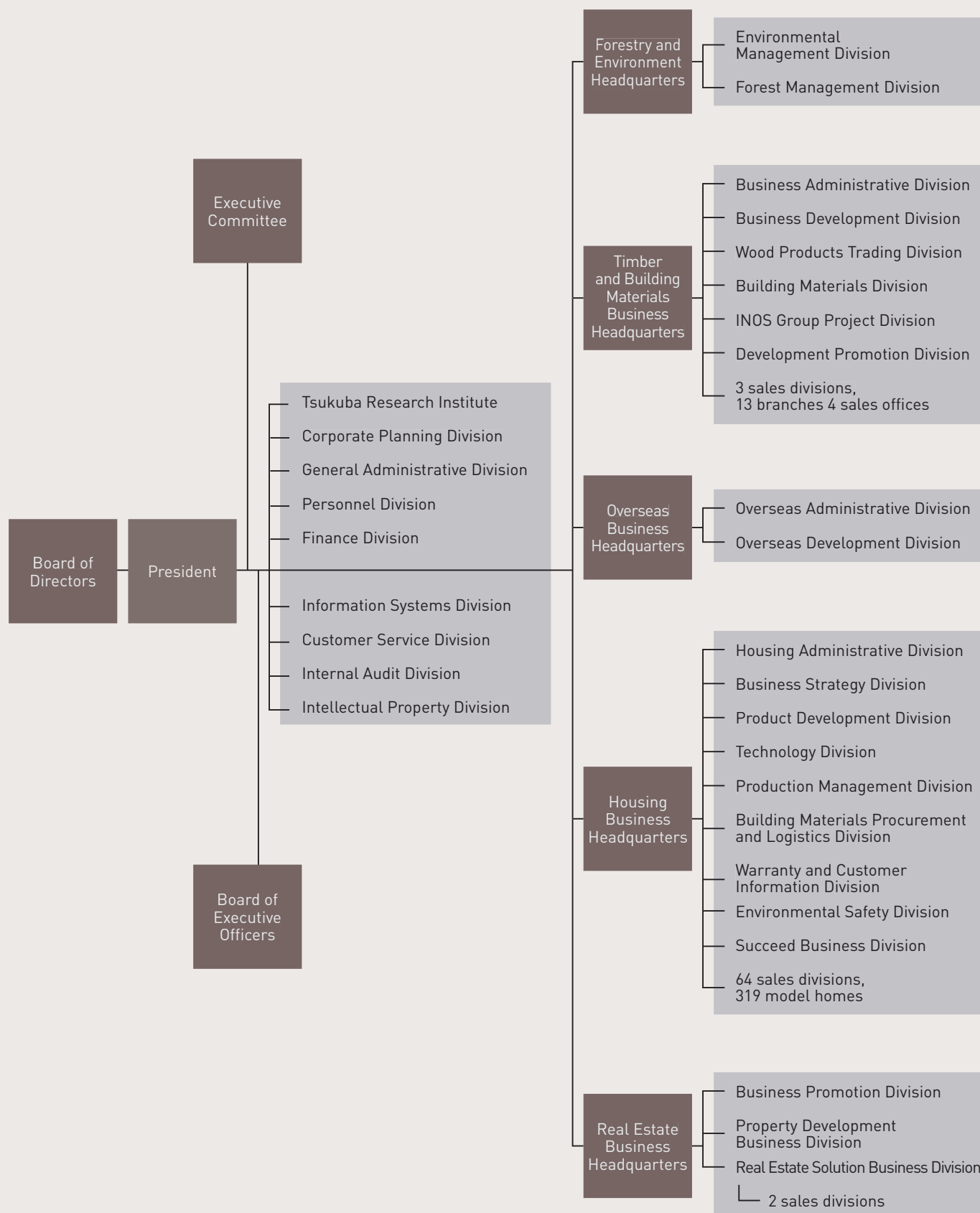
The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2007 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 4.

June 22, 2007

*Ernst & Young Shin Nihon*



# ORGANIZATION CHART



[As of April 1, 2007]

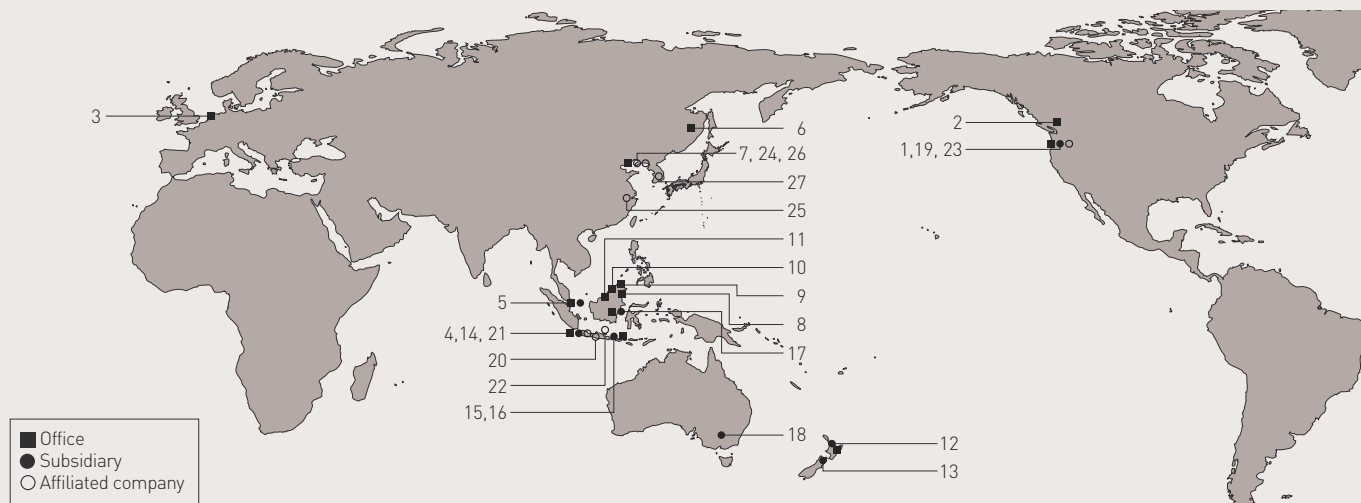
# OVERSEAS NETWORK

## OVERSEAS OFFICES AND SUBSIDIARIES

1. Seattle Office/Sumitomo Forestry Seattle, Inc.  
11235 SE 6th Street, Suite 120, Bellevue, Washington 98004, U.S.A.  
Tel: 1-425-454-2355  
Fax: 1-425-454-1106  
E-mail: sfs@sumiforsea.com
2. Vancouver Office  
460, 1140 West Pender Street, Vancouver, British Columbia, Canada, V6E 4G1  
Tel: 1-604-681-8184  
Fax: 1-604-681-6568  
E-mail: sfc1@sfcver.com
3. Amsterdam Office  
Rivierstaete Building, 3rd Floor No. 22, Amsteldijk 166 1079LH, Amsterdam, The Netherlands  
Tel: 31-20-646-4140  
Fax: 31-20-646-5372  
E-mail: sfc3@smtforams.nl
4. Jakarta Office  
Summitmas II, 8th Floor, Jl. Jend. Sudirman Kav. 61-62, Jakarta 12190, Indonesia  
Tel: 62-21-5200268  
Fax: 62-21-5202069  
E-mail: sfcjkt@cbn.net.id
5. Singapore Office/Sumitomo Forestry (Singapore) Ltd.  
6 Raffles Quay #14-04/05, John Hancock Tower, Singapore 048580  
Tel: 65-6435-0150  
Fax: 65-6435-0151  
E-mail: adm@sfspsore.com.sg
6. Khabarovsk Office  
Room 1007, Hotel Intourist, 2, Amurskiy Blud, Khabarovsk, 68000, Russia  
Tel: 7-4212-41-33-60  
Fax: 7-4212-41-33-62  
E-mail: sfc@sovintel.ru
7. Dalian Office/Sumitomo Forestry (Dalian) Ltd.  
Senmao Building, 11th Floor, 147 Zhongshan Road, Xigang District, Dalian, 116011, PRC  
Tel: 86-411-8367-8060/8062  
Fax: 86-411-8367-8061  
E-mail: dalian@sfc-cn.com
8. Tawau Office  
TB3473, 6th Floor, Wisma Indotani, Jalan Masjid, Tawau, Sabah, Malaysia  
Tel: 60-89-772979  
Fax: 60-89-761060
9. Kota Kinabalu Office  
Suite 1, 8th Floor, Wisma Perindustrian, Jalan Istiadat, Likas, 88400 Kota Kinabalu, Sabah, Malaysia  
Tel: 60-88-242031  
Fax: 60-88-268031  
E-mail: sfc2wu@tm.net.my
10. Miri Office  
P. O. Box. 493, 98007, Lot 231 No.15, Hokkien Road, Miri, Sarawak, Malaysia  
Tel: 60-85-413459  
Fax: 60-85-413598  
E-mail: sfcmiri@tm.net.my
11. Sibu Office  
P. O. Box. 1563, 96008, No. 11, 2nd Floor, Lane 1, Jalan Rakyat, Sibu, Sarawak, Malaysia  
Tel: 60-84-312777  
Fax: 60-84-317635
12. Auckland Office/Sumitomo Forestry NZ Limited  
P. O. Box. 91219, Auckland Mail Centre, Level 11, Rifleman Tower 120 Albert Street, Auckland, New Zealand  
Tel: 64-9-309-0012  
Fax: 64-9-309-0014  
E-mail: sfnz@xtra.co.nz/
13. Nelson Pine Industries Ltd.  
P. O. Box. 3049, Lower Queen Street, Richmond, Nelson, New Zealand  
Tel: 64-3543-8800  
Fax: 64-3543-8890  
E-mail: sfc@nelsonpine.co.nz
14. PT. Kutai Timber Indonesia  
P. O. Box. 6913/JKSST, Summitmas II, 8th Floor, Jl. Jend. Sudirman Kav. 61-62, Jakarta 12190, Indonesia  
Tel: 62-21-2521260  
Fax: 62-21-5200313  
E-mail: ktijkt@cbn.net.id
15. Probolinggo Factory  
P. O. Box. 101 Probolinggo, Jl. Tanjung Tembaga Baru, Pelabuhan, Probolinggo, Jawa Timur, Indonesia  
Tel: 62-335-42-2412  
Fax: 62-335-42-1669  
E-mail: pr@kti.co.id
16. Surabaya Branch  
P. O. Box. 306, Surabaya, Jl. Kusuma Bangsa No. 19, Surabaya 60272, Jawa Timur, Indonesia  
Tel: 62-31-5343835  
Fax: 62-31-5343838  
E-mail: ktisby@kti.co.id
17. Samarinda Branch  
Jl. Manggis Mo. 48/40 Samarinda 75123, Kalimantan Timur, Indonesia  
Tel: 62-541-741966/737926/748116  
Fax: 62-541-741967
18. Alpine MDF Industries Pty Ltd.  
Lot-1 Crosher Lane, Wangaratta VIC 3677, Australia  
Tel: 61-3-5721-3522  
Fax: 61-3-5721-3588  
Email: enquiries@alpinemdf.com.au
19. Pacific Wood Products LLC.  
16310 NE 85th Street, Suite 100, Redmond, Washington 98052, U.S.A.  
Tel: 1-425-885-1777  
Fax: 1-425-885-0057  
E-mail: sfs@sumiforsea.com

## AFFILIATES

20. PT. Rimba Partikel Indonesia  
P. O. Box. 127 KENDAL  
Desa. Mororejo, Kaliwungu, Kendal, Jawa Tengah, Indonesia  
Tel: 62-24-8662990  
Fax: 62-24-8662988/8662993  
E-mail: rpirsg@indosat.net.id
21. Jakarta Office  
Gedung Idola Tunggal Slipi, Jl. Letjen S.Parmar Kav.67, Jakarta 11410, Indonesia  
Tel: 62-21-5321637  
Fax: 62-21-5301313  
E-mail: rimbajkt@cbn.net.id
22. PT. AST Indonesia  
KITW Technopark Blok A-01, Jl. Raya Semarang-Kendal Km.12, Semarang, Indonesia  
Tel: 62-24-8664800  
Fax: 62-24-8664801  
E-mail: asti@ast.co.id
23. Bennett-SFS LLC.  
c/o Sumitomo Forestry Seattle, Inc. 11235 SE 6th Street, Suite 120, Bellevue, Washington 98004, U.S.A.  
Tel: 1-425-454-2355  
Fax: 1-425-454-1106  
E-mail: sfs@sumiforsea.com
24. Paragon Wood Product (Dalian) Co., Ltd.  
Rm 417, International Trade Center, #3 Haitian Road, Free Trade Zone, Dalian, 116600, PRC  
Tel: 86-411-87332208/87332218  
Fax: 86-411-87332318  
E-mail: paragonkenji@aol.com
25. Paragon Wood Product (Shanghai) Co., Ltd.  
D 902, 9th Floor, Pufa Plaza Building D, 1759 North Zhongshan Shanghai, 200061, PRC  
Tel: 86-21-61405828  
Fax: 86-21-61405826  
E-mail: paragonkenji@aol.com
26. Dalian Sumirin Information Technology Service Co., Ltd.  
Senmao Building 16th Floor, 147 Zhongshan Road, Xigang District, Dalian, 116011, PRC  
Tel: 86-411-8365-8755/8757  
Fax: 86-411-8365-8756  
E-mail: sfdln@sfits-cn.com
27. Dongwha SFC Housing Co., Ltd.  
Dongwha Bldg. 192-4, Nonhyeon-Dong, Gangnam-Gu, Seoul, 135-010, Korea  
Tel: 86-2-3218-8970  
Fax: 82-2-3445-2891

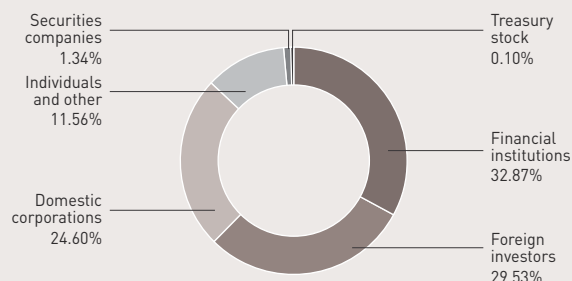


[As of September, 2007]

# STOCK INFORMATION

Stock Exchange Listings:	Tokyo, Osaka
Common Stock Authorized:	400,000,000 shares
Issued:	177,410,239 shares
Number of Shareholders:	11,012
General Meeting of Shareholders:	June

## Breakdown of Shareholders:



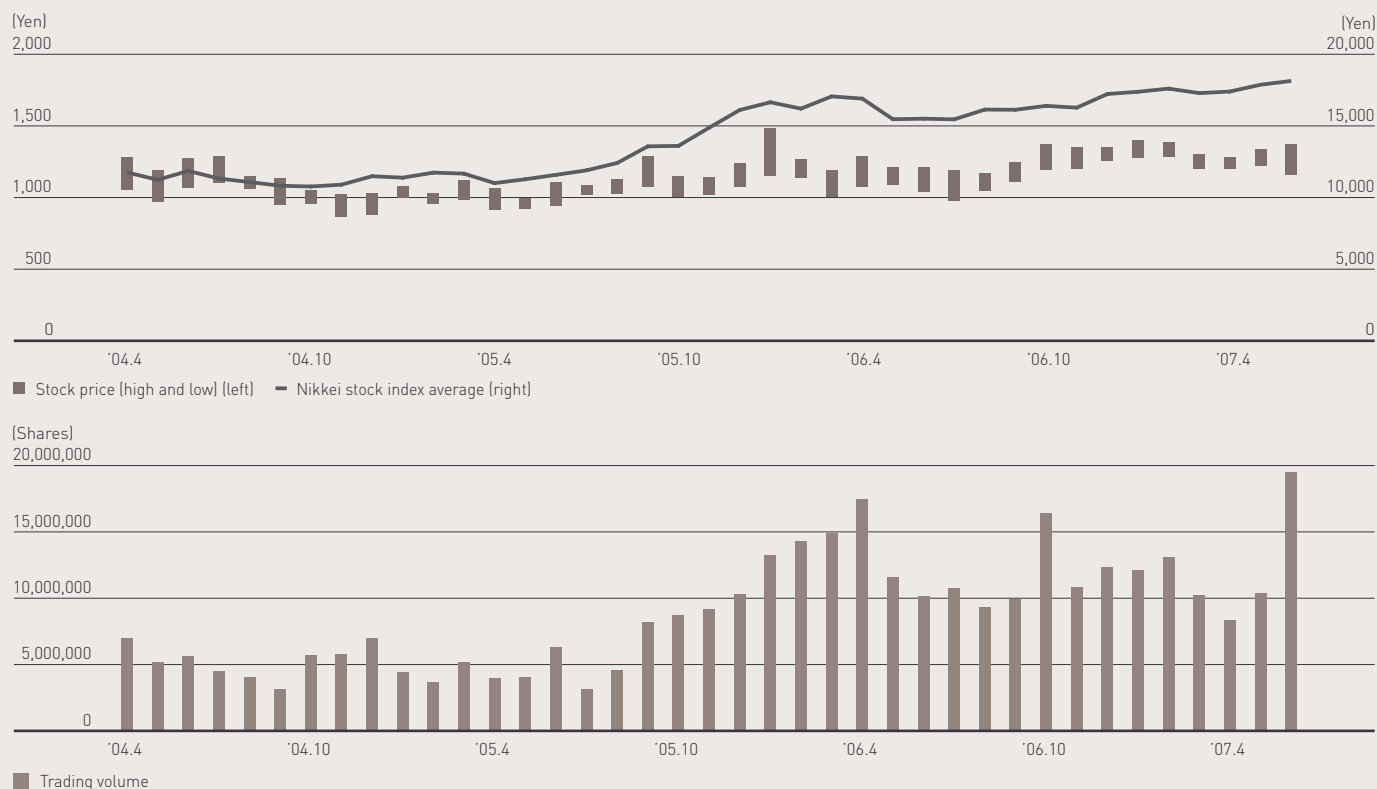
(As of March 31, 2007)

## Major Shareholders:

Shareholders	Number of shares held (Thousand shares)	Shareholding ratio (%)
Sumitomo Metal Mining Co., Ltd.	10,110	5.70
The Master Trust Bank of Japan, Ltd. (trust account)	8,472	4.78
The Iyo Bank, Ltd.	5,850	3.30
Japan Trustee Service Bank, Ltd. (trust account)	5,401	3.04
Sumitomo Corporation	4,383	2.47
Sumitomo Life Insurance Company	4,227	2.38
The Hyakujushi Bank, Ltd.	4,198	2.37
Sumitomo Mitsui Banking Corporation	4,136	2.33
The Sumitomo Trust and Banking Co., Ltd.	3,408	1.92
Employee's Stock Fund	3,044	1.72

(As of March 31, 2007)

## Stock Price and Trading Volume: (Osaka Securities Exchange)



# CORPORATE DATA

Company Name:	Sumitomo Forestry Co., Ltd.
Founded:	1691
Incorporated:	1948
Paid-in Capital:	¥27,672 million
Head Office:	Marunouchi Trust Tower North, 1-8-1, Marunouchi, Chiyoda-ku, Tokyo 100-8270, Japan Tel: 81-3-6730-3500 Fax: 81-3-6730-3504
Consolidated Subsidiaries:	45 (Overseas 13)
Associated Companies:	7 (Overseas 6)
Number of Employees (Consolidated):	12,259
Homepage:	<a href="http://sfc.jp/english/">http://sfc.jp/english/</a>
Independent Auditors:	SHIN NIHON & CO.
Transfer Agent and Registrar:	The Sumitomo Trust and Banking Co., Ltd. Stock Transfer Agency Department 1-4-4, Marunouchi, Chiyoda-ku, Tokyo 100-8233, Japan

[As of March 31, 2007]

For further information, please contact:

Sumitomo Forestry Co., Ltd.  
Corporate Planning Division

Tel: 81-3-6730-3506 Fax: 81-3-6730-3507





SUMITOMO FORESTRY CO.,LTD.

MARUNOUCHI TRUST TOWER NORTH, 1-8-1, MARUNOUCHI,  
CHIYODA-KU, TOKYO 100-8270, JAPAN

TEL: 81-3-6730-3500 FAX: 81-3-6730-3504

URL: <http://sfc.jp/english/>

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