

REVIEW OF OPERATIONS

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TIMBER AND BUILDING MATERIALS BUSINESS

Segment Performance Highlights

	(Millions of yen)			
	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.

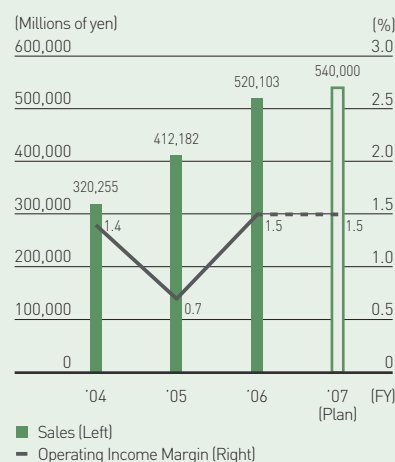
Operating Income of Main Subsidiaries

	(Millions of yen)		
	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.

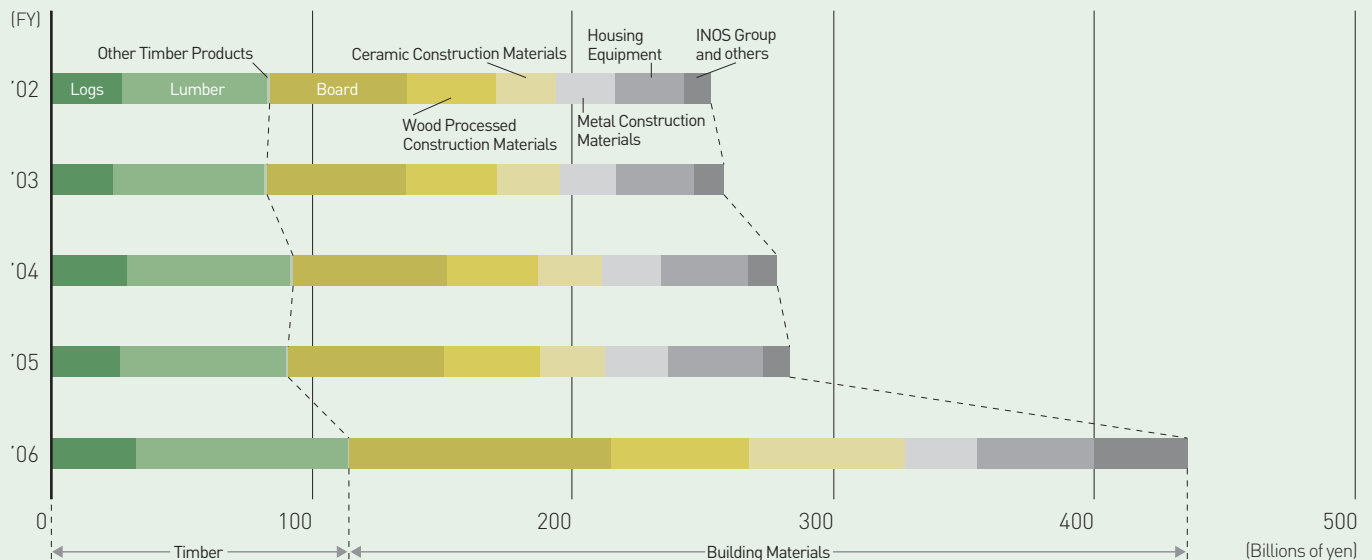
Manufacturing of Building Materials Business

- 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 be a base for future new business expansion in forest management, manufacturing, and other areas.

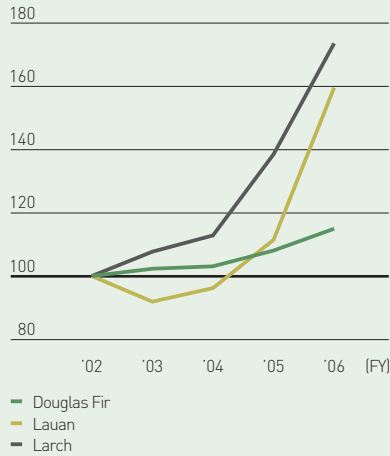
Manufacturing of Building Materials Business

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.

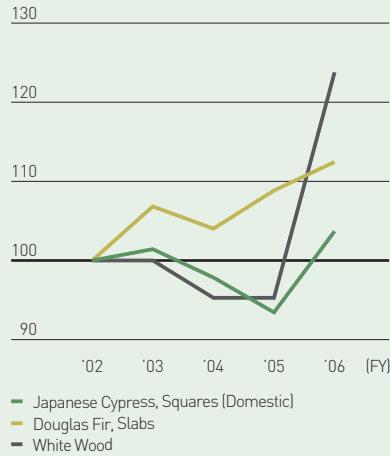
In our overseas operations, we responded to the growing concern about environmental issues around the world by expanding the use of raw materials drawn from plantation forests in our manufactured products. We invested aggressively during the year in anticipation of growing demand for wood board materials 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)

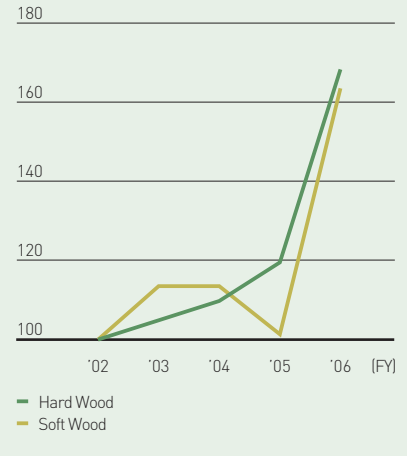
Log Price Indices



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

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 CO₂ emissions. In this way the branch is contributing to the prevention of global warming.



Cedar Plywood

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.



Processed MDF

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	—

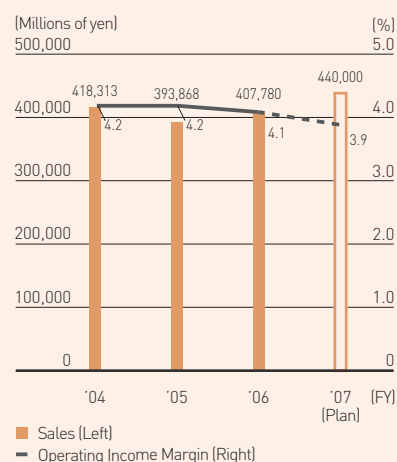
Note: The sales figures given include intersegment transactions. Operating income figures include internal profit prior to the deduction of amounts such as intersegment transactions and headquarters expenses that are not apportionable.

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.

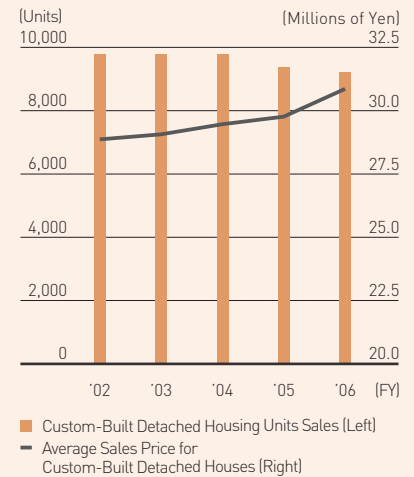


MyForest-WARAKU



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

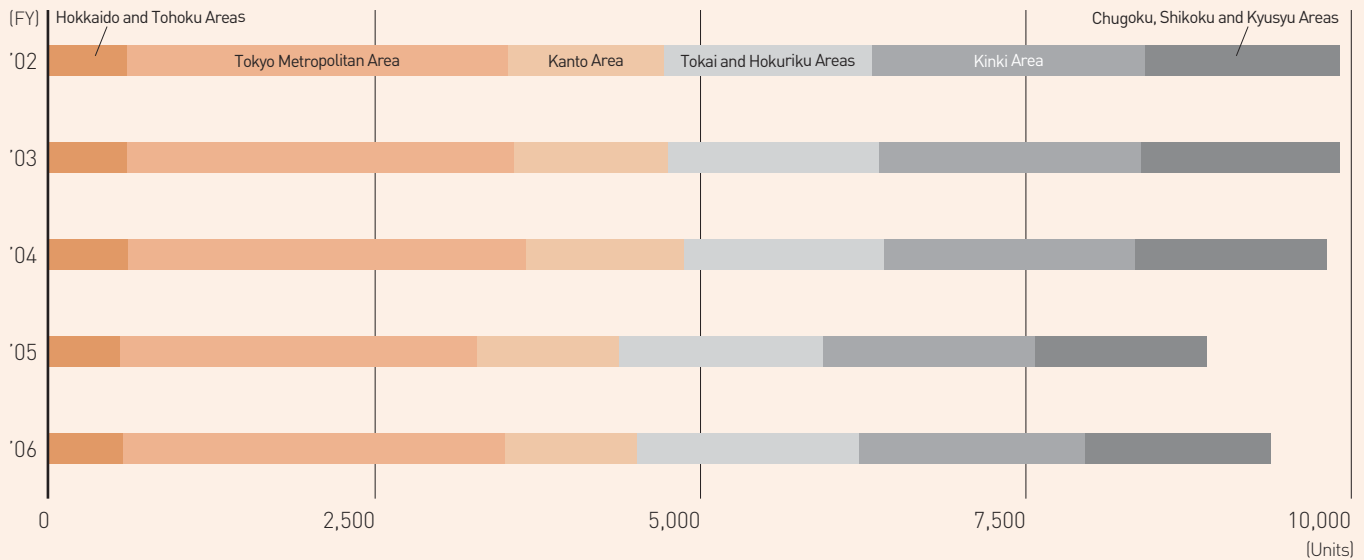
North America, MyForest-Waraku providing a blend of Japanese style elements and functionality, and MyForest-GRAND LIFE single-story homes designed to complement the simple lifestyles preferred by the baby-boomer generation. The segment also introduced housing features focused on specific consumer needs, 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.

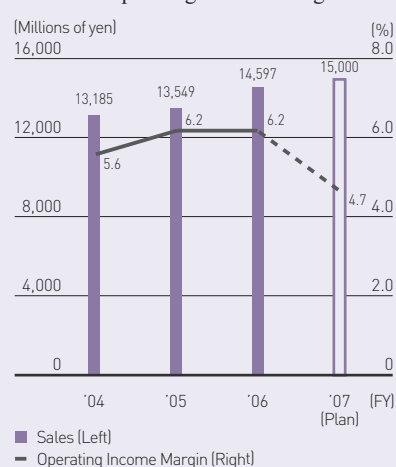
OTHER BUSINESSES

Segment Performance Highlights

	(Millions of yen)			
	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.

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.