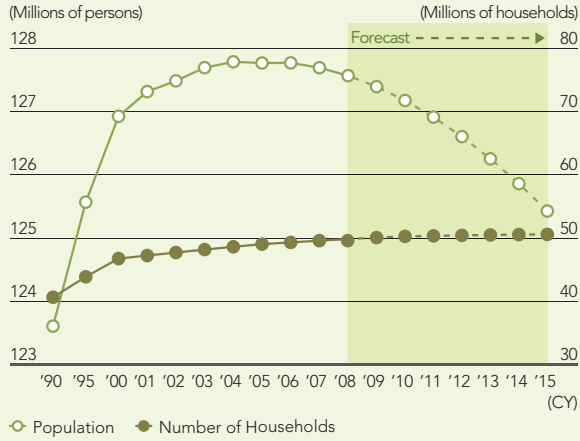


# MARKET DATA

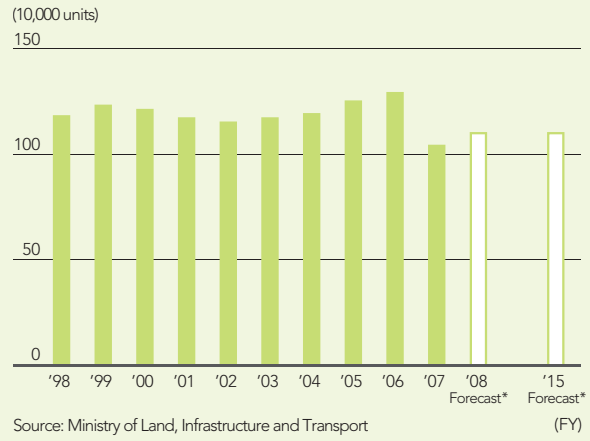
## Population and Number of Households



Source: "Population Statistics of Japan 2008", and "Forecast for number of households" published by the National Institute of Population and Social Security Research

Due to its low birthrate and aging population, Japan's total population has been in decline since reaching a peak of 127.83 million people in December 2004. Long-term forecasts increasingly point to the Japanese population falling below the 100 million mark. Given the slow pace of this population decline, however, the number of households is expected to remain steady for some time to come.

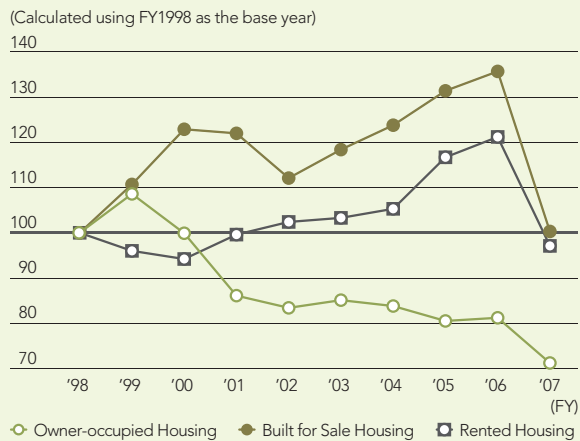
## Forecast for New Housing Starts



Source: Ministry of Land, Infrastructure and Transport (FY)  
\* In-house estimate

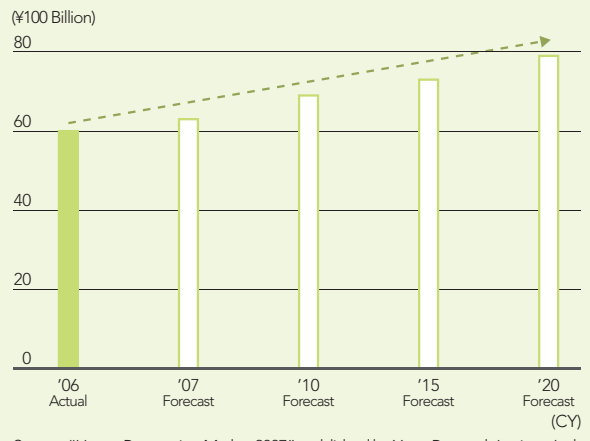
In fiscal 2007, Japan recorded a fall in the number of new housing starts for the first time in five years. The decline was due to a significant slump in condominium and other large-scale residential building starts stemming from an amendment to the Building Standards Law. The anticipated rebound in housing starts in fiscal 2008 is likely to be restricted by deteriorating economic conditions and a rise in the price of daily commodities. However, factors such as the steady number of households suggest that total housing starts will remain at around the 1.0 million level for the foreseeable future.

## Housing Starts Index by Housing Type



In fiscal 2007, the enactment of the amended Building Standards Law saw a decline in the number of owner-occupied, built-for-sale, and rented housing starts. The number of owner-occupied housing starts, which is closely related to our core business segment of new custom-built housing, has been in decline since 2000. The sizeable drop in owner-occupied housing starts recorded in fiscal 2007 stemming from the amended Building Standards Law is, however, expected to be temporary.

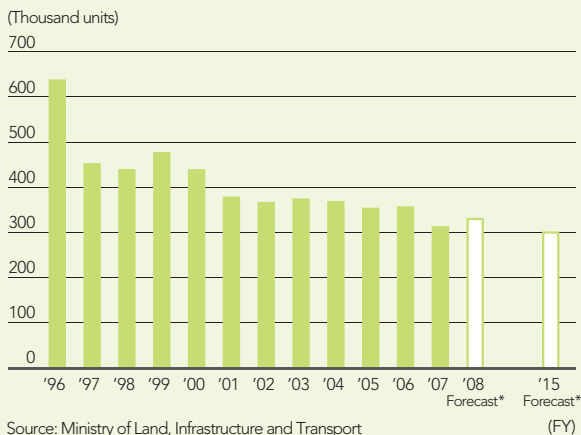
## Remodeling Market Forecast



Source: "House Renovation Market 2007", published by Yano Research Institute Ltd.

Since the majority of Japan's current housing stock was constructed prior to 1980, there are still many wooden houses that do not meet the earthquake resistance standards introduced in 1981. With growing demand for safe housing, the remodeling market is expected to grow in the medium term as the number of households peaks and society approaches a turning point for housing stock.

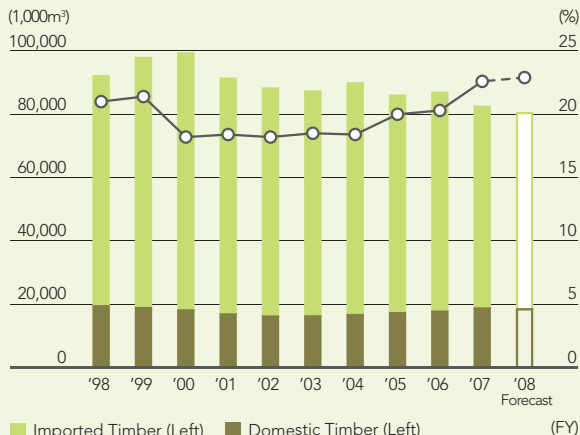
### Owner-occupied Housing Demand



Source: Ministry of Land, Infrastructure and Transport  
\* In-house estimate

In light of the continuing decline in population, over the long term we can expect to see a gradual reduction in demand for owner-occupied housing. However, as illustrated in the government's "200 Year Housing Vision," there is increasing demand for safe and high-quality housing. Although the decline in overall demand for owner-occupied housing will have a considerable impact on the majority of home builders, we believe that the Company will be relatively unaffected by this trend because of its focus on high-quality housing products.

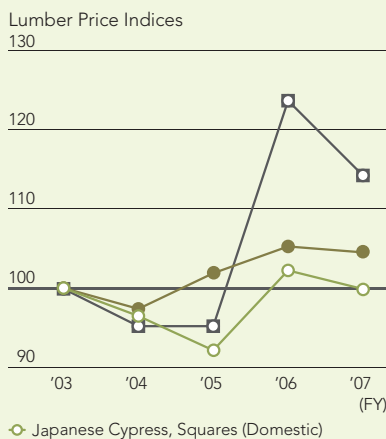
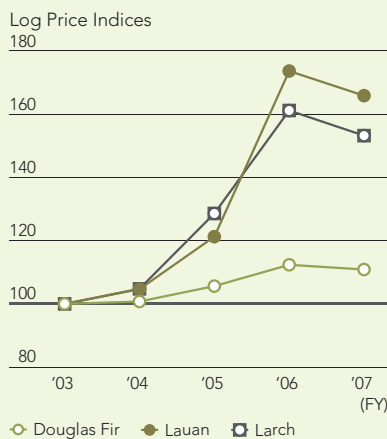
### Domestic Demand for Timber



Source: Forestry Agency

The state of Japan's housing market is reflected in sluggish growth in domestic demand for timber. However, we are seeing a move away from overdependence on imported timber, previously caused by price and supply-related factors, to a gradual shift toward the use of domestic timber. This is due to growing recognition of the importance of a sustainable forestry, coupled with other factors, including import costs and import restrictions. As a result, Japan's self-sufficiency ratio in timber is rising despite little prospect of growth in overall demand.

### Timber and Building Materials Market (Calculated using FY2003 as the base year)

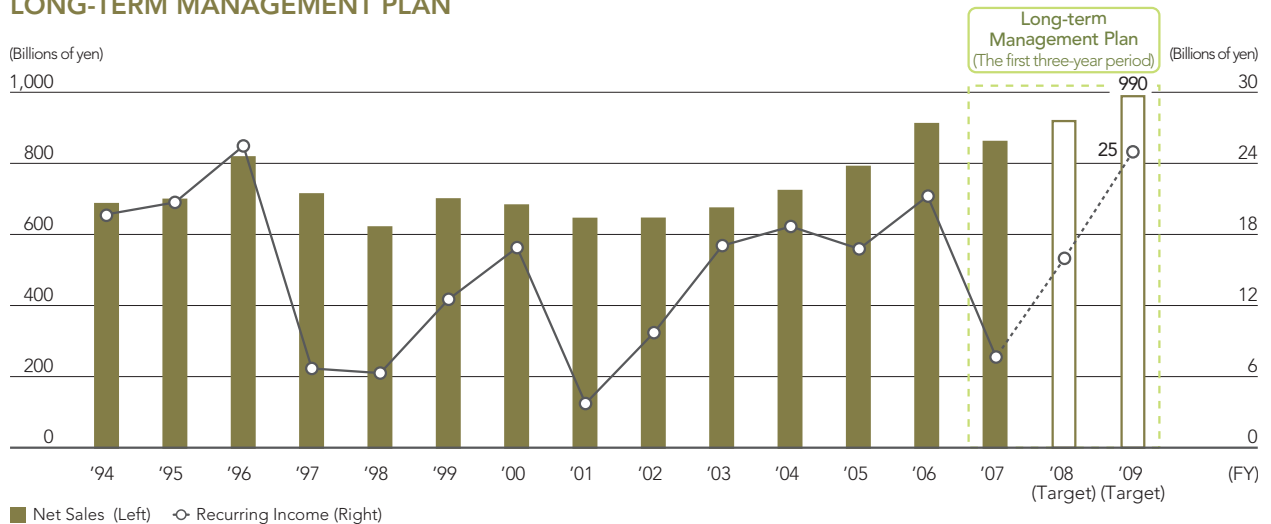


In fiscal 2006, prices for timber and wooden boards rose sharply in Japan and around the world as demand grew from the rapidly expanding economies of China and other emerging nations. In fiscal 2007, however, plywood prices plummeted due to a dramatic change in the market caused by the historic fall in new housing starts. The rapid deterioration in market conditions, combined with soaring prices for raw materials, has had a negative effect on the Company's earnings. On a positive note, however, the plywood market has already bottomed out.

# VISION: LONG-TERM MANAGEMENT PLAN

The Sumitomo Forestry Group is currently advancing its operations according to its long-term management plan, "Project SPEED."\* This plan outlines the Group's future direction and incorporates its goals for the 10-year period from April 2007 to March 2017.

## LONG-TERM MANAGEMENT PLAN



### \* Meaning of Long-term Management Plan, "Project SPEED"

**SPEED** reflects the Group's commitment to swiftly implementing the goals set out in the plan.

It serves as an acronym for:

"**S**trong **P**assion **E**nables us to become an **E**xcellent company by implementing **D**etailed strategy."

### Future Business Environment

- The owner-occupied housing market has the greatest impact on the Sumitomo Forestry Group's business performance. In the future, we expect this market segment to contract due to declines in the population and the number of households.
- We envisage significant business opportunities for remodeling and real estate business. The market for remodeling is steadily expanding thanks to growth in housing stock and improving longevity of houses. In the real estate industry, meanwhile, methods of delivering added value through services and other intangible means are diversifying.
- Looking worldwide, we expect the economies of the BRICs to continue to grow high, while the economies of the United States and the European Community will also be healthy in the long-term view. In addition, there is rising demand for natural resources, which is related to environmental issues. Therefore, we anticipate growing demand and diversifying uses for timber and building materials on a global scale.

### Business Concept

Core businesses: "Distribution/Manufacturing of Timber and Building Materials Business" and "New Custom-built Housing Business"

Priority growth businesses: "Overseas Operations," "Real Estate Business," and "Remodeling Business"

### Numerical target

Fiscal 2009: Net sales: ¥990 billion  
Recurring income: ¥25 billion

Fiscal 2016: Net sales: ¥1,600 billion  
Recurring income: ¥80 billion

## FORMULATION OF LONG-TERM MANAGEMENT PLAN

### Shift to Business Structure with Diversified Income Sources

Since commencing operations in the forestry business, the Group has advanced into various businesses related to wood and housing. Due to the nature of our business structure, however, our profitability is easily swayed by trends in the owner-occupied housing market. This is because our two core businesses—"Distribution/Manufacturing of Timber and Building Materials Business" and "New Custom-built Housing Business"—account for more than 90% of the Group's earnings. Under "Project SPEED," therefore, we will seek to diversify our

income sources by fostering and reinforcing businesses that enable us to demonstrate our competitive strength as a Group, while generating synergies with our core businesses. Specifically, we will further reinforce the earnings power of our two core businesses, which we have positioned as generators of stable cash flows. At the same time, we will focus our managerial resources on nurturing three other businesses—"Overseas Operations," "Real Estate Business," and "Remodeling Business"—which we have positioned as priority growth businesses. Here, our aim is to create third and fourth income pillars to complement our core businesses.

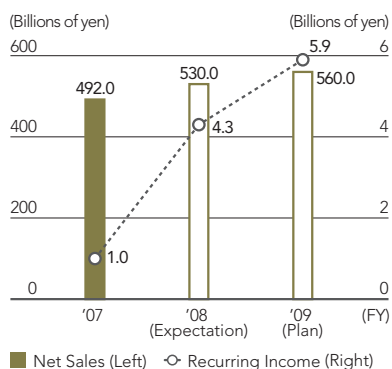
## LONG-TERM MANAGEMENT PLAN (THE FIRST THREE-YEAR PERIOD): BASIC POLICIES AND FISCAL 2007 INITIATIVES

### Core Businesses

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

In addition to earning commissions as a trader of timber and building materials, we will work to build a comprehensive value chain covering the distribution of the products we handle. We will take aggressive measures to stimulate the industry, including by providing managerial support if required, in our role as industry leader.

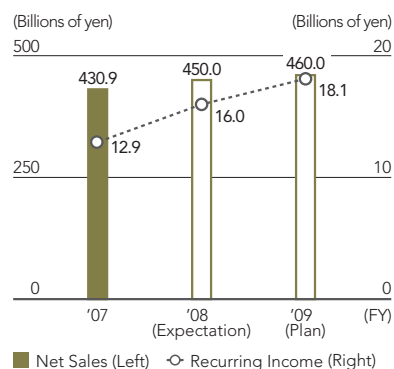
In fiscal 2007, we contributed to 40% to the establishment of a "Fund to Continue the Activities of Small and Medium-Scale Corporations in the Housing and Related Industries." By providing managerial support in this way, we stepped up efforts aimed at stimulating the industry.



#### New Custom-built Housing Business

Deploying our design and wood-related consulting capabilities, we are pursuing the building of high quality houses with a top priority on the satisfaction of our customers. We are also working to maximize synergies and enhance efficiency by creating a sales system that is united with our apartment business.

In fiscal 2007, we expanded our product variation with the release of new items. For example, we launched a flagship product with principle structural members made 100% from domestic timber. We also unveiled a product targeting first-time buyers, as well as other product for all-electricity-powered home with solar electricity system.



### Priority Growth Businesses

#### Overseas Operations

Our strategy is to manufacture wooden building materials using plantation timber to promote stable supply to world-wide sales destinations and environmentally friendly proposals. As for priority markets for wooden building materials and new markets for detached housing, we are targeting Pan Pacific countries such as South Korea, China and Australia in addition to the United States. At the same time, we will actively invest in reforestation to get hold of logs.

In fiscal 2007, we embarked on a land development and improvement project in the United States and started developing detached spec homes business in Australia.

#### Real Estate Business

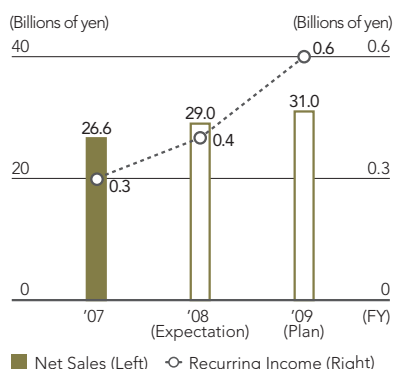
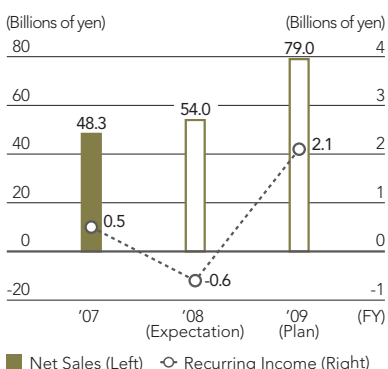
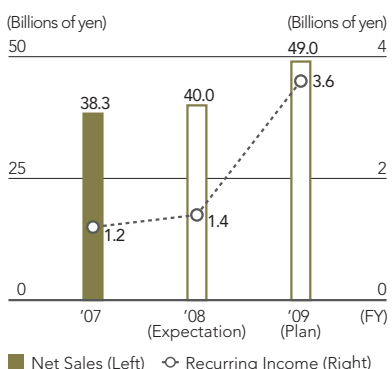
In this business, our strategy is to purchase land and add value by constructing rental properties, condominiums, or income-producing buildings, such as private pay nursing homes. We then operate or sell the completed projects. In our detached spec homes sales business, we sell high-value properties targeted mainly at first-time buyers in peripheral urban areas.

In addition to selling detached spec homes, in fiscal 2007 we expanded our real estate business in several ways. These included taking on a private finance initiative (PFI) project, entering the condominium sales business, and constructing housing and other facilities for elderly people.

#### Remodeling Business

In the remodeling business, we address wide-ranging demand from owners of homes built by both Sumitomo Forestry and other companies with traditional construction methods. Our strategy is to tap into latent demand by our technical skills in earthquake resistance, building durability, and other areas and by deploying our amassed design expertise gained through many years of experience in the custom-built housing business.

In fiscal 2007, we increased the scope of our remodeling business by opening three new sales offices and employing more staff. We also held numerous events at construction sites aimed at attracting new customers.



## TO OUR STAKEHOLDERS



Ryu Yano President / Director

The Sumitomo Forestry Group is currently implementing its long-term management plan, “Project SPEED.” The aims of the plan are to reinforce the earnings power of existing businesses and nurture new businesses into mainstay pillars of our operations, in order to achieve sustainable growth in the future. In other words, we will complement the stable earnings foundations of our core businesses—Distribution/Manufacturing of Timber and Building Materials Business, and New Custom-built Housing Business—by expanding the growth foundations of our priority growth businesses. In these ways, we will build a well-balanced business portfolio and a solid earnings base.

### REVIEW OF FISCAL 2007 RESULTS Importance of Well-balanced Earnings Structure Reaffirmed

In fiscal 2007, the Group launched its new long-term management plan, entitled “Project SPEED.” The goals of the plan are to broaden our earnings foundation and shift to a business structure capable of generating sustained growth amid a shrinking domestic market for owner-occupied housing.

Unfortunately, the housing market in fiscal 2007 faced unprecedented difficulties as new housing starts fell 19.4% year-on-year, to 1.03 million, while owner-occupied housing starts slipped 12.3%, to 0.31 million. This was due to economic uncertainty and concerns about the future, as well as the impact of an amendment to the Building Standards Law. A collateral result was a breakdown in the balance of supply and demand in the timber and building materials market, and to make matters worse, rising prices of raw materials for custom-built wooden housing placed downward pressure on earnings. To be honest, the Sumitomo Forestry Group’s business structure is heavily

weighted toward owner-occupied housing starts. In other words, in the year under review we reaffirmed the need to break away from our current earnings structure, which is excessively dependent on our two core businesses.

In fiscal 2007, the Group reported consolidated net sales of ¥861.4 billion, down 5.5% from the previous year. Operating income declined 64.5%, to ¥7.2 billion, and recurring income fell 64.0%, to ¥7.7 billion, due to the decrease in revenue combined with the effect of actuarial differences related to retirement benefit obligations and other factors. Even excluding such actuarial differences, operating income would have fallen 36.4%, to ¥11.8 billion, and recurring income would have dropped 37.0%, to ¥12.2 billion—significant declines in any event. Net income for the year plummeted 90.7%, to ¥1.1 billion, due partly to a ¥3.8 billion loss on devaluation of investment securities.

### Overview of Segment Results

**Timber and Building Materials Business**  
Sales –9.5%, Operating Income –58.2%

Sales in the Timber and Building Materials Business segment

**Income Plan by Business Segment (Long-term Management Plan; The First Three-year Period)**

(Billions of yen)

		Net Sales and Contract Revenues				Recurring Income			
		FY2009 Plan	FY2007 Actual	Change	%	FY2009 Plan	FY2007 Actual	Change	%
Core Business	Distribution / Manufacturing of Timber and Building Materials Business	560.0	492.0	+68.0	+13.8%	5.9	1.0	+4.9	+490.0%
	New Custom-built Housing Business	460.0	430.9	+29.1	+6.8%	18.1	12.9	+5.2	+40.3%
Priority Growth Business	Overseas Operations	49.0	38.3	+10.7	+27.9%	3.6	1.2	+2.4	+200.0%
	Real Estate Business	79.0	48.3	+30.7	+63.6%	2.1	0.5	+1.6	+320.0%
	Remodeling Business	31.0	26.6	+4.4	+16.5%	0.6	0.3	+0.3	+100.0%
	Elimination and/or Corporate	(189.0)	(174.8)	(14.2)	—	(5.3)	(8.4)	(3.1)	—
	Total	990.0	861.4	+128.6	+14.9%	25.0	7.7	+17.3	+224.7%

declined 9.5% year-on-year, to ¥470.9 billion, and operating income dropped 58.2%, to ¥3.3 billion. In Japan, the enactment of the amended Building Standards Law caused housing starts to decline, leading to a slump in demand and a fall in sales prices of timber and building materials. The market for plywood, which in the previous year saw sharp price increases, softened suddenly in the year under review, impacting both the distribution and manufacturing sides of the business to a degree unseen in recent years.

Overseas, our medium density fiberboard (MDF) manufacturing business, which we have been developing in Australia and New Zealand, continued reporting stable production and sales thanks to healthy demand in Japan, Oceania, and Asia, thus contributing to overall segment earnings.

### Housing and Housing-related Businesses Sales -0.1%, Operating Income -47.0%

In the housing business, we promoted sales of high-value-added products, enabling us to raise the average unit sales value, up to 1.9% to ¥31.5 million. Despite a decline in the number of sales units, therefore, total sales in the Housing and Housing-related Businesses segment remained mostly unchanged, down just 0.1%, to ¥407.7 billion. However, we were unable to offset surging prices of construction materials through cost-reduction efforts. Accordingly, segment operating income declined 47.0%, to ¥8.8 billion.

In the New Custom-built Housing business, the number of orders received decreased 4.6%, to 9,301 units, due to depressed individual incomes and the deteriorating economic outlook. However, the apartment business, which we now operate as part of the custom-built detached housing business, generated a year-on-year

increase in orders, as did the spec homes business, which has been expanding its operational scale and area.

### OUTLOOK FOR FISCAL 2008 Sharp Profit Turnaround Despite Difficult Conditions

Since the beginning of fiscal 2008, the timber and building materials market has bottomed out and is showing signs of stabilizing. However, the prices of metals and crude oil have kept rising, leading to higher prices of daily commodities. Due also to growing concern about economic slowdown, the recovery in housing starts is not expected to be strong, and the owner-occupied sector will recover only to about the 0.33 million unit level.

Facing these challenges, we have embarked on a new long-term management plan, entitled "Project SPEED," which calls for reforms to create a robust business structure to withstand changing business conditions. Specifically, we will reinforce our two core businesses (Distribution/Manufacturing of Timber and Building Materials Business and New Custom-built Housing Business), which generate stable earnings, while expanding our presence in priority growth businesses. In this way, we will create a well-balanced business portfolio and build a solid earnings foundation.

As stated earlier, the Sumitomo Forestry Group faces a business environment of unexpected difficulty. We have revised our recurring income projection for fiscal 2009, the third year of "Project SPEED" and the final year of the first three-year period, to ¥25.0 billion, down from ¥32.0 billion, based on envisaged business conditions in the years ahead. In fiscal 2008, we project a 6.8% year-on-year increase in net sales, to ¥920.0 billion. In addition, we have resolved the factors especially, occurred in fiscal 2007 caus-



ing downward pressure earnings, and we have renewed our cost-cutting efforts. Therefore, we forecast operating income of ¥16.0 billion (up from ¥7.2 billion in fiscal 2007) and net income of ¥9.0 billion (up from ¥1.1 billion).

## FUTURE POLICIES

### Raise Profitability of Core Businesses

Guided by “Project SPEED,” we will concentrate on strengthening its core businesses while expanding and nurturing its priority growth businesses. To this end, in our core businesses—Distribution/Manufacturing of Timber and Building Materials Business and New Custom-built Housing Business—we will seek to raise efficiency and boost profitability through a rigorous reassessment of costs, in order to generate stable earnings even in the face of changing future business conditions. As a prerequisite to this initiative, we will allocate the necessary managerial resources for our priority growth businesses, which will become mainstay profit pillars in the future.

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

In the Distribution of Timber and Building Materials Business, we will implement more meticulous inventory management by gaining an accurate grasp of actual demand and making purchases accordingly. To raise average earnings per employee, we will reallocate human resources along product lines. As the pace of realignment of the domestic distribution sector increases, meanwhile, we will demonstrate our strengths as industry leader in an effort to boost the growth potential of the entire sector, while also raising our market share. In addition, we will fully utilize our international network to expand our share in the global market. This will enable us to overcome challenges, including the scheduled increase in export tariffs on Russian logs (to 80%) in January 2009.

In the Manufacturing of Building Materials Business, we will establish manufacturing bases to make most effective use of plantation timber, domestic timber,

and timber waste. In these and other ways, we will work to advance our operations in an environmentally friendly manner, both in Japan and overseas.



#### New Custom-built Housing Business

Growing worldwide awareness about environmental issues serves to highlight the increasingly superior advantages of wooden housing in terms of fixing carbon dioxide and reducing environmental impact. In addition to providing the comfort of wooden housing, we are seeking to expand the market share using the “environment” keyword. Utilizing our strong brand and credibility, we will boost our market share by building houses featuring excellent designs and high-quality materials that deliver a high level of customer satisfaction. At the same time, we will strive to increase earnings through rigorous efforts to lower basic costs and reduce expenditures. At the end of the day, we understand that full-scale recovery of the owner-occupied housing market will require some time. Nonetheless, we will create a structure capable of generating steady profits by raising the efficiency of our business resources, including employees and model homes.

#### Allocated Investments to Priority Growth Businesses

As stated earlier, our first task is to swiftly implement measures to enhance the profitability of our core businesses. At the same time, we must strive to expand our presence in new fields in which we can generate synergies with our core businesses—with the aim of building future earnings pillars. Fortunately, the Group has a sound financial base and exceptional human resources capable of embracing new business challenges. While the outlook for the business environment is clearly not optimistic, we feel positive in that we have an opportunity to expand into new businesses. Our policy is to seize this opportunity and make proactive growth-oriented investments in three strategic fields that we have identified: Overseas operations, Real Estate Business, and Remodeling Business. (Please see the Special Feature section on page 27 for more details.)

#### Overseas Operations

The Japanese market is regarded as the world's most challenging in terms of emphasis on quality. Deploying the product manufacturing know-how we have amassed in such a tough market, we will reinforce our system for supplying high-quality building materials to global markets. To this end, we will upgrade our existing manufacturing operations, establish new ones, and target M&A opportunities, and considering various other possibilities, with the aim of taking the right steps based on proper research into market conditions. In addition to the United States, we are advancing our housing supply business in South Korea, China, and Australia. Our plan is to exploit these markets by bringing together the housing cultures of Japan and our partner nations, while

closely monitoring business conditions. Given growing moves to secure resources on a global basis, moreover, there are strong expectations for forest resources as well. Here, we are in an excellent position because we have forestation technologies, forestry management know-how, and a timber distribution network. In 2007, we welcomed into the Sumitomo Forestry Group a company managing around 20,000 hectares of forest in Papua New Guinea, thus broadening the total area of overseas forests in our possession. With respect to forestry resources, we will adopt a multifaceted approach to our forestation and forest management businesses in the future.

### Real Estate Business

We regard our real estate business as an area in which we can convert challenges into opportunities. The domestic real estate market, where prices have been gradually increasing, has been destabilized by concerns about economic deterioration. Due to an oversupply of condominiums, meanwhile, unsold units are now becoming conspicuous, underscoring a complete change from the situation prior to 2007. From the perspective of the Sumitomo Forestry Group that joined the business later, however, this market situation provides good opportunities to make high-quality purchases. We will focus particular attention on properties that envisage future Japanese market needs, such as dedicated facilities for the elderly and private pay nursing homes. At the same time, our policy is to expand our business by utilizing our brand strength in "wood and housing" to propose comprehensive solutions.

### Remodeling Business

Among the stock of detached housing in Japan at present, the most prevalent construction method is the wooden post-and-beam construction method, in which the Group specializes. Moreover, our remodeling business is not limited to houses built by our own company. Our target audience is broad and includes owners of detached wooden houses sold by other companies. However, the key distinguishing factors in the remodeling market are technologies and know-how. Anticipating a steady increase in demand in the future, we will differentiate ourselves by developing remodeling technologies to enhance earthquake resistance and a broad range of products for apartment. Going forward, we will actively invest resources into people, goods, and finances to target renewed growth.

### SHAREHOLDER RETURN

**Stable, Consistent Returns:**

**¥15.00 Annual Dividend Maintained**

Fiscal 2007 saw a temporary drop in net income due to

sudden deterioration of business conditions and a loss on devaluation of investment securities. In fiscal 2008, however, we forecast a major recovery in net income. We also regard the return of profits to shareholders as our most important priority. Accordingly, our policy is to ensure that profits are appropriated in a stable, consistent manner. Based on this approach, in fiscal 2007 we declared annual dividends of ¥15.00 per share, unchanged from the previous fiscal year.

### IN CONCLUSION

**"Project SPEED":**

**Combination of Offensive and Defensive Strategies**

As Japan enters an era of population decline, there will be a gradual, yet unavoidable, downward trend in the number of households. Therefore, we cannot draw a scenario for growth only by waiting for the recovery of the owner-occupied housing market. In this context, the Sumitomo Forestry Group's most urgent task is to secure wide-ranging income sources and shift to a highly profitable business structure that can withstand changes in the market environment. Our long-term management plan, "Project SPEED," is designed to achieve these objectives. With resolute persistence, I will take the lead to ensure that the plan is fully implemented.

Fortunately, the Group is in a solid position. We have diverse business domains that comprehensively advance our operations, from upstream to downstream of "wood" and "housing." We also have talented human capital, exceptional technological expertise, and a sound financial position. By effectively mobilizing these strengths, we will get our long-term management plan, "Project SPEED" into full swing as our most important priority from the perspectives of building sustainable relationships with shareholders and all other stakeholders.

We look forward to your renewed understanding and cooperation as we tackle the challenges of the future.

September 2008

Ryu Yano

President / Director



A handwritten signature in black ink that reads "Ryu Yano".