

Review of Operations

POWER TRANSMISSION PRODUCTS

In the fiscal year ended March 31, 2004, sales of automotive parts remained strong, and sales of chains and power transmission units and components were solid. As a result, sales of power transmission products rose 3.8%, to ¥90.1 billion, and accounted for 75.6% of consolidated net sales. Operating income was up 14.7%, to ¥8.6 billion. Supported by a recovery in capital investment, conditions in the domestic market were favorable in nearly all industries, but conditions in North America were challenging.

Chains

The Kyotanabe Plant, which boasts leading-edge technical development capabilities and production technologies, is the key strategic base of the Company's chain division, and the high-value-added chains made at the Kyotanabe Plant have earned Tsubakimoto Chain a position of market leadership. These products include steel chains with superior functionality and durability, environmentally friendly plastic chains that are recyclable, and cableveyors that are enjoying growing demand in the IT and automotive industries.

In chain operations, sales in Japan increased from the previous year. A recovery in private-sector capital investment led to higher orders for standard roller chains in a wide range of industries, and in the IT industry, where conditions were strong, demand was favorable for plastic cableveyors. However, conditions were sluggish in North America, as inventories in the distribution industry remained under pressure. In Europe, we made progress with market development activities, securing first-time orders from large sales agents.

The increase in orders made clear the benefits of our investment in the Kyotanabe Plant, and we achieved profitability substantially higher than the planned levels.

In January 2004, we began introducing the cell manufacturing method in the fabrication process at the Kyotanabe Plant, and over the next year we will convert the plant's fabrication lines to this method in stages. As a result, we anticipate such benefits as increased productivity, reduced work in progress, and shorter production lead times.

With a specialization in high-added-value chains, the Company aims to reach a 20% share of chain markets worldwide. To achieve that goal, in North America we will strengthen our relationship with Rexnold Corporation, of the United States, through U.S. Tsubaki, Inc. (UST), establish a new network of sales agents, and pursue OEM supply business. In Europe, we will work to strengthen relationships with large sales agents, and in Asia we will strive to aggressively build our presence in China and to secure a dominant share of the high-end market in Japan.

Automotive Parts

With a global market share of nearly 30%, Tsubakimoto Chain is a leader in timing chain drive systems, which are automobile engine modules. The high quality of our products—including not only timing chains but also such products as tensioners, guides, and sprockets—and the functionality of our comprehensive system design capabilities have been highly evaluated.

In the year under review, the use of our products grew steadily among Japanese and overseas automakers, including Toyota, Honda, Nissan, General Motors, Ford, and Jaguar. In addition, we received our first order from DaimlerChrysler. Moreover, with the start-up of full-fledged production at subsidiary Tsubakimoto Automotive (Thailand) Co., Ltd. (TAT), we made further progress in bolstering our global production system.

As a result, sales reached a record high level. However, profits declined due to expenses associated with the transfer to Sumitomo Electric Industries, Ltd., of our sintered automotive parts operations.

The Tsubakimoto Chain Group is aiming to secure a market share of 32% in timing chain drive systems by the fiscal year ending March 2006. To achieve that goal, we will reinforce our five-point global production system, with the Saitama Plant in Japan serving as a strategic base complemented by UST, in the United States; Tsubakimoto Europe B.V., in Europe; TAT, in Thailand; and Tsubakimoto Automotive (Shanghai) Co., Ltd., which was established in April 2004, in China.

In timing belts for general industrial applications, sluggish demand in the first half of the fiscal year was offset by improved conditions in the second half, but the achievement of profitability in timing pulleys remained challenging.

Power Transmission Units and Components

Tsubaki Emerson Co., a member of the Tsubakimoto Chain Group, was established in April 2002 through the merger of the Company's power transmission units and components operations and Tsubakimoto Emerson Co., Ltd. The company produces and markets a range of products, including speed reducers, such as gear motors; linear actuators, such as Power Cylinders; and power transmission related products, such as couplings and clutches. Tsubaki Emerson boasts the leading share of the domestic market for a number of products, including Power Cylinders, where it has a 60% share.

In the year under review, the second year of operations for Tsubaki Emerson, the effects of the merger were apparent. The company achieved profitability in all of its business units and increased sales and profits overall. In particular, the achievement of profitability in reducers, which account for a large percentage of sales, was a significant accomplishment. In the future, we will bolster operations in our fields of strength by accurately grasping market needs and making progress in development. We will place a special focus on products for which demand is expected to grow, such as Power Cylinders.

MATERIALS HANDLING SYSTEMS

In the year under review, we focused on core business fields and worked to reduce procurement costs; however, sales declined 3.5%, to ¥28.4 billion, due to lower sales in the distribution and automotive industries. Conditions were difficult in domestic and overseas markets, and operating income was down 23.6%, to ¥1.9 billion. The segment accounted for 23.9% of consolidated net sales.

In materials handling systems, Tsubakimoto Chain aims to achieve steady growth through the application of selection and concentration in its core fields of business. Furthermore, Group companies are working to enhance their presence in their fields of specialty, such as Tsubakimoto Mayfran Inc. and Tsubakimoto Bulk Systems Corporation, in Japan, and Tsubaki Conveyor of America, Inc., and Korea Conveyor Ind. Co., Ltd., overseas.

In the year under review, we made steady progress in sales of storage systems to customers in the pharmaceutical industry, earning a 70% share of the market. Moreover, the market's evaluation of our technical capabilities in this field has begun to increase. We secured an order for our Genome DNA Freezer Storage System from the Institute of Medical Science at the University of Tokyo, which is playing a central role in a project concerning genetic information and medicine supported by the Ministry of Education, Culture, Sports, Science and Technology.

We have a dominant share of the domestic market for paper feeding systems for the newspaper industry. In the year under review, demand for replacement equipment

improved, and sales of these systems rose. In products for the automotive industry, where body paint shop conveyor systems are our flagship product, there was an increase in factors adversely affecting profitability, especially in China. Currently, we are developing products for fabrication lines, which will be a new field for the Company.

In the distribution industry, conditions were sluggish due to weak consumer spending. However, accompanying competition in mail delivery between Japan Post and private delivery companies, demand for our Mailsort system is growing, and we are implementing marketing activities to secure new orders.

In the IT industry, where the recovery in business conditions has been notable, orders are increasing. In line with the trend toward larger LCDs, we plan to boost sales with an improved version of our unmanned monorail system.

Tsubakimoto Chain is also working to expand its business in the provision of after-sales maintenance services, a field which benefits from synergies with system equipment sales. In particular, we are striving to bolster sales of maintenance services at automotive plants in North America.