Management's Views

Takashi Fukunaga
Chairman, President and Representative Director

We will leverage our manufacturing prowess to attain constant growth, and continue to further strengthen our competitive position through greater product quality, technology, and production capacity.

In fiscal 2008, the economy deteriorated particularly in the second half of the year, but the Tsubaki Group registered sales and profit growth for the sixth straight term, while also recording historically high profits for the third consecutive fiscal year.

Both sales and profit increased substantially on the back of strategies that maintained a balance between measures to improve our underlying business structure and initiatives for strengthening our core operations. We bolstered our financial standing and made our organizational structure more effective. We put priority on developing globally—based on the quality of our products and superior technologies—to help us bolster production capacity and improve productivity.

External operating conditions eroded markedly as the currency markets fluctuated rapidly and crude oil and raw material prices surged. However, we aim to hone our product capabilities, strengthen production potential, and build a stable supply network. Furthermore, we will not shirk from making the necessary investments to ensure that these changes reap rewards.

These initiatives will probably have a short-term negative effect on financial performance. Nevertheless, we are confident that the Group can enhance its growth potential from fiscal 2012 onward as it rekindles its potential for expansion and takes the steps to strengthen its resistance to the volatility in the current external business environment.

We thank our shareholders, investors, and associates for their continuing support.

On August 25, 2008, Tatsuhiko Mimoto, Tsubakimoto Chain Co. President and Representative Director, passed away. Following his appointment as president in June 2005, he had striven for three years to develop the Company's business. We would like to offer our heartfelt thanks to all our shareholders and investors for their kind support during his tenure.

Following a special Board of Directors' meeting held on August 28, 2008, the Company appointed Chairman and Representative Director Takashi Fukunaga as Chairman, President and Representative Director.

Management's Views

Growth record and achievements in the past 10 years

Let's examine the Group's growth record and achievements over the past decade or so.

The Tsubaki Group was susceptible to the domestic economy and capital investment and was highly exposed to the economic cycles of the 1990s. In the second half of the decade, we enacted a number of strategies to reduce our reliance on the domestic economy.

The fruits of these efforts are apparent in the numbers. For example, total capital investment in Japan in fiscal 2008 was largely unchanged from 10 years earlier (fiscal 1998) even though the economy has been on a recovery course over the past several years. In fiscal 2008, unit auto production was only 6% higher than 10 years earlier. However, the Group's consolidated net sales were 1.3x higher, and its ordinary income was 3.3x higher.

The Group's first strategies for improving its underlining foundations has been to bolster its financial standing. The ratio of interest-bearing debt to total assets was 28.2% 10 years ago and then worsened to 37.7% in fiscal 2001. However, it has improved consistently since then and fell to 19.4% at the end of fiscal 2008.

Secondly, the Group has pushed forward with its "Global Best" strategy for an active expansion into overseas markets. The overseas sales ratio has increased sharply, from 29.7% 10 years ago to 37.5% in fiscal 2008. In particular, industrial-use steel chains, which have particular quality advantages, and mainstay timing chain drive systems in Automotive Parts operations command leading shares in their markets worldwide.

The Group has strengthened production capacity and improved productivity. The plant adjacent to the head office in Osaka, which was particularly outdated, has been replaced with a large plant with cutting-edge chain operation capabilities in Kyotanabe City, Kyoto Prefecture. Although this investment has resulted in an increase in interest-bearing debt, it has dramatically improved productivity. Moreover, we have been enhancing our production capacity overseas, which has been at the forefront of efforts to procure products at the best possible locations worldwide.

We believe the steady implementation of this balanced strategy, consisting of both aggressive and defensive actions, has rendered the Group largely immune to conditions in the external economy.

Perceptions of external business conditions

What is the outlook for fiscal 2009 and beyond? Do you think external business conditions will worsen?

The slowdown in the U.S. economy due to the subprime loan problem and other factors has clearly had some serious repercussions for the global economy. In addition, the surge in crude oil and raw material prices and the rapid depreciation of the U.S. dollar have naturally had some detrimental effects on our own industry. For fiscal 2009, we forecast that consolidated net sales will rise by just over 1% and that ordinary income will decrease by more than 5%.

Under these circumstances, the Group has enacted STEP10, a new three-year medium-term management plan that runs

The Tsubaki Group's major strategic achievements in the past 10 years

	FY1998	FY2008	Change
Net sales (millions of yen)	¥128,298	¥167,203	1.3x higher
Ordinary income (millions of yen)	5,511	18,051	3.3x higher
Ratio of interest-bearing debt to total assets	28.2%	19.4%	8.8% improvement
Ratio of SG&A costs to sales	21.7%	17.9%	3.8% improvement
Overseas sales ratio	29.7%	37.5%	7.8% increase

Delicate Balance between Defensive and Expansionary Strategies Strengthening the Tsubaki Group's Ability to Withstand Economic Volatility

through fiscal 2011. Fortunately, the Group has many competitive products and has been steadily offsetting the negative factors that are presenting challenges by raising the prices of core products and increasing productivity. We intend to continue increasing sales as we elevate market share worldwide. Even assuming appreciation of the yen on foreign-exchange markets to ¥100=U.S.$1 and ¥159=€15, we forecast that average annual growth in ordinary income of 4.4% annually is attainable over the next three years.

As will be explained in detail, the Group plans to aggressively step up capital investment, with total expenditures coming to about ¥35 billion over the next three years. The resulting depreciation will total about ¥26 billion for the three years through fiscal 2011, representing a fairly large cost increase of ¥7.2 billion from the three years through fiscal 2008. As noted, we are targeting average annual growth in ordinary income of 4.4% annually as these rising costs are absorbed.

Issues facing the Tsubaki Group

What do you think are the biggest issues now facing the Tsubaki Group?

Looking back at the last 10 years, the main issue we face is that even though we have effectively strengthened the foundations for ensuring persistent growth, our initiatives are still some way from being completed. Our projection for a decline in ordinary income in fiscal 2009, albeit in single digits, is testament to this fact. We are still somewhat vulnerable to rapid appreciation of the yen in foreign-exchange markets. In addition, the Group must increase production and procurement in local markets.

We have been concentrating domestic output at the Saitama plant for production in Japan as automotive parts production remains at extremely high levels. Although it has not yet been a major problem, a major fire, earthquake, or other unforeseen occurrence could quickly disable our stable supply network, which is one of the Group's strengths. This would have serious consequences.

In addition, even though globalization has been advancing, products with a higher market share worldwide are clearly subject to the prevailing economic, social, and physical conditions of particular geographical regions. Making ourselves more able to absorb the impact of regional fluctuations would greatly strengthen our foundations for achieving consistent ongoing growth.

Basic strategies

Tell us about your strategies for dealing with these issues.

We will continue focusing on the two strategic areas where our efforts have been concentrated so far. That is, we will further enhance the competitiveness of our product lines and production capacity while further strengthening our financial standing.

Based on the topics previously discussed, we will accelerate strategic initiatives in the following four areas:

1. Decentralize plant operations and increase production capacity in Automotive Parts operations

The Group will decentralize some of its production at the Saitama plant, which is now the only production facility in Automotive Parts operations in Japan, to the Kyotanabe plant. This will be done to strengthen our ability to withstand natural disasters and any other unforeseen circumstances. Plans call for shifting around 10% of output to the Kyotanabe plant.

We are also considering expanding plant operations in Thailand.

2. Accelerate production and supply procurement from the best possible locations worldwide

For example, we plan to raise the local production and supply procurement ratios in Automotive Parts operations to 50% and raise the local procurement ratio in Power Transmission Units and Components operations to 20% in fiscal 2009.

3. Penetrate new markets and attract new customers

In Chain operations, we have established sales bases in Brazil and India. Even as the

STEP10 Plan—Building the Foundations for Ensuring Consistent Growth

global economy has been slowing, the Group is increasingly tapping into BRICs and other emerging markets that still have strong growth potential over the medium and long term. Moreover, for sectors with specific customers, we are focusing on capturing business from industries such as mining and basic materials and food production where active growth is occurring.

4. Promote technological innovation and new product development

The Group is stepping up technological innovation for lightweight, silent, and wear resistant applications to gain a technological edge in power-drive chains in Automotive Parts operations, which is now being targeted as a second key pillar of earnings accompanying the timing chain drive system business, an area where the Group is already a leading global manufacturer. In addition, another of our goals for Automotive Parts operations is to raise the portion of the sales mix accounted for by highly profitable new products from its current 20% to 30% over the long term.

These four strategies will require upfront investment in the near future, which will put downward pressure on profits. In other words, prioritizing profits for the future as external business conditions deteriorate now will temporarily exert pressure on earnings and limit profit growth over the next three years, as already noted. However, these initiatives will further raise earnings levels over the medium and long term, and I believe investment here will be crucial for ensuring consistently strong growth ahead.

Maximizing returns for shareholders

Tell us your basic views on maximizing returns for shareholders. Your dividend payout is not necessarily very high, is it?

Dividends per share (excluding commemorative dividends) were increased incrementally from ¥6 in fiscal 2004 to ¥7 in fiscal 2005 and ¥8 in fiscal 2008. That said, the consolidated dividend payout of 14.4%, 25.7% unconsolidated, in fiscal 2008 cannot be considered high.

This is because the Group aims to raise its profit levels and strengthen its potential for consistent growth, and is now at a stage when utilizing funds for capital spending and other upfront investment is crucial for nurturing earnings growth.

We will prudently and responsibly weigh up all of the options and benefits from either maintaining high retained earnings or further increasing the dividend payout.

Given these conditions, for the current growth stage the Group intends to maintain a high retained earnings ratio and promote policies for increasing market capitalization over the medium and long term in order to increase the share price as much as possible.

Naturally, raising the dividend payout will continue to be one of our major priorities, and we ask for the continuing understanding and support of shareholders and investors as we pursue these policies.

The Tsubaki Group will maintain its steadfast focus on becoming a global enterprise that can consistently register growth, thanks to the backing of its customers, shareholders, business partners, community members, and other stakeholders with whom we share a common goal.

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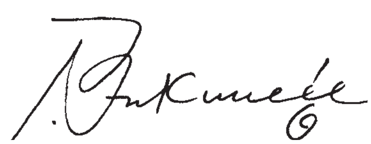

Takashi Fukunaga

Chairman, President and Representative Director

Enhancing Economic Value-Creation in the Group for Maximizing Shareholder Returns during Growth Stages