NIPPON PAPER GROUP, INC.
**Annual Report 2004**
For the Fiscal Year Ended March 31, 2004

PEOPLE

FOREST

# Looking for Sustainable Growth

PAPER

## Profile

Nippon Paper Group, Inc.* is a pure holding company for Nippon Paper Industries Co., Ltd. and Nippon Daishowa Paperboard Co., Ltd. Nippon Paper Group engages in the pulp and paper business, which produces and sells paper, paperboard, and household tissue; the paper-related business, which handles paper cartons and chemical products; and other businesses, such as logs and lumber, construction materials and logistics. The pulp and paper business is the main business pillar, accounting for nearly 80% of total sales and profits. Our diverse range of other operations is developed closely alongside the pulp and paper business.

*Nippon Paper Group, Inc. is the new name for Nippon Unipac Holding, as of October 1, 2004.

## Contents



**Disclaimer Regarding Forward-Looking Statements**

Statements contained in this annual report regarding current plans, outlooks, strategies and beliefs of Nippon Paper Group, Inc., other than those of historical fact, are forward-looking statements or forecasts based on the management assumptions of the Nippon Paper Group, Inc. in light of currently available information. Accordingly, one should refrain from making any investment decision based solely on the statements and forecasts contained in this annual report. The Company's actual future performance and results may be affected by changes in a number of factors and thus may differ materially from those described therein.

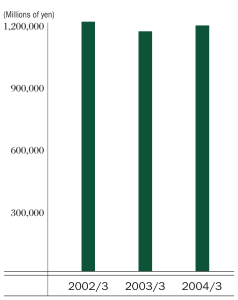
## CONSOLIDATED FINANCIAL HIGHLIGHTS

(Millions of yen)

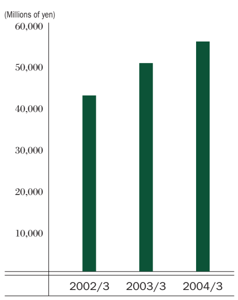
| | 2002 (Note 1) 2001.3.30 – 2002.3.31 | 2003 2002.4.1 – 2003.3.31 | **2004** 2003.4.1 – 2004.3.31 |
|---|---|---|---|
| Net sales | ¥1,211,422 | ¥1,165,450 | **¥1,192,649** |
| Operating income | 42,422 | 50,450 | **55,679** |
| Net income (loss) | (636) | 4,880 | **24,258** |
| Total assets | 1,721,745 | 1,630,126 | **1,637,366** |
| Current assets | 517,698 | 455,445 | **476,649** |
| Property, plant and equipment, net | 941,428 | 924,597 | **900,013** |
| Total investments and other assets (Note 2) | 262,618 | 250,083 | **260,703** |
| Liabilities and others | 1,314,376 | 1,221,923 | **1,207,744** |
| Total shareholders' equity | 407,369 | 408,202 | **429,621** |
| Interest-bearing debt | 903,336 | 851,311 | **842,278** |
| Debt/Equity ratio (times) | 2.1 | 2.0 | **1.9** |
| **(Per share: yen)** | | | |
| Net income (loss) | (590.30) | 4,283.53 | **22,025.22** |
| Total shareholders' equity | 377,308.99 | 374,133.23 | **392,140.80** |
| Dividends | 8,000 | 8,000 | **8,000** |
| **(Principal financial indicators)** | | | |
| Operating income to net sales | 3.5% | 4.3% | **4.7%** |
| Net income (loss) to net sales | (0.1)% | 0.4% | **2.0%** |
| Return on equity (ROE) (Note 3) | (0.2)% | 1.2% | **5.8%** |
| Return on invested capital (ROIC) (Note 4) | 3.4% | 4.2% | **4.9%** |
| Equity ratio | 23.7% | 25.0% | **26.2%** |
| Return on assets (ROA) (Note 5) | 2.6% | 3.2% | **3.8%** |
| Capital expenditure | 69,511 | 76,904 | **57,423** |
| Depreciation | 87,144 | 83,223 | **81,259** |
| Free cash flow | 13,221 | 56,804 | **14,425** |

Notes: 1. Fiscal 2002 (from March 30, 2001 to March 31, 2002) is the total of the 1st accounting period (from March 30, 2001 to September 30, 2001) and the 2nd accounting period (from October 1, 2001 to March 31, 2002).
2. Intangible assets and deferred charges are included in total investments and other assets.
3. Return on equity (ROE) = Net income/Total shareholders' equity
4. Return on invested capital (ROIC) = (Ordinary income + Interest expense)/(Interest-bearing debt + Total shareholders' equity)
5. Return on assets (ROA) = Ordinary income before interest/Interim averaged assets

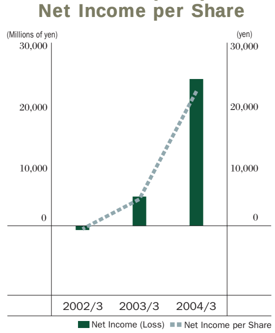
### Net Sales



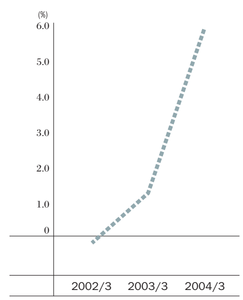

### Operating Income




### Net Income (Loss) and Net Income per Share




### Return on Equity (ROE)



On October 1, 2004, Nippon Unipac Holding changed its name to **Nippon Paper Group, Inc.** In renaming the holding company in sync with the widely recognized **Nippon Paper** brand, we aim to improve corporate value by further establishing our corporate brand as a leading company in the domestic pulp and paper industry.

On April 1, 2003, we reorganized Group companies, placing the paper business in the hands of Nippon Paper Industries Co., Ltd. and the paperboard business under the management of Nippon Daishowa Paperboard Co., Ltd., and launched the First Medium-Term Business Plan (hereinafter referred to as "the Plan") under the new structure. The Plan's initial targets call for:

- **Higher** (Consolidated ordinary income over ¥100 billion)
- **Faster** (Rationalization of production facilities)
- **Stronger** (Reducing consolidated interest-bearing debt to under ¥700 billion and raising productivity to over 10%.)

These targets place Nippon Paper Group on firm ground toward achieving its aim of becoming a world-class company.

Reflecting on fiscal 2004, ended March 31, 2004, the first year of the Plan, we continued to make steady progress on reducing costs, resulting in a stronger consolidated performance than in the previous fiscal year. Net sales increased 2.3%, or ¥27.2 billion, to ¥1,192.6 billion, operating income advanced 10.4%, or ¥5.2 billion, to ¥55.7 billion, ordinary income climbed 27.7%, or ¥11.0 billion, to ¥50.7 billion and net income soared 397.0%, or ¥19.4 billion, to ¥24.3 billion. Profits have grown steadily since the business integration in 2001. In particular, the paperboard business, one of the Group's core businesses, achieved a marked recovery in performance as a result of efficiently deploying management resources after business reorganization.

However, the paper business fell short of targets in the Plan owing to a rise in material and fuel prices as well as softer market prices, undermining the overall performance of the Nippon Paper Group. Moreover, we expect prices for woodchips, coal and crude oil to significantly increase in fiscal 2005 and fiscal 2006. Despite efforts by management, it was impossible to compensate for all these negative factors. As a result, we downwardly revised our original ordinary income target of ¥100 billion in fiscal 2006.

In May 2004, we formulated measures to reinforce the Plan, and in fiscal 2005 and 2006 we are promoting further cost reductions and paper sales reinforcement. Through these reinforcement measures, we plan to achieve our revised ordinary income target of ¥85 billion in fiscal 2006 by maximizing profitability. In addition, we are striving to achieve our initial target for ordinary income of more than ¥100 billion as soon as possible to create a robust corporate foundation able to sustain growth in any operating environment.

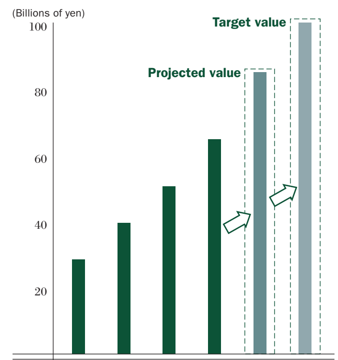
Nippon Paper Group has three areas of strength for achieving long-term profit growth. Our leading share of the domestic paper market is our first area of strength, backed by a solid customer base of major newspa-

### Three-year Performance Trends Following Management/Business Integration

(Billions of yen)

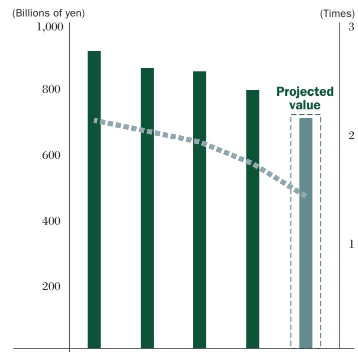
| | 2002/3 | 2003/3 | 2004/3 |
|---|---|---|---|
| Net sales | 1,211.4 | 1,165.5 | 1,192.6 |
| Operating income | 42.4 | 50.5 | 55.7 |
| Ordinary income | 28.6 | 39.7 | 50.7 |
| Net income (loss) | (0.6) | 4.9 | 24.3 |

### Projected Ordinary Income




| 2002/3 | 2003/3 | 2004/3 | 2005/3 Forecast | 2006/3 Projection | |
|---|---|---|---|---|---|
| 28.6 | 39.7 | 50.7 | 65.0 | 85.0 | 100.0 |

### Interest-bearing Debt Reduction Plan

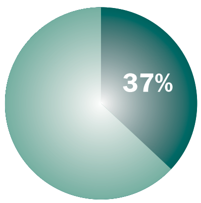



| | 2002/3 | 2003/3 | 2004/3 | 2005/3 Forecast | 2006/3 Projection |
|---|---|---|---|---|---|
| Interest-bearing Debt | 903.3 | 851.3 | 842.3 | 785.0 | 699.0 |
| D/E | 2.1 | 2.0 | 1.9 | 1.7 | 1.4 |

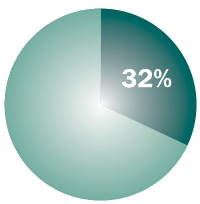
**2003 Company's Share of Paper Production in the Japanese Market**

| | Production amounts (thousands of tons) | Estimated share | Ranking |
|---|---|---|---|
| **Newsprint** | **1,332** | **37%** | **1** |
| Uncoated printing paper | 840 | 30% | 1 |
| Coated printing paper | 1,897 | 30% | 1 |
| Special printing paper | 117 | 36% | 1 |
| Business communication paper | 720 | 42% | 1 |
| **Printing and business communication paper** | **3,573** | **32%** | **1** |
| **Packaging, sanitary and other paper** | **744** | **20%** | **1** |
| **Paper total** | **5,649** | **31%** | **1** |
| Containerboard | 1,510 | 16% | 3 |
| White board | 285 | 16% | 3 |
| Other paperboard | 151 | 14% | 2 |
| **Paperboard total** | **1,946** | **16%** | **3** |
| **Paper/paperboard total** | **7,595** | **25%** | **2** |

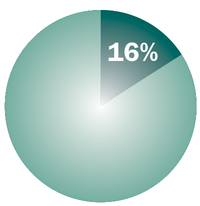
**Newsprint**




**Printing and business communication paper**




**Paperboard**




(Source: Compiled by Nippon Paper Group, Inc. Investor Relations, based on data supplied by Japan Paper Association and other sources)

per and publishing companies in the Japanese market, which is considerably large compared with other markets around the world. In recent years, growth in market scale has tapered off somewhat, but we expect stable revenue expansion in the domestic market in the future as we continue to respond to changing markets and growing demand for high-value-added products especially in publishing paper and business communication paper.

Our second area of strength is the superior location of our mills. Most of our main paper mills are located along the coast, and since most of the materials and fuel in the Japanese pulp and paper industry are imported from overseas, we enjoy significant cost advantages. In addition, compared with our competitors, our main mills for newsprint and containerboard are located near the Tokyo metropolitan area, making it easier to reuse wastepaper generated in cities.

Our third area of strength is our presence in a diverse range of unique businesses that create synergies with the pulp and paper business. In the liquid-packaging cartons business, which uses environmentally friendly paper materials, NIPPON PAPER-PAK CO., LTD. is one of the largest producers in Japan, with an approximately 34% share of the domestic market. Nippon Paper Chemicals Co., Ltd. manufacturers and sells various products that use compounds extracted from lumber, and boasts the highest share of the world market in low-chlorinated polyolefins. Nippon Paper Lumber Co., Ltd. is building a solid position as a top company in the domestic lumber distribution industry.

To ensure future growth, we are concentrating efforts on strengthening R&D, developing unique products, and using biotechnology in afforestation to ensure a stable and efficient supply of raw materials.

One of the most important management issues is how to achieve growth while avoiding risks, whereas the domestic paper and paperboard market is not expected to grow significantly. In tandem with bolstering its business foundation in Japan, Nippon Paper Group considers overseas markets, especially China, as crucial to future growth, and is promoting the launch of overseas operations as early as possible with low risk exposure.

Amid a rapidly changing operating environment, Nippon Paper Group intends to maximize its strengths in pursuing sustainable growth. We ask for your continued support of Nippon Paper Group.

T. Miyoshi

TAKAHIKO MIYOSHI
President, Nippon Paper Group, Inc.

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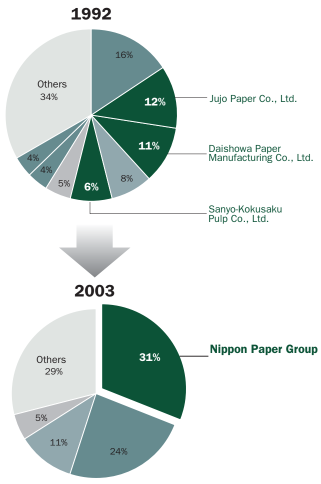
## Challenge

*The establishment of Nippon Unipac Holding (currently the Nippon Paper Group) in 2001 changed the face of the pulp and paper industry in Japan. In 2003, the top two companies in the industry, which included Nippon Paper Group, together commanded a 55% share of paper production, forming a new order in the industry. However, the operating environment for the paper industry presents the challenge of rising raw material and fuel prices, which directly affect the Group's earnings.*

*Under these circumstances, we formulated a Medium-Term Business Plan that targets consolidated ordinary income of at least ¥100 billion, productivity improvement of more than 10% and consolidated interest-bearing debt of less than ¥700 billion. Guided by the Medium-Term Business Plan, we are strengthening our profit base and financial position.*

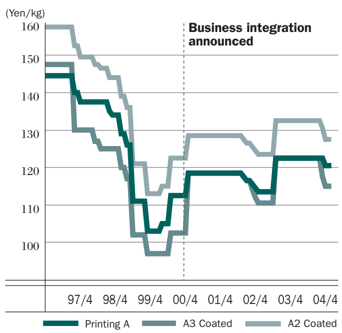
*In this section, we discuss our analysis of the operating environment and concrete measures and our philosophy regarding efforts to reinforce our First Medium-Term Business Plan.*

**Changes in Paper Production Share from Market Reorganization**



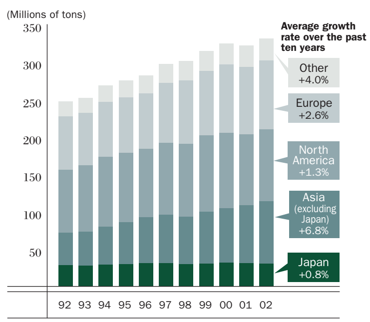

(Source: Compiled by Nippon Paper Group, Inc. Investor Relations, based on data supplied by Japan Paper Association and other sources)

**Paper Price Trends**




(Source: Nihon Keizai Shimbun, Inc.)

**Paper and Paperboard Consumption by Geographical Region**




(Source: Pulp & Paper International)

# Changes in the Operating Environment for Japan's Pulp and Paper Industry

## Restructuring in the Domestic Pulp and Paper Industry

Despite favorable conditions with demand growth in the Japanese pulp and paper industry, excess numbers of mid-sized manufacturers have brought instability in the market, leading to an inevitable decline in the earnings of pulp and paper companies for years. These companies have repeatedly made aggressive capital investments in anticipation of future demand growth during favorable market conditions, creating excessive supply capacity that triggers declines in market prices and deterioration in the operating environment.

However, after a series of mergers since 1993, Nippon Unipac Holding (currently Nippon Paper Group, Inc.) was established in 2001, creating a two-company structure, which includes our company, in the paper industry. In 1992, the top two companies in the industry only had a 28% share of the market, competing for market share with other companies. This figure increased significantly to 55% by 2003. This share of the domestic market is extremely high even compared with the pulp and paper industries in North America and Europe.

As a result of increasing our market share and making inventory management possible through production adjustments, paper prices have been stable since the announcement of business integration between Nippon Paper Industries Co., Ltd. and Daishowa Paper Manufacturing Co., Ltd. in March 2000. Since 2001, amid weakness in the Japanese economy, prices were relatively stable as a result of the new two-company structure in the paper industry.

## Global and Domestic Consumption of Paper and Paperboard

Consumption of paper and paperboard around the world is steadily increasing. In some advanced countries in North America and Europe, economic weakness over the past few years has caused negative growth, but globally consumption of paper and paperboard is increasing in most regions and countries around the world.

Today, Japan's paper and paperboard market accounts for approximately 10% of global consumption, or more than 30 million metric tons per year. Japan is the third largest market for paper and paperboard in the world after the United States and China. The rate of growth in consumption in Japan has tapered off due to the deceleration of growth in Japan's GDP since the 1990s.

Although Japan's GDP is unlikely to grow substantially as in other advanced nations, we believe sustainable growth is possible in paper and paperboard consumption.

## Growth in Consumption of Paper and Paperboard in China

Consumption of paper and paperboard in Asia (excluding Japan) has grown at an average of 6.8% annually over the past decade. We expect strong growth to continue in China due to its massive population. Per capita consumption of paper and paperboard in 2002 was 33kg in China, still a low level compared with 314kg in the United States and 241kg in Japan. According to the Almanac of China's Paper Industry, consumption of paper and paperboard in China will soar by the amount compared to that in Japan within 10 years.

Economic development in Asian countries such as China offers Nippon Paper Group significant business opportunities. We believe an issue of increasing importance is enhancing our international competitiveness through further cost reductions and stronger research and development capabilities, as raw material and fuel prices are rising along with growth in their consumption.

## Three Factors Affecting Earnings

### (1) GDP and Domestic Production Volume of Paper and Paperboard

The Japanese materials market appears to have peaked in terms of volume for steel, metals, cement and other materials. However, production volume of paper and paperboard, our core business, has continued to grow stably.

Domestic production of many other materials did not grow due to competition with imports, but production of paper and paperboard has grown steadily along with growth in GDP. Paper in particular has shown an elasticity of 1.0 versus real GDP over the past 10 years, an extremely high correlation.

Some of the reasons for this are that paper materials are suitable for conveying a lot of information, which can be easily glanced through, it is possible to distribute large volumes at low cost (as with flyers), and paper offers superior potential as a long-term storage medium. Even though the advent of a paperless society has been stated on countless occasions, and even with the emergence of the Internet, we expect demand for paper to remain on a stable growth path as the absolute volume of information continues to increase.

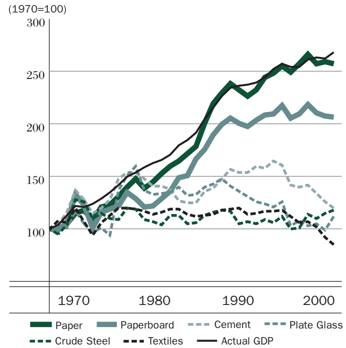
### (2) Exports and Imports of Paper

Although imports of copier paper and other types of paper account for a certain share of the market, most types of paper made in Japan are competitive in terms of quality, cost and service, so we believe that the impact of imports will be limited over the long term. The ratio of exports to imports of paper in Japan roughly counteract each other, with paper exports reaching 4.7% of domestic production and imports accounting for 6.6% of domestic consumption in 2003.

In 2003, the ratio of imported paper increased for mainly coated paper as a result of some customers proactively using imported paper due to an increase in paper prices in Japan in autumn 2002.

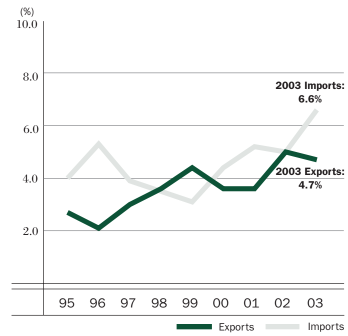
In the future, we expect about the same volume of paper imports as in 2003. At the same time, we are fully aware of the need to pay attention to fluctuations in exchange rates and the possibility of a deterioration in the worldwide supply/demand balance for pulp and paper from significant changes in regions such as China.

**Growth Trends by Material**




(Sources: Ministry of Economy, Trade and Industry, Economic & Social Research Institute)

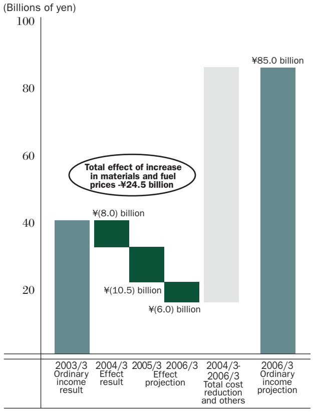
**Comparative Trends in Paper Imports/Exports**




(Sources: Compiled by Nippon Paper Group, Inc. Investor Relations, based on data supplied by Japan Paper Association, Japan Paper Exporter's and Importer's Association and The Japan Newspaper Publishers and Editors Association)

Note: Newsprint from Japanese manufactures' overseas operation is not included in imports.

**Effects of Raw Materials and Fuel Price Increases—Actual Results and Forecasts**




**Tree Farm Initiative**

**More than 100,000 hectares of afforested area by 2008**

**(Overseas Afforestation Area)**

| | |
|---|---|
| Australia | 61,600ha |
| Chile | 13,500ha |
| South Africa | 4,200ha |
| At the end March 2004 | 79,300ha |

### (3) Raw Material and Fuel Prices

The economies of Asian countries, in particular China, have come to exert considerable influence on world prices for raw materials and fuel. Wastepaper exports from Japan to China have increased substantially from the second half of fiscal 2003, tightening the supply/demand balance for wastepaper prices in Japan and spurring a significant rise in prices. In addition, prices for primary materials and fuels, such as coal, crude oil, pulp and woodchips, have increased across the board from the second half of fiscal 2004. As a result, Nippon Paper Group expects increased costs from higher prices to total ¥24.5 billion over the three years spanning from fiscal 2004 to fiscal 2006.

## Our Strategy

With rising raw material and fuel prices, the operating environment surrounding Nippon Paper Group is not conducive to an optimistic outlook. Nippon Paper Group aims to compensate for these higher cost factors by rationalizing its production facilities ahead of schedule and redoubling efforts to reduce expenses such as variable costs. To compete with imported paper and maintain market prices, Nippon Paper Group aims to reinforce its marketing structure and slash distribution costs while continuing to aggressively develop new and unique products toward attaining a firm lead in terms of quality and service.

In order to secure a stable source of raw materials and fuel, Nippon Paper Group is aggressively promoting its Tree Farm Initiative for overseas afforestation. Using our strength in biotechnology, we plan on developing high-yield timber adaptable to various climates and using these technologies in afforestation. In the area of domestic resources, we also aim to proactively use low-grade wastepaper, which had been difficult to recycle and reuse as paper until now. Moreover, Nippon Paper Group aims to reduce costs with the installment of a boiler and turbine that use waste such as paper sludge, used cut tires and construction scrap materials as an alternative to fossil fuels.

In order to expand corporate scale, Nippon Paper Group is seeking growth in Asian countries including China amid a slowdown in growth in demand for paper and paperboard in Japan. By transplanting machinery that has been suspended from use from restructuring in Japan to China, we are able to minimize cash outflow and increase the potential for establishing a position in the market there from an early stage. We plan to start a corrugating medium board business in the Shanghai region by the end of 2004 and an uncoated paper business in the Huabei region by the end of the first half of fiscal 2006.

# Aiming for Corporate Growth: From Business Integration to Full Merger

## 1st Stage: Realize Business Integration Effects (Fiscal 2002 - Fiscal 2003)

During the two years after Nippon Unipac Holding (currently Nippon Paper Group, Inc.) was established in March 2001, our first priority was to realize benefits from business integration between Nippon Paper Industries Co., Ltd. and Daishowa Paper Manufacturing Co., Ltd.

Through integration, we realized ¥56.5 billion in benefits during fiscal 2002 full year and fiscal 2003, mainly with cost reductions in materials procurement, production, distribution and financing. As a result of being able to control inventories through production adjustments after integration, we have succeeded in stabilizing paper prices, which has been a long-standing concern, despite weak demand after the collapse of the IT bubble in 2000.

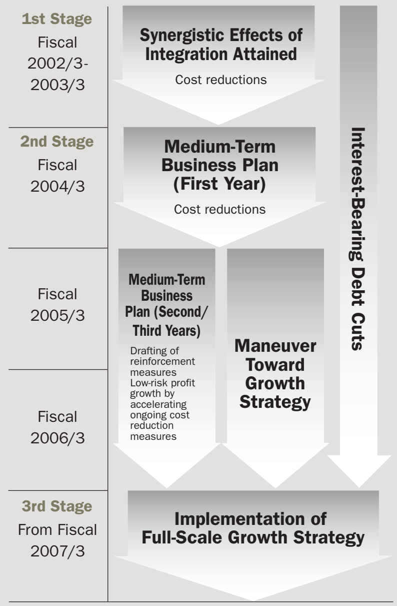
The early realization of integration effects during those two years and the stabilization of market prices has built our confidence and helped bring together the corporate cultures of the two predecessor companies. Accordingly, we believe that the merger and business reorganization in April 2003 was a success that produced tangible results.

## 2nd Stage (Part 1): Launch First Medium-Term Business Plan (Fiscal 2004)

In April 2003, we launched our First Medium-Term Business Plan to cover fiscal 2004 through fiscal 2006.

Under the First Medium-Term Business Plan, based on the slogan of “higher, faster and stronger,” Nippon Paper Group is promoting rationalization of production facilities and implementing measures to quickly realize synergy effects from business reorganization. The original goals of the plan were for consolidated ordinary income of ¥100 billion or more in fiscal 2006, along with a decrease in interest-bearing debt to ¥700 billion or less, and an increase in productivity of 10% or more. To achieve these targets, the Group foresaw the need to reduce costs by ¥60 billion by rationalizing production facilities, lowering material costs, improving manufacturing costs, improving financial balance and reducing labor costs.

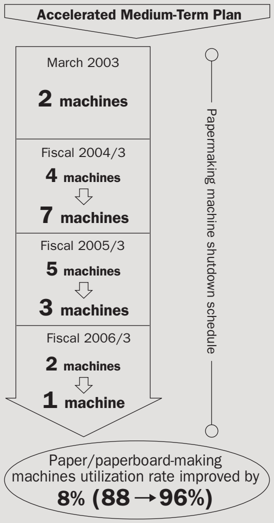
In rationalizing production facilities, Nippon Paper Group planned to shut down 13 low-efficiency papermaking machines and reduce labor costs, variable costs and depreciation. Moreover, the Group planned to promote unified raw materials and resource procurement to reduce procurement costs. At the same time, in improving manufacturing costs, we aimed to make capital investments that would reduce costs of raw materials and fuels, improve production efficiency and reorganize the distribution structure that would lower distribution costs. To improve its financial balance, the Group aimed to keep interest-bearing debt below ¥700 billion through stricter screening of capital investment. To reduce labor costs, the plan called for improved labor productivity through reductions in the number of group employees by approximately 2,300.




### Cost Reductions from Medium-Term Business Plan

| | |
|---|---|
| **Cost reduction by rationalizing production facilities**<br>• Associated with the shutting down of 13 papermaking machines and equipment reduction of deprecation, labor and variable costs | **¥14.0 billion** |
| **Acceleration of material procurement integration** | **¥7.0 billion** |
| **Cost improvements**<br>• Installation of more de-inked pulp lines<br>• Installation of generators that run on waste material<br>• Emergence of independent power production business<br>• Improvements in operational efficiency, yields, etc. | **¥17.0 billion** |
| **Distribution costs**<br>• Elimination of cross transportation through distribution system reorganization, etc. | **¥4.0 billion** |
| **Labor costs**<br>• Increase productivity by more than 10% | **¥12.0 billion** |
| **Result of reducing interest payment burden**<br>• Interest-bearing debt below ¥700 billion<br>• Rate cut | **¥6.0 billion** |
| **Total** | **¥60.0 billion** |

**Accelerated Rationalization of Production Facilities**




**Effects of Reinforcement Measures**

(Billions of yen)

| | Fiscal 2005/3 | Fiscal 2006/3 | Fiscal 2005/3-2006/3 Total |
|---|---|---|---|
| Variable costs reduction | 2.5 | 2.5 | 5.0 |
| Labor cost reduction | 2.0 | 3.0 | 5.0 |
| Sales reinforcement (Distribution and logistics cost reduction) | | 3.0 | 3.0 |
| Reinforcement measures total | 4.5 | 8.5 | 13.0 |

## 2nd Stage (Part 2): Operating Environment Changes and Reinforcement Measures under the Medium-Term Business Plan (Fiscal 2005 - Fiscal 2006)

In fiscal 2004, the first year of the Medium-Term Business Plan, the operating environment surrounding Nippon Paper Group underwent substantial change. One factor was rising prices for primary raw materials and fuels, which drove up costs by ¥8 billion in the first year of the plan. We expect price increases to add ¥16.5 billion in costs for fiscal 2005 and fiscal 2006.

As for sales, domestic market prices for paper slightly softened due to an increase in imports of coated printing paper and other factors, having a negative impact on the Group's earnings in fiscal 2004. In fiscal 2005, we are passing part of soaring material and fuel costs onto product prices and expect an improvement in operating conditions. However, it is impossible to absorb all negative factors.

In order to overcome these negative factors and further strengthen our international competitiveness, we announced reinforcement measures under the Medium-Term Business Plan in May 2004.

New measures for fiscal 2005 and fiscal 2006 are to reduce variable costs, lower overall labor costs, and to reinforce paper sales. Since we accelerated the rationalization of production facilities, we are capable of raising our targets for lowering variable costs and overall labor costs.

For reducing variable costs, our primary measures are to improve material composition by increasing the composition of de-inked pulp and reducing usage of market pulp. We expect cost reduction effects of ¥5 billion overall from reductions in chemical costs, improvements in yields and energy conservation, etc.

In an effort to reduce overall labor costs, we implemented special incentives for early retirement, and are increasing our labor reduction target from the initial 2,300 employees to 2,580 employees over the three years of the plan. Combined with the introduction of an early transfer system and the promotion of work contracts, we expect an additional ¥5 billion in cost reductions over the final two years of the plan.

To reinforce our paper sales, in July 2004 we implemented measures to rebuild Nippon Paper Industries Co., Ltd.'s paper sales organization and reinforce its functions. In particular, we integrated functions into two departments, one for commodity marketing for large-volume markets and the another for direct customer marketing for specialized products tailored to customer needs. We will promote information sharing among departments and greater authority for section managers to create a paper sales structure with vitality.

We are beginning to reorganize our sales channels. While it is difficult to change long-held sales practices over a short period of time, we aim to streamline our sales channels based on economical rationality.

We plan for an additional ¥3 billion in cost reductions by fiscal 2006 through reductions in distribution costs.

With the addition of these three cost reduction measures, namely lowering variable costs, reducing overall labor costs and reinforcing paper sales, we plan to reduce costs by an additional ¥13 billion over the final two years of the plan.

By the stepping up of cost reductions, we are now aiming for ordinary income of ¥85 billion and operating income of ¥90 billion in fiscal 2006, supported by the additional cost reduction measures in the Medium-Term Business Plan. Nippon Paper Group is continuing efforts to boost profitability in order to quickly attain the plan's original ordinary income target of ¥100 billion.

The First Medium-Term Business Plan is a running start toward creating a solid corporate foundation through cost reductions. We believe that most of the earnings improvements under the Medium-Term Business Plan are achievable through our own efforts. Even in a slow-growth operating environment, we believe significant profit growth is possible through selective investments and the efficient deployment of Group assets.

### 3rd Stage: Stepping-Stone to a Growth Strategy

The Japanese market is in a stable growth stage, and to achieve further expansion in profit and corporate value, we believe it is necessary to implement differentiation strategies for the domestic market and engage in full-scale business development overseas.

At our domestic facilities, we are steadily implementing the necessary measures to focus on main mills. After the First Medium-Term Business Plan ends, we aim to improve overall profitability by further concentrating production on our most competitive mills.

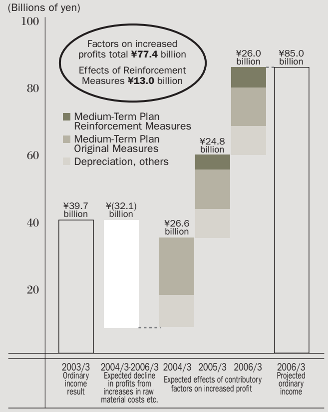
In addition, Nippon Paper Group aims to reinforce R&D activities to develop unique products through integrated efforts at mills, in research and marketing, and introduce products to market in a timely fashion.

To expand corporate scale, we are looking to enter overseas markets, especially the Chinese market. We aim to aggressively develop operations in China as the central focus of efforts to build a foundation there for future business development.

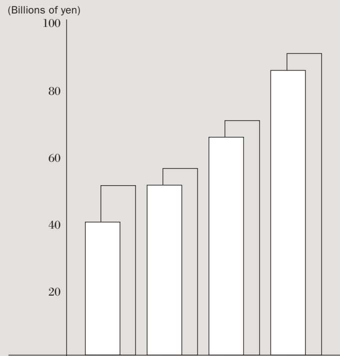
However, there are various risks, such as recovering invested capital, that accompany operations in China. While minimizing these risks, we believe an early entry into the market is a necessary first step in our Chinese business strategy. Our approach is to use existing facilities and sales networks through joint operations with local companies. We are aware of the significance of this approach and the urgency in quickly launching facilities in China, and to minimize cash outflow by transferring facilities to China that were made redundant by the rationalization of production facilities in Japan.

In the paper business, Nippon Paper Group established Nippon Paper Industries Chengde Co., Ltd. in Hebei Province, China, and plans to start paper production in the first half of fiscal 2006. We plan on making an investment in kind by transferring three paper machines with a total annual production capacity of 150,000 metric tons from the Shiraoi Mill of Nippon Paper Industries Co., Ltd. In 2005 production capacity for coated printing paper is expected to increase in the Shanghai area. Nippon Paper Group plans to fulfill a wide range of local needs while avoiding the risk of excessive competition by producing various uncoated paper such as, wood-free paper and groundwood paper in Hebei Province near Beijing.

#### Effects of Contributory Factors on Increase Profits over Three Years and Reinforcement Measures

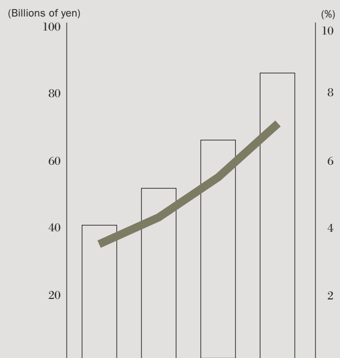



#### Operating Income/Ordinary Income



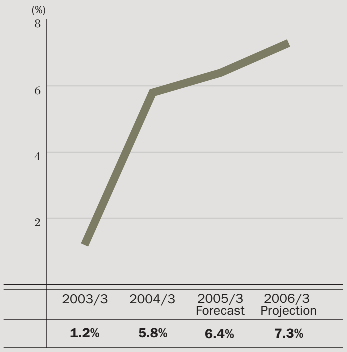

| | 2003/3 | 2004/3 | 2005/3 Forecast | 2006/3 Projection |
|---|---|---|---|---|
| □ Ordinary income | 39.7 | 50.7 | 65.0 | 85.0 |
| □ Operating income | 50.5 | 55.7 | 70.0 | 90.0 |

#### Ordinary Income/Ordinary Margin on Sales

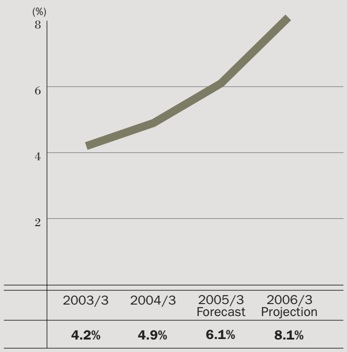



| | 2003/3 | 2004/3 | 2005/3 Forecast | 2006/3 Projection |
|---|---|---|---|---|
| □ Ordinary income | 39.7 | 50.7 | 65.0 | 85.0 |
| ■ Ordinary margin | 3.4% | 4.2% | 5.4% | 7.0% |

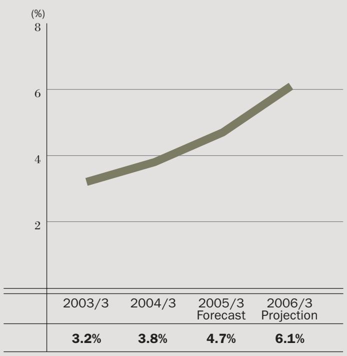
### ROE




### ROIC




### ROA




In the paperboard business, we are focusing on the strong growth in demand for corrugated board in Shanghai, and plan to produce and sell reinforced corrugating medium board, for which we expect latent demand. We aim to launch operations with a minimum of risk by transferring equipment from the former Japan Paperboard Industries' Kameari Mill with plans calling for the start of commercial operations by the end of 2004.

In addition, backed by its strengths in corrugated board manufacturing and liquid-packaging cartons, Nippon Paper Group aims to rapidly enter growth in these areas.

Although China is new territory for Nippon Paper Group, we aim to begin building a network of contacts in the country by sending our young employees there to accumulate experience and gather information in preparation for our full-scale growth strategy under the second Medium-Term Business Plan and beyond.

### Chinese Market / Low-risk Early Entry

| Company name | Area of business | Shareholding | 2003–2006 |
|---|---|---|---|
| Nippon Paper Industries Trading (Shanghai) Co., Ltd. | Imports/Sales | 100% | Commenced operations in the first half of fiscal 2005 (Liaison office for Chinese market) |
| Nippon Paper Industries Chengde Co., Ltd | Paper manufacture | 55%** | Agreement reached December 2003 → Establishment, construction and transfer in of equipment from the first half of fiscal 2005 → Commencing operations in the first half of fiscal 2006 (150,000 tons) |
| Zhejiang Jingxing Nippon Paper Co., Ltd. | Manufacture of corrugating medium board | 41%** | Founded September 2003 → Transferred in equipment in the first half of fiscal 2005 → Commencing operations in the second half of fiscal 2005 (150,000 tons) |
| Everwealth Paper Industries (Shanghai) Co., Ltd. | Corrugated board | 23% | Capital participation August 2003 |
| Elopak China Ltd. * | Manufacture of beverage cartons | 25% | Agreement reached December 2003 → Establishment and construction in the first half of fiscal 2005 → Commencing operations in the first half of fiscal 2006 |
| Shouguang Liben Paper Making Co., Ltd. | Manufacture of base paper for carbonless copying paper | 62% | Established December 1995 → Commenced operations January 1997 |

Full-scale entry

* Provisional name
** Investment-in-kind: Nippon Paper Industries Chengde Co., Ltd. Relocating Shiraoi Mill (Hokkaido) machine No's 2,4 and 5
Zhejiang Jingxing Nippon Paper Co., Ltd. Relocating No.5 machine from the former Kameari Mill

## Corporate Data (As of October 1, 2004)

| | |
|---|---|
| **Name** | Nippon Paper Group, Inc. |
| **Headquarters** | Shin-Yuraku-cho building 1-12-1 Yurakucho<br>Chiyoda-ku, Tokyo 100-0006, Japan<br>Tel: +81-(0)3-3218-9300<br>Fax: +81-(0)3-3216-5330 |
| **Date of Establishment** | March 30, 2001 |
| **Paid-In Capital** | ¥55,730 million |
| **Number of Employees** | 4 |

## Investor Information

| | |
|---|---|
| **Code No.** | 3893 |
| **Fiscal Year-End** | March 31 (The date shareholders who shall receive dividends are decided) |
| **Ordinary General Meeting of Shareholders** | Within three months from the day following the fiscal year-end |
| **Reference Dates** | March 31 for matters relating to the Ordinary General Meeting of Shareholders.<br>Reference dates for other matters, if necessary, shall be determined individually and announced in advance. |
| **Newspaper Where Public Notice Shall Be Made** | *Nihon Keizai Shimbun* |
| **Transfer Agent** | The Chuo Mitsui Trust and Banking Company, Limited<br>3-33-1 Shiba, Minato-ku, Tokyo, Japan |
| **Administrative Office of Transfer Agent (Mailing Address and Telephone Number for Inquiries)** | Stock Transfer Agency Department<br>The Chuo Mitsui Trust and Banking Company, Limited<br>2-8-4 Izumi, Suginami-ku, Tokyo 168-0063, Japan<br>Phone: +81-(0)3-3323-7111 |

* Please refer to the Transfer Agent at the following telephone number or website for the forms required for change of shareholder's address, purchase of broken lot shares, transfer of shares and designation of bank account to which dividend is to be remitted.

Toll-free : 0120-87-2031
URL : http://www.chuomitsui.co.jp/person/p_06.html

## Stock Information (As of March 31, 2004)

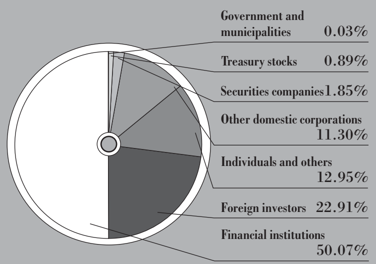
| | |
|---|---|
| **Total Number of Stocks Authorized to Be Issued** | 3,000,000 |
| **Total Number of Outstanding Stocks Issued** | 1,105,235.63 |
| **Number of Shareholders** | 64,658 |
| **Securities Traded** | Tokyo Stock Exchange, Osaka Securities Exchange and Nagoya Stock Exchange |
| **Independent Accountant** | Shin Nihon & Co. |

### Major Shareholders (10 Largest)

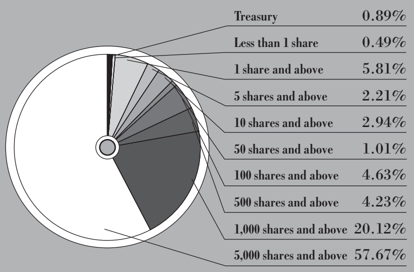
| | Number of Shares Held (Shares) | Voting Stake (%) |
|---|---|---|
| Japan Trustee Services Bank, Ltd. (Trust Account) | 85,816 | 7.9 |
| The Master Trust Bank of Japan, Ltd. (Trust Account) | 70,757 | 6.5 |
| Mizuho Corporate Bank, Ltd. | 42,314 | 3.9 |
| Nippon Life Insurance Company | 34,956 | 3.2 |
| Sumitomo Mitsui Banking Corporation | 23,876 | 2.2 |
| Mitsui Mutual Life Insurance Company | 22,589 | 2.1 |
| Mizuho Bank, Ltd. | 21,467 | 2.0 |
| The Chuo Mitsui Trust and Banking Company, Limited | 20,242 | 1.9 |
| Daio Paper Corporation | 20,241 | 1.9 |
| The Chase Manhattan Bank, N.A. London | 19,096 | 1.8 |

1. Shares held less than one share have been omitted
2. Mitsui Mutual Life Insurance Company became Mitsui Life Insurance Co., Ltd. on April 1, 2004

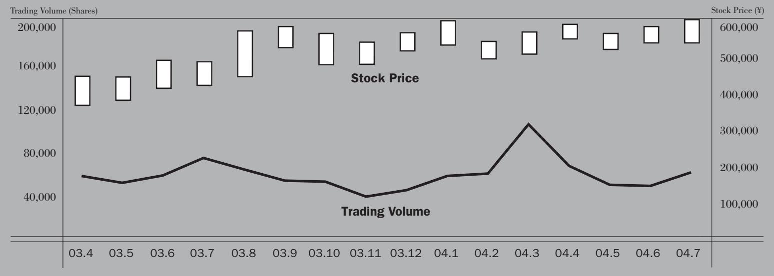
### Percentage of Shares Held by Shareholder Type




### Percentage of Shares Held by Size of Holdings




### Stock Price and Trading Volume



NIPPON PAPER GROUP

NIPPON PAPER GROUP, INC.

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Text: Nippon Paper Industries "U-LITE" 157g/m²
"OPERA CREAM ZEUS" 115g/m²

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