



NIPPON PAPER GROUP, INC.

ANNUAL REPORT 2005

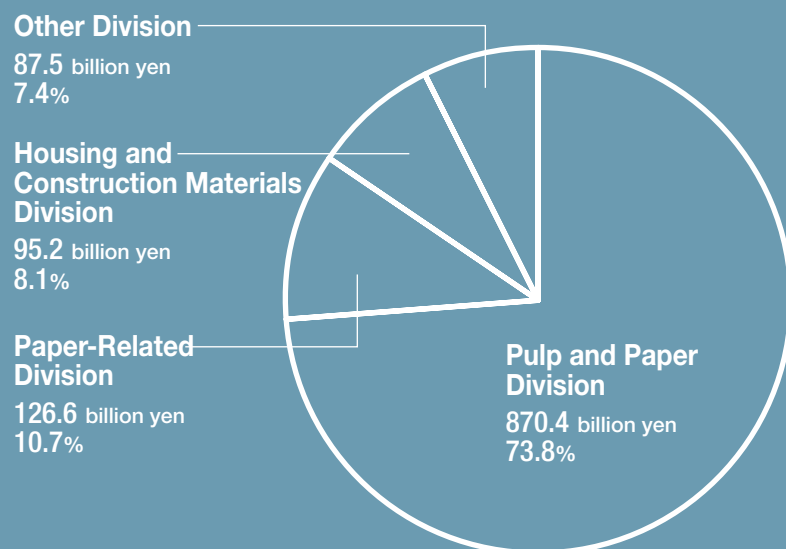
For the Fiscal Year Ended March 31, 2005

NIPPON PAPER GROUP, INC.



Nippon Paper Group, Inc. is the pure holding company for the Nippon Paper Group, which comprises Nippon Paper Industries Co., Ltd., Nippon Daishowa Paperboard Co., Ltd., and their 150 subsidiaries and 52 affiliated companies. Engaged in recycling-oriented businesses in symbiosis with the communities in which it serves, Nippon Paper Group, as a corporate group that underpins a wide range of culture and industries, has been committed to continually and actively contributing to society. Nippon Paper Group will endeavor to fulfill its corporate social responsibility, which includes the highest standards in ethics, fairness and transparency, and continue to serve society as an excellent company.

Sales Composition by Business Segment
(FY2004*)



* To achieve consistency with fiscal years used in Japanese reports, the fiscal year ended March 31, 2005 will be known as fiscal 2004 (fiscal year 2004) and the fiscal year ending March 31, 2006 will be known as fiscal 2005 (fiscal year 2005) throughout this annual report. All references to prior and future fiscal years have been restated accordingly.

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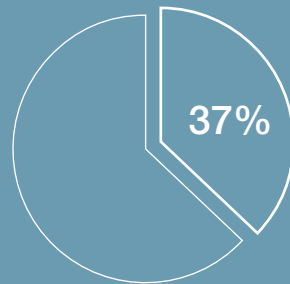
Nippon Paper Group's Production Share and Ranking in the Japanese Market (2004)

Newsprint

Production **1,374** thousand tons

Estimated share **37%**

Ranking **1**

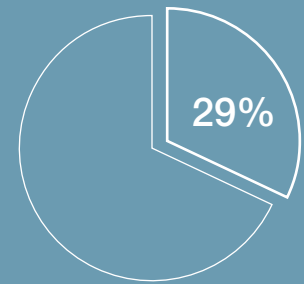


Printing paper

Production **2,814** thousand tons

Estimated share **29%**

Ranking **1**

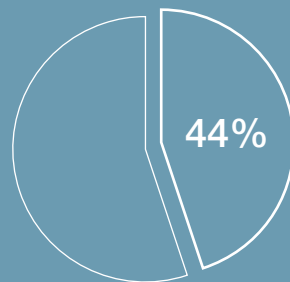


Business communication paper

Production **722** thousand tons

Estimated share **44%**

Ranking **1**

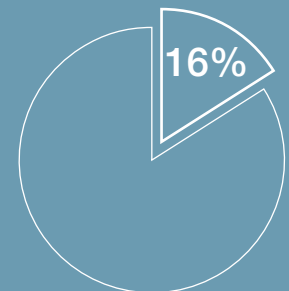


Paperboard

Production **1,940** thousand tons

Estimated share **16%**

Ranking **3**



Consolidated Financial Highlights

	Millions of yen			Thousands of U.S. dollars ¹
	FY2002 April 1, 2002 - March 31, 2003	FY2003 April 1, 2003 - March 31, 2004	FY2004 April 1, 2004 - March 31, 2005	FY2004 April 1, 2004 - March 31, 2005
Net sales	¥1,165,450	¥1,192,649	¥1,179,696	\$11,025,196
Operating income	50,450	55,679	65,231	609,636
Ordinary income	39,671	50,665	62,801	586,925
Net income	4,880	24,258	24,350	227,570
Total assets	1,630,126	1,637,366	1,529,975	14,298,832
Total shareholders' equity	408,202	429,621	442,876	4,139,028
Interest-bearing debt ²	851,311	842,278	766,139	7,160,178
	Yen			U.S. dollars
Net income per share	4,283.53	22,025.22	21,996.96	205.58
Cash dividends per share	8,000.00	8,000.00	8,000.00	74.77
Operating income to net sales (%)	4.3	4.7	5.5	
Return on equity (ROE) (%) ³	1.2	5.8	5.6	
Return on invested capital (ROIC) (%) ⁴	4.2	4.9	5.9	
Equity ratio (%)	25.0	26.2	28.9	
Return on assets (ROA) (%) ⁵	3.2	3.8	4.7	
Number of employees	15,662	14,987	13,774	

(Notes) 1. Amounts in U.S. dollars are included solely for the convenience. The rate of ¥107 = U.S.\$1.00, the approximate rate of exchange in effect on March 31, 2005, has been used.

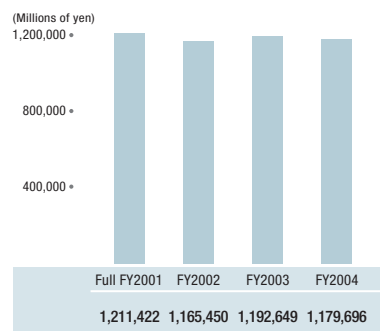
2. Interest-bearing debt = Short-term borrowings + Long-term debt

3. Return on equity (ROE) = Net income / Average shareholder's equity × 100

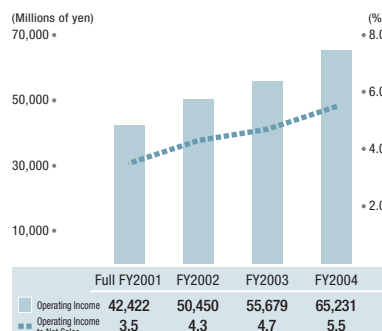
4. Return on invested capital (ROIC) = (Ordinary income + Interest expense) / (Total shareholder's equity + Interest-bearing debt) × 100

5. Return on assets (ROA) = (Ordinary income + Interest expense) / Total assets × 100

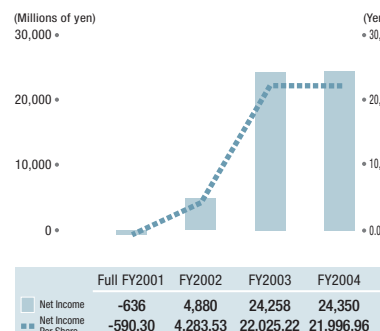
Net Sales



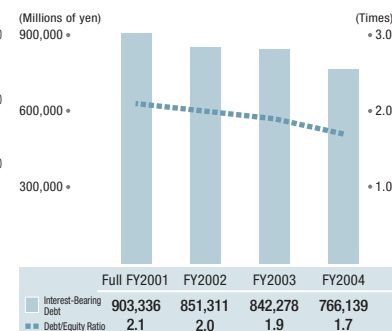
Operating Income and Operating Income to Net Sales



Net Income (Loss) and Net Income (Loss) Per Share



Interest-Bearing Debt and Debt/Equity Ratio



*Full fiscal year 2001 is the total of the first accounting period (from March 30, 2001 to September 30, 2001) and the second accounting period (from October 1, 2001 to March 31, 2002).

To Our Shareholders



In May 2005, the Nippon Paper Group announced its Group Vision 2015. It sets forth the goals that the Group intends to achieve by 2015, and provides guidance for the management of the Group. Viewed from a global perspective, the paper industry is a growth field with abundant business opportunities. The Nippon Paper Group enjoys a favorable location, Japan, which has rapidly growing Asian markets as its neighbors and a sophisticated domestic market where we are laying the ground for an expected expansion of earnings. With paper and paperboard as its core business, the Nippon Paper Group will fully employ its management resources to survive in today's tumultuous business environment amid fiercer, future international competition, while working for growth and increased shareholder value.

As an element in realizing the goals of Group Vision 2015, we renewed the top-management team in June 2005. During fiscal 2005, we will pour our efforts into formulating the Second Medium-Term Business Plan as the starting point of Group Vision 2015, and we will incorporate effective measures at the earliest timing possible into the plan. We will exert ourselves to the utmost to meet shareholder expectations by creating corporate value.

M. Nakamura

MASATOMO NAKAMURA
President
Nippon Paper Group, Inc.

T. Miyoshi

TAKAHIKO MIYOSHI
Chairman of the Board of Directors
Nippon Paper Group, Inc.



Review of Performance in Fiscal 2004*

*the fiscal year ended March 31, 2005

There were a number of noteworthy events in fiscal 2004. In October 2004, Nippon Paper Industries Co., Ltd. began operating thermal-recycling power generation facilities, which use wood scrap as their primary fuel, at the Nakoso Mill. In October, Nippon Paper Industries entered the independent power production (IPP) business at its Kushiro Mill, a new field of business for the Company. At the end of January 2005, Chinese joint venture Zhejiang Jingxing Nippon Paper Co., Ltd. began commercial production of

corrugating medium. In April 2005, we decided to withdraw from a joint venture business that had begun construction of a paper mill in northern China.

Fiscal 2004 was the second year of the First Medium-Term Business Plan, and the consolidated earnings of the Nippon Paper Group showed growth. Net sales declined by ¥12.9 billion, or 1.1%, to ¥1,179.7 billion, but operating income grew ¥9.5 billion, or 17.2%, to ¥65.2 billion, ordinary income increased ¥12.1 billion, or 24.0%, to ¥62.8 billion, and net income rose ¥100 million, or 0.4%, to ¥24.4 billion. This marks the third consecutive year of growth in earnings since the business integration of 2001, and manifests the Group's ability to achieve steady earnings growth.

The prices of woodchips, heavy oil, and coal rose steeply, and prices for paper and household tissue fell, putting substantial pressure on earnings. The Group pushed forward with self-help measures, centering on the reinforcement measures of the First Medium-Term Business Plan. These included the reduction of labor costs through the implementation of an early retirement program, variable costs such as energy cost, and distribution costs. This allowed the Group to absorb the rising costs of raw materials, and to achieve record-high ordinary income.

Domestic demand for paper is forecast to remain strong in fiscal 2005, while the prices of woodchips, heavy oil, coal, and other raw materials and fuels are forecast to hover or rise further. By working to absorb these through reductions in manufacturing costs and other self-help measures, we anticipate another record on an ordinary income basis.

In this final year of the First Medium-Term Business Plan, we will complete the elimination of unneeded capacity and redundant personnel, and will reduce interest-bearing debt to our original target levels, creating a corporate structure that is capable of achieving growth in any business environment. Moreover, we will aim at increasing corporate value through formulating our Second Medium-Term Business Plan, an action plan for long-term earnings growth, which will start in fiscal 2006.

Four-year Performance Trends Following Business Integration

	(Billions of yen)			
	Full FY2001*	FY2002	FY2003	FY2004
Net sales	1,211.4	1,165.5	1,192.6	1,179.7
Operating income	42.4	50.5	55.7	65.2
Ordinary income	28.6	39.7	50.7	62.8
Net income (loss)	(0.6)	4.9	24.3	24.4

*Full FY2001: From March 30, 2001 to March 31, 2002

The Business Environment and Outlook

Introduction—The Reorganization of the Domestic Pulp and Paper Industry

>> The era of excessive competition

Demand for paper and paperboard in Japan has risen steadily in tandem with growth in GDP. Domestic paper manufacturing was not seriously eroded by imports, but instead increased. During the era when there were many medium-sized paper manufacturers, though, oversupply often drove prices down as these mid-size companies expanded production capacity whenever the industry approached an appropriate supply-and-demand balance. This vicious cycle was repeated time and again.

>> The era of two major manufacturers

Taking the opportunity presented by the 1993 birth of Nippon Paper Industries, the industry moved forward with sweeping reorganization. With the 2001 business integration of Nippon Paper Industries and Daishowa Paper Manufacturing, the Nippon Paper Group was formed and emerged, along with the Oji Paper Group, as the two major manufacturers. The current industry structure, with both groups leading the paper sector and with the Rengo group active in the paperboard sector, has resulted in price stability with inventories maintained at appropriate levels. The price of paperboard recovered in the second half of 2003 and has since remained steady. Imported products weakened the paper market, but the decline was extremely slight in comparison to previous drops. In addition, the industry succeeded in restoring price levels at the end of 2004.

>> Outlook

As outlined above, the Japanese pulp and paper industry appears to have entered a period of stability; however, a number of hurdles remain to be surmounted. These include the leveling off of demand, increasing imports, and soaring material costs. I think, therefore, that yet another reorganization of this industry's manufacturers is needed.

Severe conditions persist in the paper-distribution sector, as a number of distribution firms engage in senseless price wars, and distributors themselves have begun to take measures toward reorganization to survive. Our two principal paper agents, OKURA SANKO CO., LTD. and THE OKAMOTO CO., LTD., will merge in October 2005 to form SHINSEI PULP&PAPER COMPANY LIMITED. Further reorganization will strengthen the competitiveness of the pulp and paper industry as a whole.

I would like to briefly discuss four areas regarding the changes in the business environment that have provided the background for the aforementioned trends and will serve as the basis for our strategy to be mentioned later. Namely, these are the 1) macroeconomic environment, 2) supply and demand for paper and paperboard, 3) imports, and 4) prices of raw materials.

Outlook for the Macroeconomic Environment

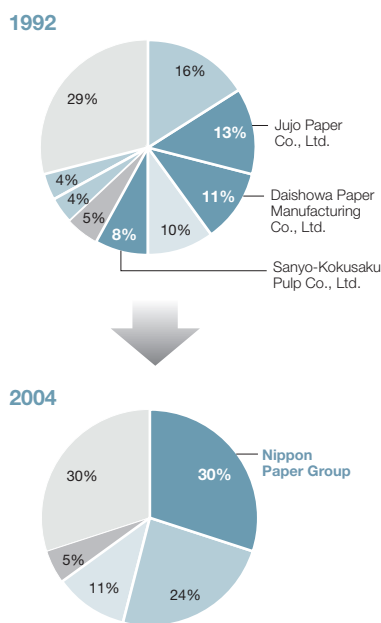
>> Stabilization in Japan

Following the collapse of the bubble economy at the beginning of the 1990s, conditions in the Japanese economy remained extremely adverse. The IT bubble of 2000 collapsed in just a year, and conditions again took a turn for the worse, but around the second half of 2003 signs of full-scale recovery began to appear. Supported by the Olympics and other events, the recovery gained strength in 2004. There was a bit of a plateau in the second half, but corporate earnings took an upswing as Japanese banks drew closer to completing the write-off of bad debts. This improvement in fundamentals is expected to spread gradually to the domestic budget and usher in long-term recovery. Japan's population is forecast to begin declining in 2007, resulting in stable but low growth of around 2% in real GDP.

>> World economy steady, sustained high growth in China

The world economy is sustaining a comparatively high growth rate. Although the U. S. is having problems with its budget deficit, its economy is being fueled by consumer

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)

spending and remains steady. Growth of about 3% is forecast. Economic growth is striking in some emerging nations, including Brazil, Russia, India, and China (BRICs). China has in recent years achieved extremely high rates of growth, and in the run up to the 2008 Beijing Olympics and the 2010 Expo is expected to sustain annual growth of approximately 8%.

Supply and Demand for Paper and Paperboard in Japan, China, and the World

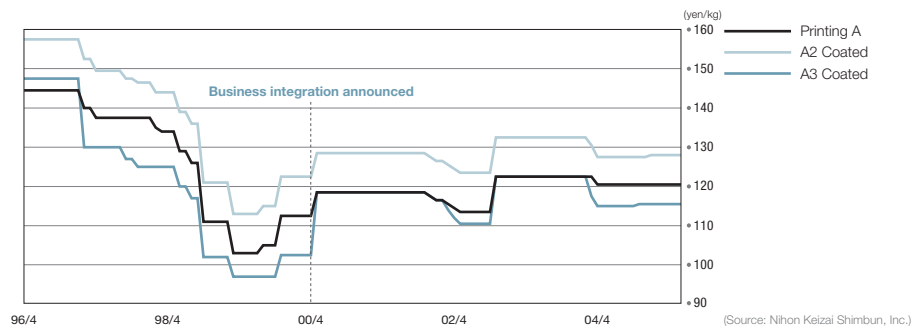
>> Worldwide expansion of manufacturing and consumption—future focus will be China, other Asian countries

The volume of world paper and paperboard consumption is growing steadily, and the pulp and paper industry can be regarded as a growth industry. It is undeniable that markets are reaching maturity in North America, Western Europe, and other advanced countries where major growth in volume cannot be expected. However, consumption of paper and paperboard is growing rapidly in the emerging nations of Asia, Eastern Europe, and South America where economic growth has in recent years been striking. China has already become the world's second-largest market but has significant room for growth, with per capita consumption reaching only 42kg per year in 2004 according to the China Paper Association. If consumption continues to grow rapidly, in tandem with economic expansion, in ten years the scale of this market will exceed 100 million tons. The creation in such a short time of a market on that scale—larger than Japan's, currently the world's third largest—will have an immense effect on the world supply-and-demand balance.

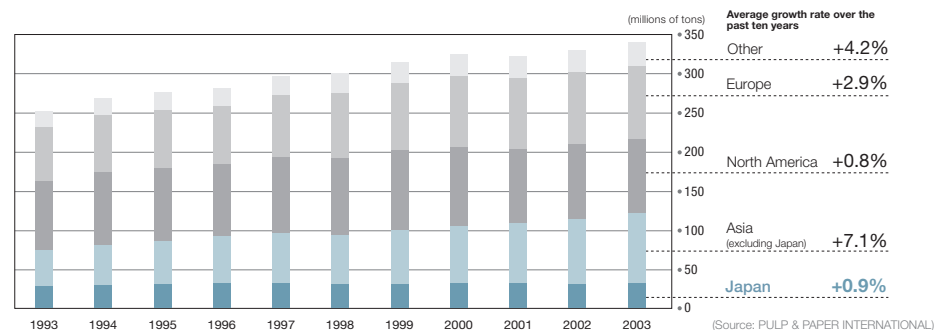
>> Japan's domestic demand stabilizes

As with other advanced countries, Japan's paper and paperboard market is maturing. The average growth rate over the past 10 years was a low 0.9%. Paperboard averaged only 0.3% growth, which is virtually flat. Reductions in usage of packaging materials, an increase in imported vegetables, and demand for lighter packaging

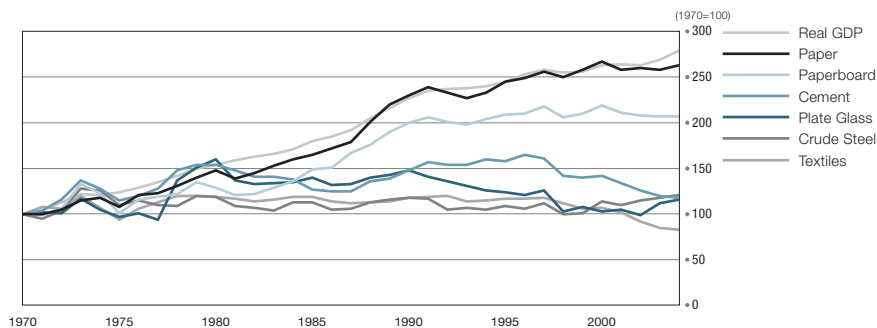
Paper Price Trends



Paper and Paperboard Consumption by Geographical Region

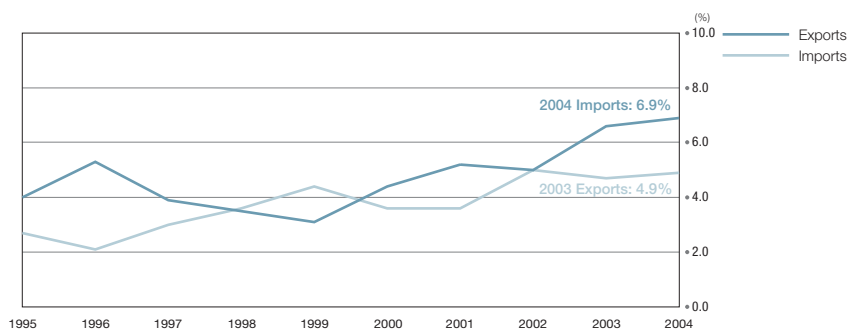


Growth Trends by Material



(Sources: Ministry of Economy, Trade and Industry, "Preliminary Report on Paper, Pulp, Plastics Products and Rubber Products Statistics", "Preliminary Report on Ceramics and Building Materials Statistics", "Preliminary Report on Iron and Steel, Non-ferrous Metal and Fabricated Metals Statistics", "Preliminary Report on Textiles and Consumer Good Statistics", Economic & Social Research Institute)
Note: Real GDP from 1970 to 1979 is calculated roughly.

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 manufacturers' overseas operation is not included in imports.

materials all had negative effects. A sudden drop, however, is not likely while corrugated board retains its superiority as a packaging material. Driven by its cost competitiveness as well as concerns for environment, shifts from other materials can be observed. Growth in paper has been 1.8%, virtually the same as GDP growth. The volume of shipments of printing paper and business communication paper was at an all-time high in 2004, and forecast to grow gradually thereafter as demand shifts from uncoated paper to coated paper.

Electronic paper, electronic books, and other forms of new information display appear still to be in the testing stage. Paper offers ease of viewing, allows high-volume distribution at low cost, and can be stored for long periods of time. The color and texture of paper used to print a book can become a part of the book's message. It is necessary to keep an eye on trends in new media, but the various properties and characteristics of paper will allow it to co-exist with them.

Paper and Paperboard Imports and Exports

>> Imports now at all-time high

In the second half of the 1990s, PPC imports began to rise sharply, and in 2004 held a 33% share of the Japanese market. In addition, following the increase in the price of printing paper in autumn 2002, some customers began turning to imports for these products, and in 2003 there was a sharp increase in the use of coated paper imports. The use of imported coated paper continued to rise in 2004, and has reached an all-time high.

>> Outlook: Market penetration by imports will be limited over the long-term

The increase in imports in recent years is drawing attention, but a broader view reveals that the weight of imports and exports (excluding imports of newsprint by domestic manufacturers) in 2004 remained at low levels, 6.9% and 4.9% respectively, offsetting each other. Logistics costs for paper and paperboard are high in comparison to their added value, and domestic products better meet the needs of domestic customers for meticulous services and

differentiated products. While the rush to expand manufacturing facilities in China may temporarily result in a substantial supply-and-demand imbalance, over the long-term market penetration by imports will be restricted to some commodity grades and limited in volume.

>> An emerging risk: Increasing borderlessness

The movement of commodity grade products is becoming increasingly borderless, and prices will be converging on "East Asian market prices." This means that we need to look at the possibility of prices falling below their current domestic levels.

Trends in Prices of Fuel and Raw Materials

>> Current status: Growth in China sustains a tight supply-and-demand balance

The effects of China's economic growth on the balance of fuel and raw material supply and demand cannot be disregarded. Their development into a motorized society and growing demand for electricity are driving unprecedented increases in the prices of petroleum and coal worldwide. In addition, the fast and furious expansion of paper and paperboard manufacturing facilities has resulted in tight supply-and-demand for fiber. This is also affecting Japan's domestic industry. An increase in wastepaper exports to China beginning in the second half of fiscal 2002 has driven prices up substantially. Woodchip markets are relatively stable in areas that are outside the reach of China's manufacturers, such as South America, South Africa, and Oceania, but in Southeast Asia prices are rising. The rush to expand pulp manufacturing facilities in South America is advancing, making the forecast of pulp prices extremely difficult.

>> An emerging risk: Sustained high prices for raw materials and fuel

As manufacturing and consumption in China continue to rise, it is necessary to consider that this may keep prices for raw materials and fuel at high levels.

Our First Medium-Term Business Plan

In April 2003, two years after business integration, we launched the First Medium-Term Business Plan to cover fiscal 2003 through fiscal 2005.

The goals of the First Medium-Term Business Plan, based on the slogan of "higher, faster and stronger," were to achieve consolidated ordinary income of ¥100 billion or more in fiscal 2005, 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 goals, the Group formulated and executed the measures below.

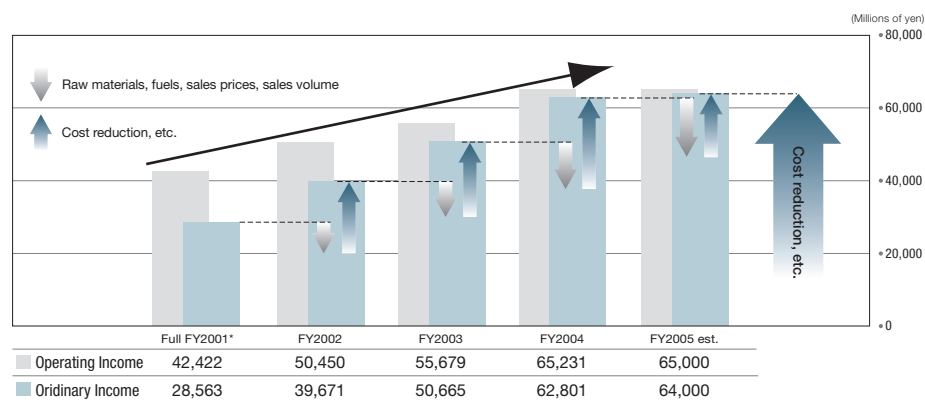
>> Eliminate unneeded production capacity

Rebuild the manufacturing structure companywide; shut down 13 low-efficiency papermaking machines to reduce labor costs, variable costs, and depreciation.

>> Reduce costs

Move forward with reductions in total costs; promote unified purchasing management of supplies and raw materials to reduce procurement costs; make capital investments to reduce input cost and improve production efficiency; reorganize logistics systems to eliminate redundancy.

Improving Profitability and Financials through Cost Cutting



*Full FY2001: March 30, 2001-March 31, 2002



>> Reduce liabilities

Secure free cash flow through stricter screening of capital investments; reduce interest-bearing debt to below ¥700 billion; improve the financial account balance.

>> Reduce the labor force

Reduce Group employees by approximately 2,300; improve labor productivity.

Reinforcement Measures Under the Medium-Term Business Plan, and Status of Implementation Through Fiscal 2004

In the first year of the Medium-Term Business Plan, the business environment surrounding Nippon Paper Group underwent substantial change. The greatest factor was rising prices for primary raw materials and fuels, which drove up costs by ¥8 billion in fiscal 2003 and ¥8.3 billion in fiscal 2004. We expect price increases to add substantially to costs for fiscal 2005.

To overcome these negative factors and establish a solid revenue base, we announced reinforcement measures under the First Medium-Term Business Plan in May 2004. These include reducing variable costs, lowering overall labor costs, and reinforcing paper sales.

With regard to variable costs, improvements in material composition, yields, and energy conservation to result in lower unit variable cost and unit energy cost.

To reduce overall labor costs, we implemented special incentives for early retirement and early transfer systems, and are moving forward with measures to promote a shift to contract employment.

To strengthen our paper sales system, in July 2004 we implemented measures to rebuild our paper sales organization of Nippon Paper Industries and bolster its functions.

Specifically, we integrated four sales departments into two departments, one to handle commodity marketing in large-volume markets, and the other to have charge of direct customer marketing of differentiated products tailored to customer needs.

Despite the initial and additional measures described above, progress toward the goals of the First Medium-Term Business Plan in fiscal 2004 was hindered not only by rising prices for raw materials and fuel, but also by price competition in the household tissue market that resulted in a substantial decline in the earnings of our household tissue business. As a result, our performance was below our target. At the same time, we pressed forward with self-help measures to reduce costs and dealt with changes in the external environment.

Measures taken to strengthen our corporate structure have resulted in extraordinary losses of ¥14.1 billion in fiscal 2003, and ¥16.0 billion in fiscal 2004. These were primarily composed of losses on disposal of fixed assets in connection with the rebuilding of our manufacturing structure, and supplementary retirement benefits paid in connection with our establishment of the early retirement program.

These extraordinary losses are transient costs incurred in the course of strengthening our revenue base, and indicate that measures called for in our First Medium-Term Business Plan to strengthen our corporate structure—including reductions in facilities, personnel, and interest-bearing debt—are advancing steadily.

Outlook for Fiscal 2005

In fiscal 2005, the adverse effects of the continued increase in prices of raw materials and fuels are forecast to be even stronger than in fiscal 2004. We expect the prices of heavy oil and woodchips to have a particularly strong effect on the Nippon Paper Group. In anticipation of this, we are proceeding with self-help measures intended to reduce production costs and shrink labor costs.

Buoyed by the Olympics and other major events, domestic demand for paper took an upturn in fiscal 2004, and the Group forecasts an increase in sales volume as a result of the growth in domestic demand. In the second half of 2004, finding itself unable to cover the soaring costs of raw materials and fuel through cost reductions, the Group adjusted the prices of its printing and business communica-

tion paper in an effort to pass some of these costs on to the user. As the top firm in this industry, we will continuously seek to maintain appropriate sales prices.

As a result of earnings increases that more than offset the negative effects of changes in the business environment, the Group forecasts that fiscal 2005 will see a record high in ordinary income for the second consecutive year.

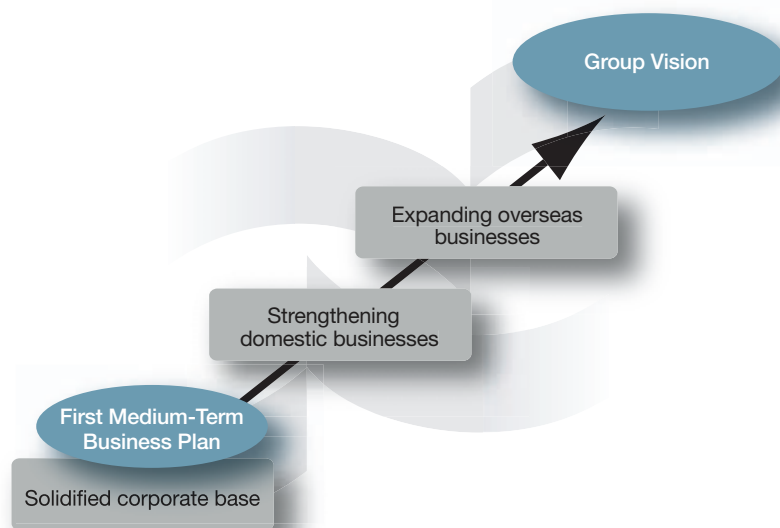
As a result of the downward pressure on profits exerted by the rising prices of raw materials and fuel, the Group is on a slightly longer track to reach the ¥100.0 billion ordinary income target set in the First Medium-Term Business Plan. However, we expect to reach our goals of reducing interest-bearing debt to below ¥700.0 billion and raising productivity by ten percent, as originally planned. We will exert ourselves to the utmost to attain those targets in fiscal 2005, and to strengthen our revenue base, and under our Second Medium-Term Business Plan will move forward with further measures to increase profitability and execute growth strategies.

Group Vision 2015

The Making of Group Vision 2015

Group Vision 2015 was formulated in May 2005 to provide a vision of the Group's position ten years in the future, to share our philosophy with all the companies of the Group, and to guide us all on the same vector into the future. Looking at the paper industry worldwide, it is a growth industry rife with business opportunities. Paper and paperboard is the Nippon Paper Group's core business, and it must overcome international competition that will only intensify in the future. The Group must continually heighten its corporate value. This will require strengthening its domestic business by enhancing cost competitiveness to secure stable earnings, while advancing into overseas markets and expanding through M&A. This is the central theme of Group Vision 2015. The Group has set a goal of becoming one of the top five pulp and paper firms in the world by 2015.

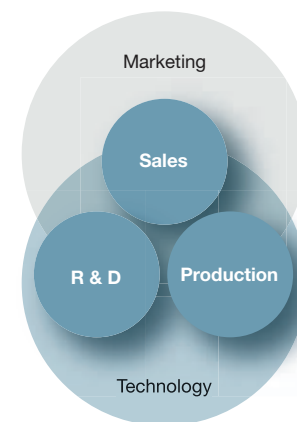
Making of Group Vision 2015



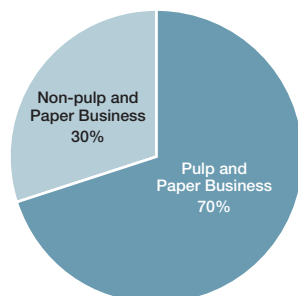
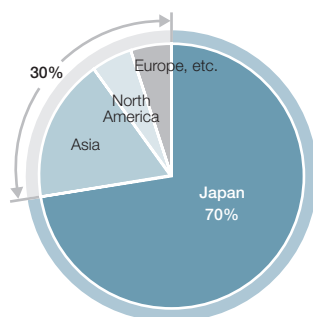
Fundamental Strategies in Group Vision 2015

One fundamental strategy described in Group Vision 2015 is a market strategy that calls for the Group to remain ahead of its competitors by employing original technology and the Group's expertise in new product development to assemble the strongest, deepest product lineup in the industry. Nippon Paper Industries is ahead of its competitors in the development and marketing of low-density paper, which has gained user acceptance. Our frontline sales powerhouse will strive to know customers needs earlier than any other rivals, and our strongest production site will produce the products that meet the needs.

We believe that the mission of the manufacturing industry is to provide a stable supply of good products at appropriate prices. The Group's main paper mills are highly cost competitive, and maintain exacting standards in both shipping and quality assurance. In the future we will employ the strength of our user-accepted quality and service in our marketing strategy. However, in recent years a growing number of users have been turning toward inexpensive,



Sales Portfolio of 2015



imported commodity grade products. In addition to quality and service, we must develop increased international competitiveness in the realm of cost.

To achieve corporate growth, which is to say expansion in scale, it is important to secure both raw materials and energy resources. It is necessary to build a system for stable and competitive procurement of the raw materials and fuels that are needed to keep up with the growth in the Asian markets.

Business Issue—Strengthening Domestic Business

In our domestic paper business, the strengthening of our manufacturing structure and distribution is an important issue. Under the First Medium-Term Business Plan we moved forward with the rebuilding of our manufacturing structure, and are working to achieve higher cost competitiveness. The Nippon Paper Group's paper business commands the top share of the domestic paper market, where competition with imports has already become fierce in some grades as mentioned previously. We are formulating a strategy based on dividing products into categories, such as grades with high growth potential that are likely to be imported; grades with low growth potential but high profitability, and specialty grades that are unlikely to be imported, and will move forward with the concentration of manufacturing on this basis. Scrap and build is also an option. While concentrating manufacturing, we are establishing the optimum domestic paper manufacturing structure.

The Nippon Paper Group has a number of paper mills at coastal locations, and the cost advantage this confers in the domestic market is another of the Group's strengths. Japan's pulp and paper industry is largely dependent on overseas procurement of raw materials and fuels. However, location and product mix result in differences in competitiveness among our mills. On the basis of fundamental competitiveness, we have divided our mills into core mills, potential core mills, and mills requiring corrective measures, and are investing management resources accordingly. At

core mills, we are ensuring the cost competitiveness needed to survive international competition. We are strengthening operations at potential core mills to allow them to precisely meet the needs of the domestic market and secure stable earnings. Among the mills requiring corrective measures—such as those with issues related to location, facilities, growth potential, and other fundamentals—we will also pursue drastic cuts in fixed costs. In addition, we will consider the consolidation of some mills based on their earnings situation.

To enhance cost competitiveness, we are already moving forward with reductions in our use of increasingly costly fossil fuels. We have completed and are advancing the installation of a number of boilers fueled by biomass and waste, and are anticipating expanded utilization of these with the building of a biomass and waste fuel procurement system. In addition, we are securing stability in woodchip procurement by expanding our afforestation program.

Regarding the strengthening of distribution, the reorganization of the paper distribution industry is underway as discussed previously. We are building an efficient distribution network that will be responsive to trends in user needs, distribution modes, product types, and our competitors. The Group will achieve efficiency in logistics and establish a competitive advantage in total costs from manufacturing through sales.

The paperboard business is a small part of the Group's entire operation, and we intend to expand the scale of these operations through M&A, and make them a significant source of earnings. One step will be strengthening the corrugated board business, a downstream sector of the paperboard business, to heighten the profitability of the paperboard and corrugated board business overall. In the household tissue business, we will be expanding operations in the field of adult care products and incontinence products.

We have other businesses such as the liquid-packaging cartons business, the chemical products business, and the lumber business. Each of these has its individual strengths and technologies, and we are fostering these operations to

become able to make a contribution to the corporate growth of the Nippon Paper Group and the stability of its domestic high-earnings structure. To that end, we are considering M&A in these areas and the forging of alliances outside our industry.

Business Issue—Strengthening Overseas Operations

Today the Nippon Paper Group is pressing forward with the expansion of operations in three major markets: Asia, North America, Europe, and will continue to emphasize growth in these regions. Our plan is to increase the contribution of overseas operations to the Group's net sales to 30% after ten years.

The Asian markets, and particularly China's, are important when we aim for growth in scale. Because of our decision to withdraw from a joint venture business in northern China, our paper business as yet has no prospects for local manufacturing operations in that country. However, we will be focusing on the development of a customer base and a marketing network through our Shanghai subsidiary, Nippon Paper Industries Trading (Shanghai) Co., Ltd., and are now considering the question of the optimum production site. In the paperboard business, Zhejiang Jingxing Nippon Paper Co., Ltd. commenced operations in January 2005. In China, we will expand the local manufacturing and sales of the paperboard business, including the corrugated board business, preceding the paper business.

In North America, the Nippon Paper Group is employing its technological expertise to expand the volume of local sales and increase its presence in this market. In Europe, we have already decided to double the production capacity of our thermal paper business, and established Nippon Paper Industries' Europe Office to expand sales of high-value-added products, and seek business opportunities through information gathering as well as to support the expanded thermal business.

Company Scale and Performance Targets for 2015

Consolidated sales turnover	1.5 – 2 trillion yen
Consolidated operating income	100 billion yen domestically (with stability) + Operating income from overseas business
Consolidated operating income to net sales	8 – 10%
Business portfolio	Domestic business 70%, Overseas business 30% Pulp and paper business 70%, Non-pulp and paper business 30% Business expansion into three key markets -Asia, North America, and Europe
Aggregate market value	1 trillion yen
Cash flow	150 billion yen

The Nippon Paper Group's target position for 10 years into the future is shown in the table above. To be ranked in the top five, we must not only grow beyond our present scale, but also bring profitability to a high level, and generate healthy cash flows. We would like to see these improvements in the quality of the Group be reflected in aggregate market value.

In this unsettled business environment, the entire Nippon Paper Group will make maximum use of its strengths in an effort to achieve sustained growth. We will strive to ensure returns to shareholders and other stakeholders through corporate growth.

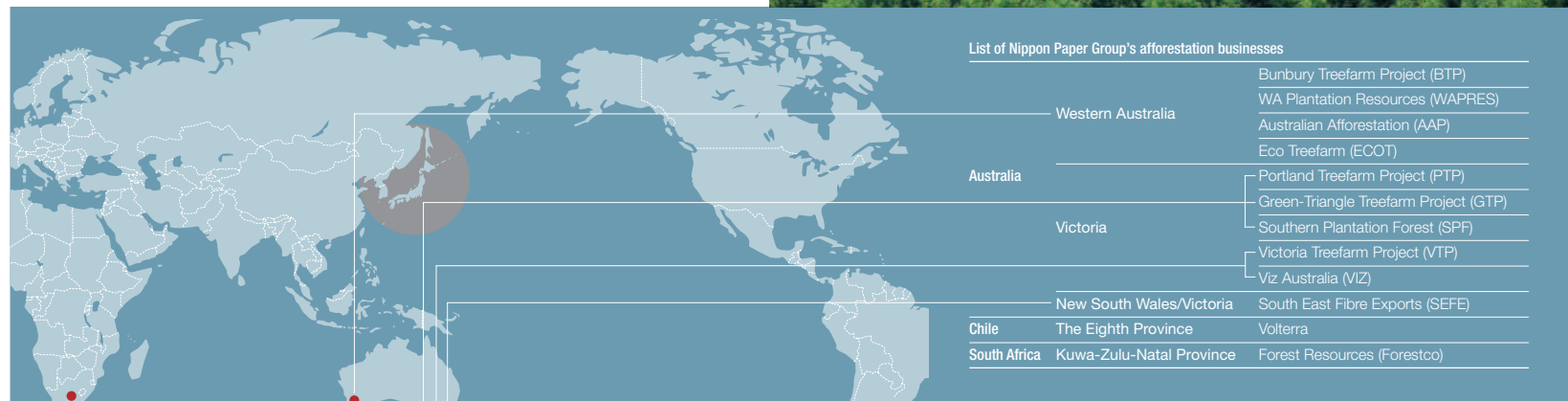

MASATOMO NAKAMURA
President
Nippon Paper Group, Inc.



Special Features

Raw Material Strategy

—Structure for Overseas Procurement of Woodchips



At Nippon Paper Group, we annually use approximately 6.4 million BDT (bone dry tons) of woodchips, our main raw material for paper manufacturing. The overseas and domestic procurement ratios are approximately 70% and 30% respectively.

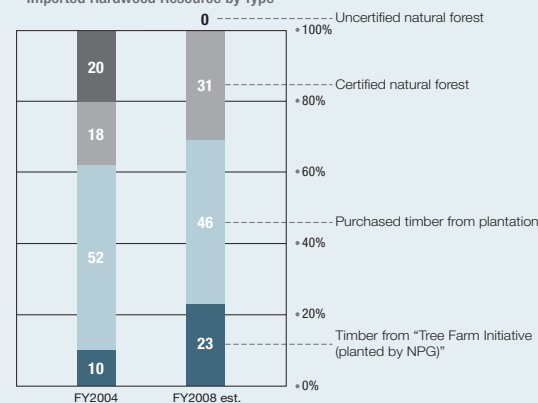
Concerning overseas woodchip procurement, we have positioned Australia, South Africa and Chile—lands rich in afforested wood resources—as procurement bases. Based upon long-term purchasing contracts with major local suppliers, we have constructed a stable supply structure. In addition, we are promoting our Tree Farm Initiative* and developing our own afforestation business in the previously mentioned areas (initial goal 100,000 hectares). As the end of March 2005, we had completed planting of afforestation areas covering 82,000 hectares, certain areas of which we have already begun harvesting. Moreover, we have the world's foremost fleet of 32 ships for transporting woodchips, and continue to advance in the construction of a stable delivery structure. The Group's fleet of ships for transporting woodchips is contracted on a long-term basis, making our fleet immune to short-term shifts in the sea transport market, and giving us sufficient shipping tonnage to respond to development of sources in distant areas.

We are also placing emphasis on domestic resources and utilizing the network of Group affiliate companies to establish a competitive supply structure, and working to make effective use of scrap wood generated from lumber product lines and thinned wood.

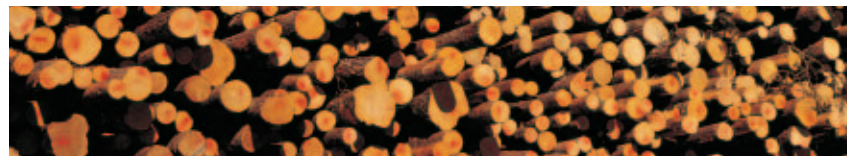
As we move toward our Group Vision 2015, in order to see growth in the pulp and paper business as we target the international market, we believe it is essential to further strengthen and expand our raw material supply base. We are therefore pushing ahead to expand further overseas afforestation as the second stage of our Tree Farm Initiative, with a goal of increasing area by 200,000 hectares. We are considering possibilities such as enclosing local resources around our afforestation areas, and the purchase of the current afforestation business by a third party. Nippon Paper Group will strategically implement these sorts of measures, and continue to construct an increasingly competitive raw material supply structure for the international market.

*Overseas afforestation business to create a sustainable supply of paper production materials.

Imported Hardwood Resource by Type



Introduction of Biomass Boilers and Utilization of Non-Fossil Fuels



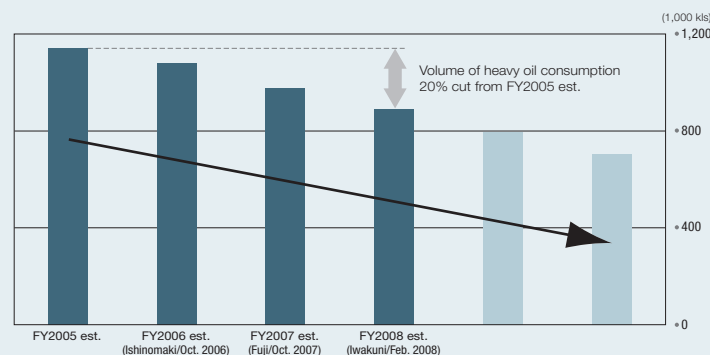
Biomass boiler
(Nakoso Mill of Nippon Paper Industries Co., Ltd.)

	Location	Invested amount	Operation start
Nippon Daishowa Paperboard	Tohoku	¥4.3 billion	Oct. 2003
Nippon Paper Industries	Nakoso	¥3.8 billion	Oct. 2004
	Ishinomaki	¥5.3 billion	Oct. 2006 (planned)
	Fuji	¥6.4 billion	Oct. 2007 (planned)
	Iwakuni	¥9.0 billion	Feb. 2008 (planned)

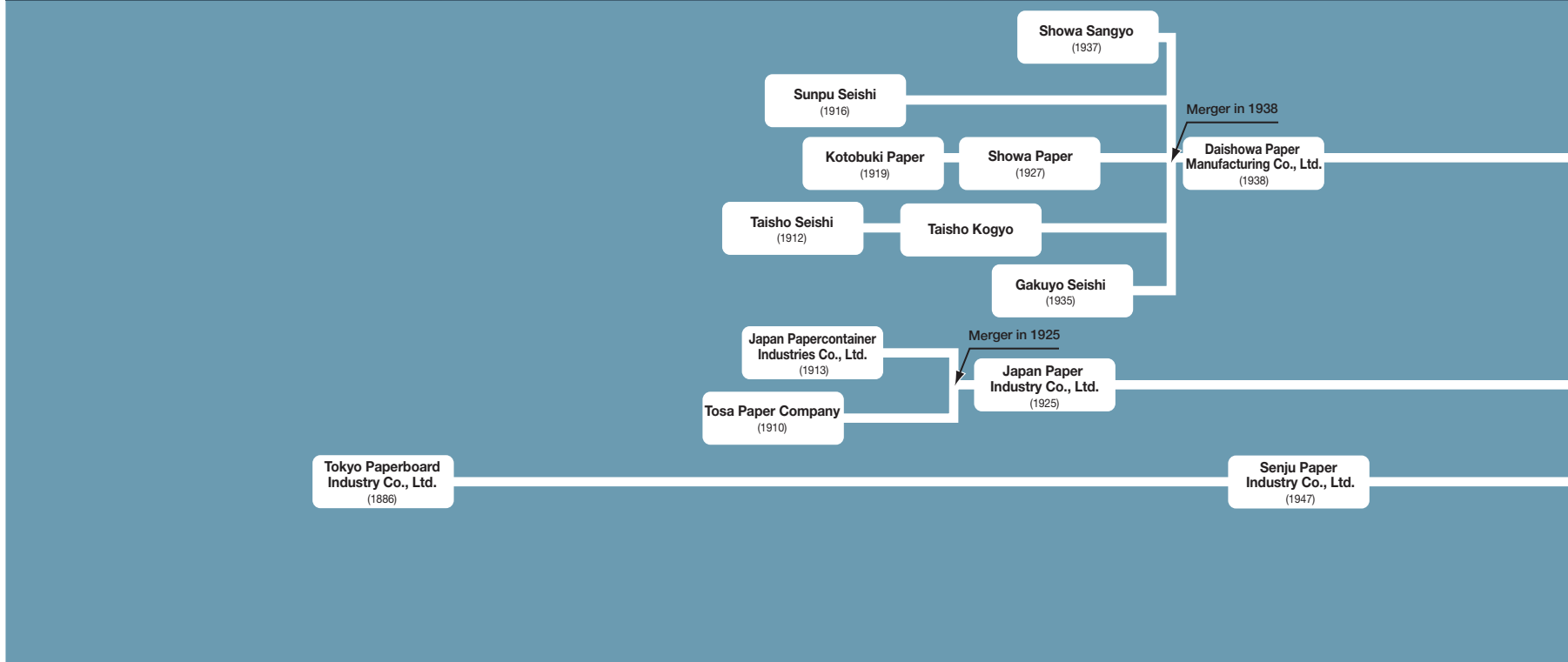
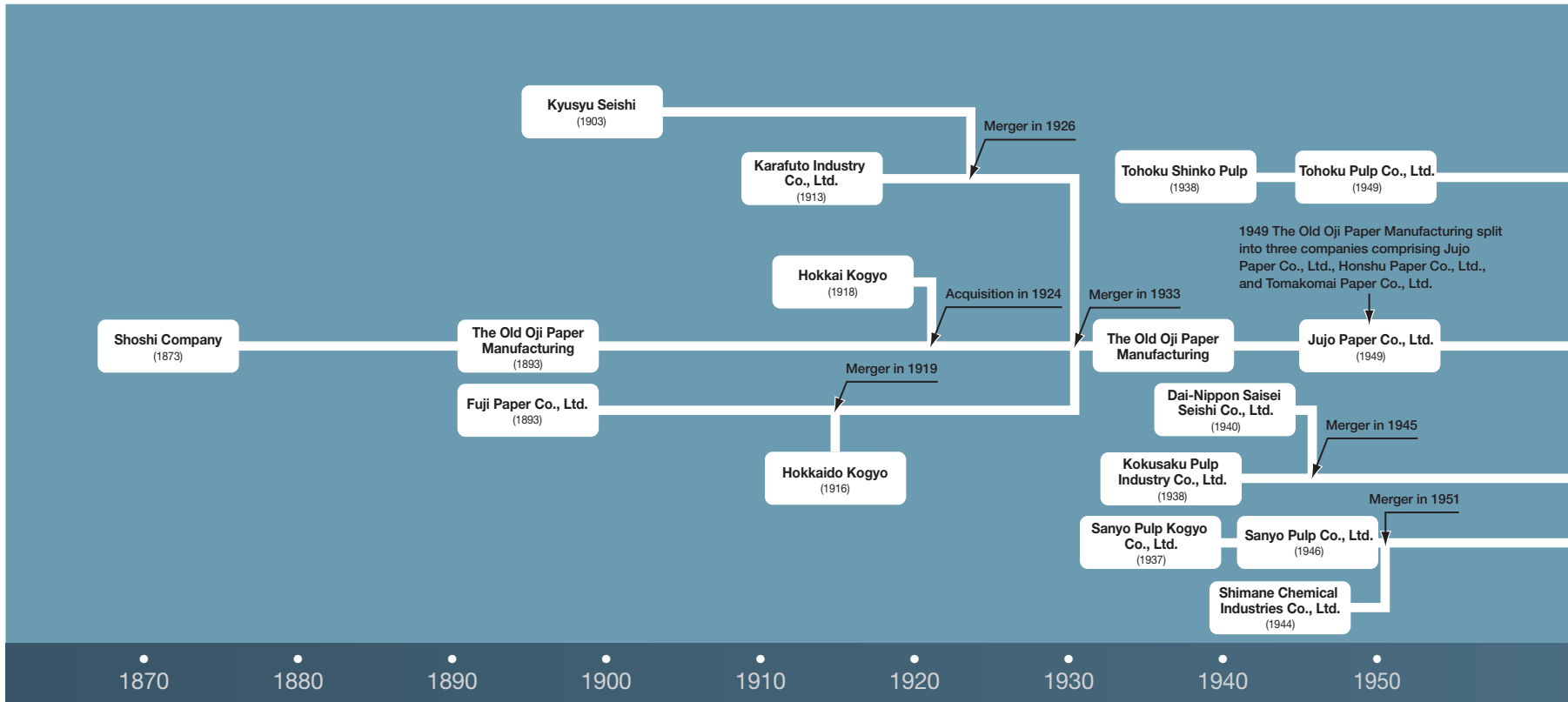
In the paper and pulp manufacturing process, large amounts of steam and electricity are used. Paper and pulp mills have traditionally handled the effluent (black liquor) generated in the pulp manufacturing process by incinerating it in recovery boilers for energy recovery, which aids in reducing the amount of fossil fuels such as coal and heavy oil that is used. At Nippon Paper Group, as part of our efforts in curbing greenhouse gas emission, we are promoting shifts from fossil fuels to non-fossil fuels. In addition to utilizing wood scraps, RPF and other fuels in existing coal boilers, we are also making capital investment for a significant shift to non-fossil fuels.

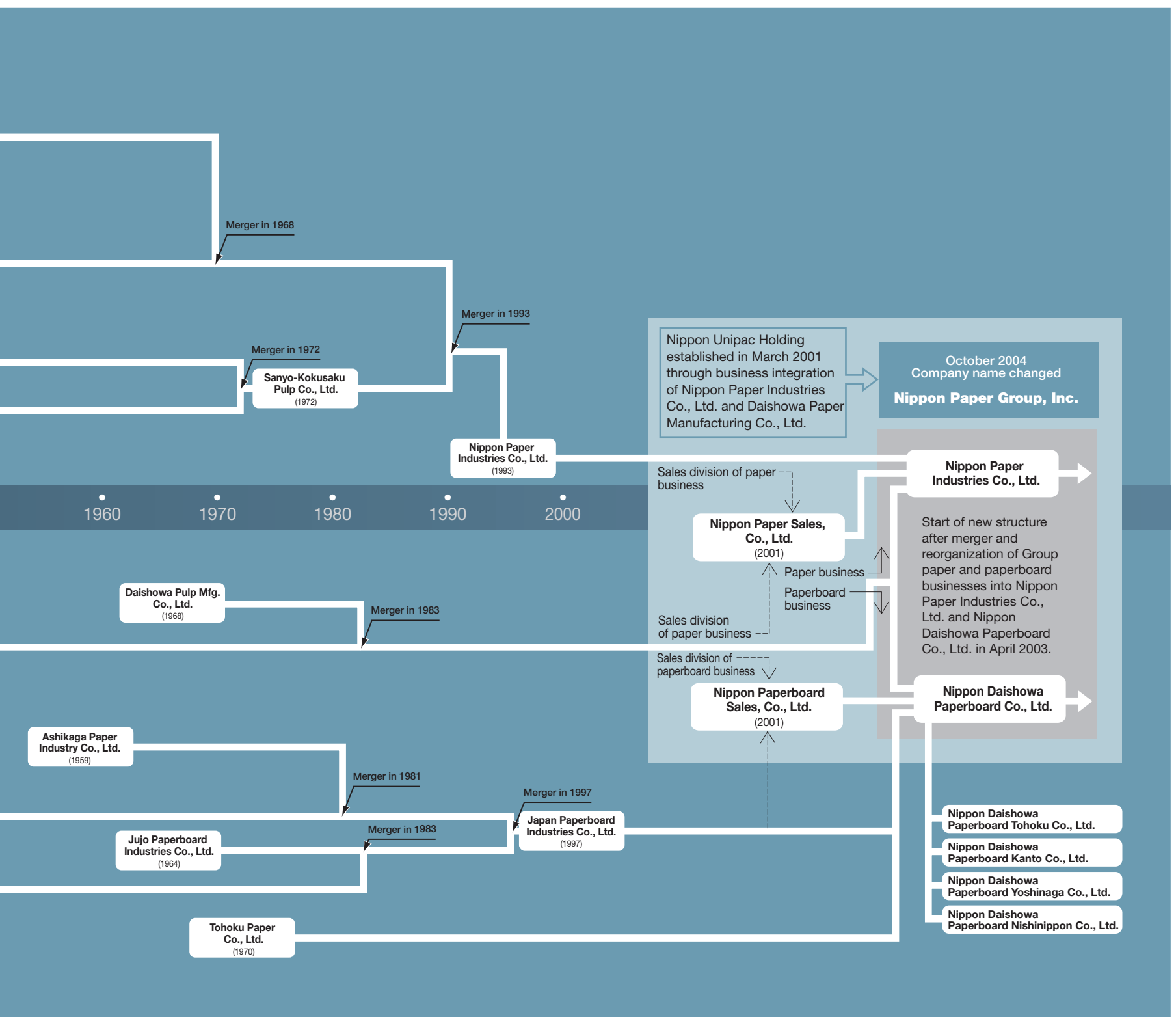
In October 2004, the Nakoso Mill of Nippon Paper Industries Co., Ltd. began operation of a boiler and a turbine primarily fueled by scrap wood. We also plan to introduce several new biomass boilers, with construction of facilities scheduled for completion in October 2006 at the Ishinomaki Mill, October 2007 at the Fuji Mill, and February 2008 at the Iwakuni Mill. We plan to power the new boilers with scrap wood. Because the mills mentioned currently use heavy oil boilers, the transfer to biomass boilers will enable us to cut down on our volume of heavy oil consumption. Accordingly, carbon dioxide emissions derived from fossil fuel use are projected to decrease. In addition, scrap wood is included in construction waste, a form of industrial waste, and using this wood as a fuel also contributes to social needs related to waste disposal.

When comparing heavy oil and scrap wood in terms of the necessary expenditures to yield the same amount of energy, scrap wood proves to be superior in terms of cost effectiveness. With heavy oil prices projected to continue rising, introducing biomass boilers and moving away from heavy oil use will enable us to reduce overall fuel costs.

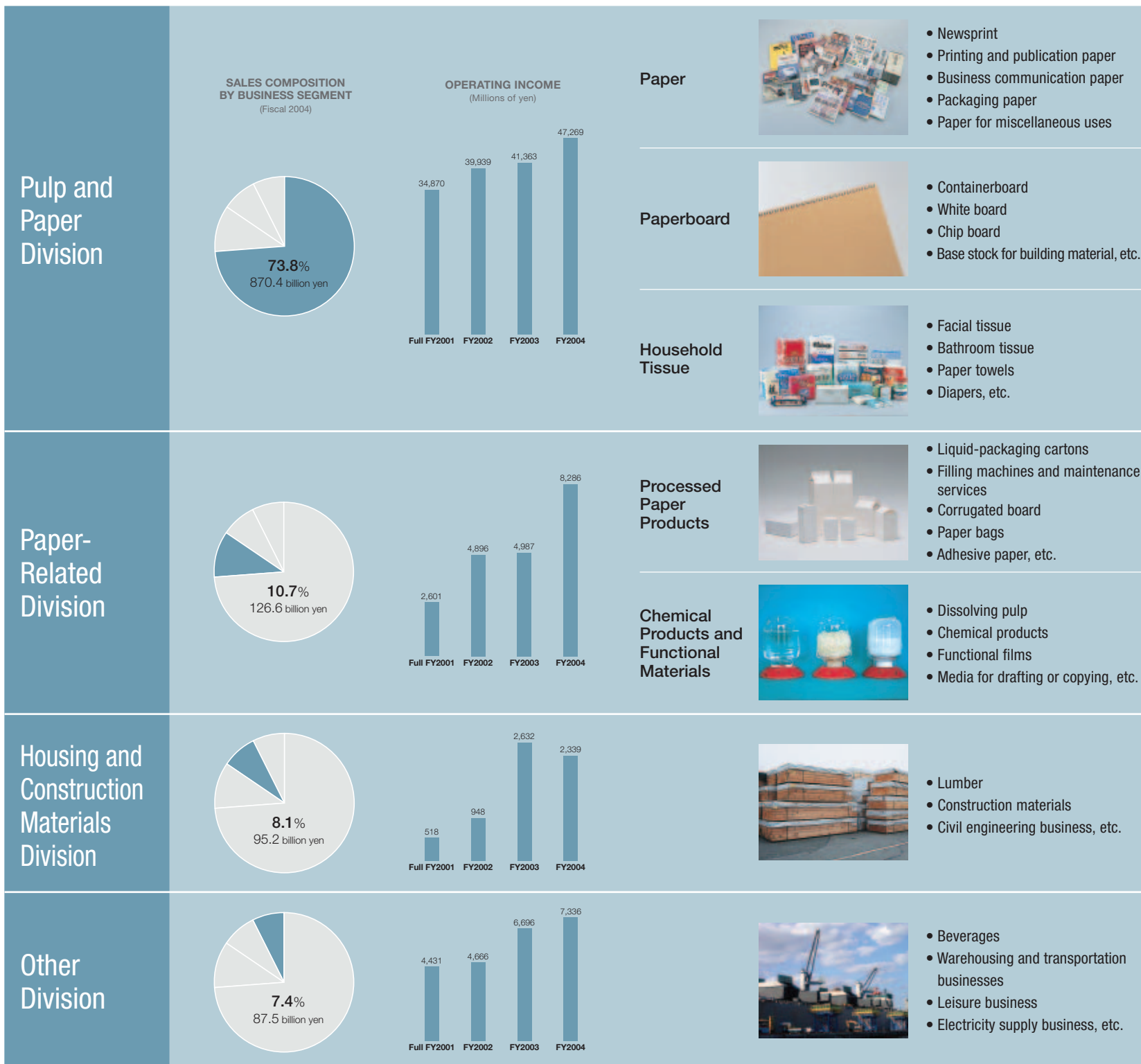


History of Nippon Paper Group





At a Glance



* Full fiscal year 2001 is the total of the first accounting period (from March 30, 2001 to September 30, 2001) and the second accounting period (from October 1, 2001 to March 31, 2002).

* The electricity supply business is included in "Pulp and Paper Division" in full fiscal year 2001 and fiscal year 2002, and is included in "Other Division" in fiscal year 2003 and 2004.

CONSOLIDATED SUBSIDIARIES AND AFFILIATES ACCOUNTED FOR BY EQUITY-METHOD

Nippon Paper Industries Co., Ltd.
 Nippon Daishowa Paperboard Co., Ltd.
 Nippon Daishowa Paperboard Tohoku Co., Ltd.
 Nippon Daishowa Paperboard Kanto Co., Ltd.
 Nippon Daishowa Paperboard Yoshinaga Co., Ltd.
 Nippon Daishowa Paperboard Nishinippon Co., Ltd.
 CRECIA Corporation
 San-Mic Shoji Co., Ltd.
 KOYO PAPER MFG. Co., Ltd.
 HAGA PAPER Co., Ltd.

Kokuei Paper Co., Ltd.
 Kitakami Paper Co., Ltd.
 Daishowa North America Corporation
 Nippon Paper Industries USA Co., Ltd.
 Daishowa International¹
 North Pacific Paper Corporation²
 Daishowa-Marubeni International Ltd.²

1. Liquidation of Daishowa International was completed on May 24, 2005.
 2. Affiliates accounted for by equity method (The same applies to the following.)

NIPPON PAPER-PAK CO., LTD.
 Nippon Paper Chemicals Co., Ltd.
 Sakurai Co., Ltd.
 Nippon Seitai Corporation
 FLOWRIC CO., LTD.

Nichiita Package Industries Co., Ltd.³
 LINTEC Corporation²
 Daishowa Paper Converting Co., Ltd.²
 Dixie Japan Co., Ltd.²

3. Nichiita Package Industries Co., Ltd. will become "NIPPON TOKAN PACKAGE CO., LTD." by merger on October 1, 2005.

Nippon Paper Lumber Co., Ltd.
 NIPPON PAPER UNITEC CO., LTD.
 Daishowa Unitec Co., Ltd.
 Kokusaku Kiko Co., Ltd.
 Kunimoku House Co., Ltd.

PAL CO., LTD.
 N&E CO., LTD.
 Daishowa Uniboard Co., Ltd.
 Daishowa Kohrin Co., Ltd.
 Daishowa Housing Co., Ltd.

South East Fibre Exports Pty. Ltd.
 Greenport Co., Ltd.²

NANKO UNYU CO., LTD.
 IWAKUNI-KAIUN CO., LTD.
 Kyokushin Transport Co., Ltd.
 NIPPON PAPER LOGISTICS CO., LTD.

Hotoku Co., Ltd.
 Daishowa Logistics Co., Ltd.
 Daishowa Port Warehousing Co., Ltd.
 SHIKOKU COCA • COLA BOTTLING CO., LTD.

Nippon Paper Development CO., LTD.
 Graphic Arts Communication
 Asahikawa Grand Hotel Co., Ltd.
 NEW HOKKAI HOTEL CO., LTD.

MAJOR SUBSIDIARIES

Nippon Paper Industries Co., Ltd.

→ P. 20–21

Nippon Daishowa Paperboard Co., Ltd.

→ P. 22–23

CRECIA Corporation

→ P. 24

NIPPON PAPER-PAK CO., LTD.

→ P. 25

Nippon Paper Chemicals Co., Ltd.

→ P. 26

Nippon Paper Lumber Co., Ltd.

→ P. 27

Major Subsidiary Profiles



M. Nakamura

Masatomo Nakamura
President

A Word from the President

The Company is building a more robust organization through “total optimization” and “Gemba-first approach” policies and shifting from a defensive to an offensive posture.*

**Management style rooted in workplace realities*



Nippon Paper Industries Co., Ltd.

>> **Business Environment** In 2004, there was a modest recovery in the economic environment in the paper industry, and the Athens Olympics provided economic impetus. On a calendar year basis, domestic demand for paper showed solid growth of 2.1% in 2004.

However, soaring demand in China drove prices of heavy oil, coal, and other raw materials upward, and the business environment remained severe.

>> **Company Strengths** A number of our core mills are located along the coast, which results in extremely strong cost competitiveness in Japan, which is dependent on imports of woodchips, coal, and other raw materials and fuels.

Nippon Paper Industries has an established reputation for technological expertise and product development capabilities. We have employed these strengths to develop various new products, including low-density paper, which has brilliant characteristics such as lightness while having volume, and high-quality next-generation newsprint with high opacity. In addition, most of the products in our domestic paper business command the top shares of their markets, and, as the top firm in the industry, we enjoy strong brand power and trust.

>> **Performance in Fiscal 2004** Domestic demand was solid in fiscal 2004, and our domestic sales volume showed year-on-year growth. Particularly sales of coated paper were strong, in connection with strong demand for fliers for tours, catalogs, and other commercial printing, as well as sales of new products.



As with other firms in this industry, we have been affected by the soaring prices of raw materials and fuels, but a price recovery of printing and business communication paper, together with a reduction in costs, allowed us to achieve major growth in both operating income and ordinary income over fiscal 2003.

>> **Outlook** The prices of heavy oil, woodchips, and other raw materials and fuels are forecast to cause a significant increase in costs during fiscal 2005, but we will be striving for steady improvement in earnings through reductions in the costs of production and labor. As a stepping-stone in the execution of our growth strategy, we established an office in Europe in July 2005, and through that office we plan to increase sales of business communication paper and other high-value-added products.

The second stage of rebuilding our domestic manufacturing structure will begin in fiscal 2006. Bringing further concentration of manufacturing and optimization of our manufacturing structure and increased efficiency in distribution and logistics, we will create a competitive advantage by reducing total costs in every operation from manufacturing through sales.

Overseas, we positioned the three regions of Asia, Europe, and North America as important markets, and in each of these regions are expanding existing businesses, while establishing and fostering new businesses, in a push for vigorous growth.

Established:

August 1, 1949

Paid-in Capital:

¥104,873 million

Web Site:

<http://www.np-g.com>

Representative:

President Masatomo Nakamura

Principal Products:

Newsprint
 Printing and publication paper
 Business communication paper
 Packaging paper
 Paper for miscellaneous uses

Fiscal 2004 Net Sales (including intragroup sales):

¥634.5 billion



Tetsuji Horikawa

Tetsuji Horikawa
President

A Word from the President

I believe my duty is to strengthen Nippon Daishowa Paperboard and Japan's paperboard business, to enhance the welfare and happiness of all concerned.



Nippon Daishowa Paperboard Co., Ltd.

>> **Business Environment** A hot summer in fiscal 2004 drove up demand for beverage use, but the unseasonable weather that followed caused the total volume of paperboard sales in Japan for the year to decline 0.4% compared with 2003. Many paperboard manufacturers energetically adjusted their inventories, and selling prices remained at a stable level, but sharply rising crude oil prices in the second half drove up the costs of heavy oil and other petroleum-based raw materials, exerting pressure on profits. Crude oil prices are expected to remain at high levels, and a continuation of severe business conditions is forecast.

Using wastepaper as the primary raw material, paperboard has only a small environmental impact, and it is and will be in demand for use as a wrapping material for products and a packaging material for logistics. No large-scale increase in domestic demand is predicted, but the environment in this business can be expected to remain fundamentally stable.

>> **Company Strengths** Nippon Daishowa Paperboard has a core mill near the Kanto region (Tokyo and its environs), the key consuming region, which gives it an advantage in both sales and the procurement of raw materials (wastepaper). We also have mills located throughout the country, so the expansion of its business is effectively completed. In addition, the concentration of manufacturing accomplished during the Group's business reorganization allows them to maintain a high operating rate.



>> **Performance in Fiscal 2004** We achieved profits exceeding its management plan in fiscal 2004. This is primarily as a result of the stabilization of prices achieved in fiscal 2003, particularly of containerboard, continued in fiscal 2004, the use of low-cost raw materials such as unused magazine wastepaper, increased yields and efficiency as a result of improved operating, reduction of fixed costs through laborsaving and other measures, and reductions in warehousing costs and other logistics expenses. These efforts allowed us to offset the higher costs of fuel and wastepaper and achieve growth in profits.

>> **Outlook** In fiscal 2005, we will continue to market its products at appropriate prices, while working to heighten cost competitiveness through buildup of daily improvement. Especially energy conservation is important not only to cost reductions, but also to the prevention of global warming, and we will be placing emphasis on this area. In the corrugated board manufacturing sector, Nichiita Package Industries Co., Ltd. is merging with ally Tokan Packaging System Co., Ltd. to form NIPPON TOKAN PACKAGE CO., LTD. in October 2005. The strengthening of this sector is an important issue for the Nippon Paper Group, and this merger will make the Group stronger.

Established:

August 28, 1913

Paid-in Capital:

¥10,864 million

Web Site:

<http://www.nichidaiita.co.jp>

Representative:

President Tetsuji Horikawa

Principal Products (applications):

Containerboard (corrugated board)

White board (packaging for confectionery and daily commodities, publishing, and catalogs)

Other paperboard (gypsum board base paper and paper core)

Specialty paper (plug wrap paper, teabags and filters)

Fiscal 2004 Net Sales (including intragroup sales):

¥152.9 billion



Akihiko Hada
President

A Word from the President

This year will be crucial in our efforts to reduce costs. We are moving forward with unflagging determination to weather this adversity.

Established:	April 2, 1963
Paid-in Capital:	¥4,667 million
Web Site:	http://www.crecia.co.jp
Representative:	President Akihiko Hada
Principal Products:	Facial tissue Bathroom tissue Paper towels Pre-moistened wipes Personal-care products Industrial-use wipes
Fiscal 2004 Net Sales (including intragroup sales):	¥56.7 billion



CRECIA Corporation

>> **Business Environment** The institution of a requirement to show full prices including consumption tax on product packages in April 2004 was the cause of a decline in prices and the intensification of price competition. Then, at the beginning of autumn, our major competitor changed its marketing strategy that plunged the entire household tissue market into an unprecedented price war. As a result, while total 2004 shipments of sanitary paper rose 1.6% year-on-year to 1,699,000 tons, the value of sales declined 1.3% to ¥301 billion.

>> **Company Strengths** CRECIA Corporation has continued to grow on the strength of an alliance with Kimberly-Clark Corporation. This alliance is based on two major brands, Kleenex® and Scottie®, and gives CRECIA access to a high level of technological expertise. In addition, our four manufacturing facilities near the major consuming regions from the Tokyo Metropolitan area to western Japan give us an advantage enjoyed by none of our competitors.

>> **Performance in Fiscal 2004** CRECIA has conducted energetic marketing activities such as the 40th anniversary campaign of the commencement of Kleenex® tissue sales in Japan, and has engaged in marketing programs that took price restoration into account. However, we were involved in price competition, and had to respond adequately. In October 2004, we adopted a new sales organization in an endeavor to strengthen its marketing capabilities. We reformed the staffing structure at each of our manufacturing facilities, and worked to cut production costs. However, the decline in selling prices was substantial, and net sales for fiscal 2004 declined more than 10% to ¥56.7 billion.

>> **Outlook** Continued price competition will make for severe conditions, but through the repeated introduction of new high-value-added products, we are striving to become “a firm that generates high and stable earnings, with a fundamental focus on price.” We will also concentrate on the establishment of a significant presence in the personal care business and other growth. We are accelerating the reduction of labor costs by the implementation of measures to strengthen our revenue base and other operating costs to quickly build a competitive corporate structure.



Toshihiko Maeda
President

A Word from the President

We strive to realize transparent management based on our merit-based system and driven by a shop-floor mindset while carrying out our “customer-first policy” with environmental considerations.

Established:	March 18, 1965
Paid-in Capital:	¥4,000 million
Web Site:	http://www.nipponpaper-pak.com
Representative:	President Toshihiko Maeda
Principal Products and Services:	Liquid-packaging cartons Filling machines and related maintenance services Paper containers Film for food packaging use Film for industrial packaging use
Fiscal 2004 Net Sales (including intragroup sales):	¥45.8 billion



NIPPON PAPER-PAK CO., LTD.

>> **Business Environment** The Japanese food industry is becoming increasingly demanding in terms of sanitation and safety controls within our operations. Further, consumers are increasingly concerned about environmental issues; thus paying more attention to supplier involvement in recycling and other supportive activities. Extraordinary weather, such as an exceptionally cool or hot summer, directly affects beverage consumption and consequently sales of liquid-packaging cartons. The surge in oil prices has had a significant impact on the cost of raw materials such as paperboard and plastic resins. Under these circumstances, we have conducted our operations from a “customer-first” perspective, focusing on quality, safety and the environment.

>> **Company Strengths** We sell a broad range of packaging products made of “paper” as environmentally friendly material, from PURE-PAK® chilled liquid-packaging cartons to NS-FUJI PAK® aseptic packaging cartons. We supply these cartons as part of an integrated system that includes special filling machines and related maintenance services, thereby proactively responding to all customer needs.

>> **Performance in Fiscal 2004** Thanks to the summertime heat wave that brought a significant growth in beverage consumption and especially of ready-to-drink tea, the sales volume of liquid-packaging cartons surpassed that of fiscal 2003, despite decreased milk consumption and stiff competition among carton suppliers. On the other hand, sales of general paper containers decreased due to intense competition in the household tissue industry, increased supply from overseas competitors and sluggish growth in new product sales. As a part of our continual challenge to strengthen our corporate structure, we outsourced logistics operations and conducted the buyout of a film business subsidiary while rationalizing headcounts and improving production efficiency.

>> **Outlook** The operating environment in fiscal 2005 appears to remain severe as raw material prices are expected to hike and rivalry in the market is expected to intensify. In addition to the cost-reduction project already started, we have committed ourselves to strive for improved productivity and competitiveness by upgrading facilities through a scrap and build process. In China, a joint venture project with Elopak AS for the PURE-PAK® business is continuing. At the same time, we will carry on with aggressive marketing efforts in the NS FUJI-PAK® business.



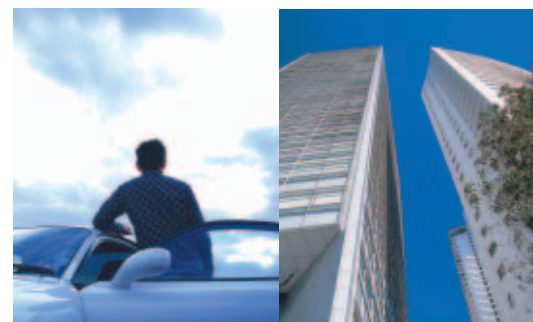
Toshio Inoue

Toshio Inoue
President

A Word from the President

The scope of our business fields was greatly expanded by integrating the functional materials business of Nippon Paper Industries into our operations in October 2004. At the same time as we strengthen existing businesses, we are also aiming for further growth and development.

Established:	October 1, 2002
Paid-in Capital:	¥3,000 million
Web Site:	http://www.npchem.co.jp
Representative:	President Toshio Inoue
Principal Products (applications):	Dissolving pulp (rayon, cellophane, cellulose derivatives, etc.), Chlorinated polyolefin, Special polyolefinic resin (paint, ink, adhesives, etc.), Lignin products (concrete admixture, bonds, etc.), Carboxymethyl cellulose (CMC) (thickener, stabilizer, etc.), Powdered cellulose (resin additive, filter auxiliaries, food additives, etc.), Yeast extract (foods, animal feed, etc.), Ribonucleic acid (seasonings, culture media, etc.), Stevia extract, glycyrrhizin (natural sweetener), Optical films for displays (various flat-panel displays)
Fiscal 2004 Net Sales (including intragroup sales):	¥27.9 billion



Nippon Paper Chemicals Co., Ltd.

>> **Business Environment** Nippon Paper Chemicals recorded an increase in net sales, with a stable market for dissolving pulp since 2004, robust global demand for automobile paint supporting strong sales of chlorinated polyolefin, and contributions from the rapid growth of the functional materials business, which was integrated in October 2004. On the other hand, unprecedented rises in crude oil prices and the resulting increase in an array of raw material prices raised the level of severity in the operating environment.

>> **Company Strengths** We have gained the long-lasting trust of our customers based on three strengths. The first strength is our agile business operations through synergetic cooperation in production, sales and R&D from the customers' perspective. Second, we have a flat organizational structure that enables rapid decision-making. Our third strength is a development structure that emphasizes the cultivation of proprietary technologies.

>> **Performance in Fiscal 2004** During fiscal 2004, our third fiscal period as a new company, the integration of the functional materials business in the second half of the period provided momentum to the expansion of our business base. As a result, we saw significant gains in sales and earnings, with net sales rising 10% over fiscal 2003 figures and operating income increasing 32%.

>> **Outlook** Fiscal 2005 is the last year of our First Medium-Term Business Plan. In spite of severe circumstances related to raw material and fuel prices, we are making even more vigorous efforts to improve profitability by internal controls. In the business of liquid crystal display materials, we are responding to steadily rising sales volume by boosting production capacity, and expect to see growth in both sales and earnings.



Satoru Tanada
President

A Word from the President

Based upon a spirit of self-autonomy and self-reliance, we aim to establish ourselves as the top company in Japan's lumber distribution industry, while continuing to grow as company with a significant role in the Nippon Paper Group.

Established:	September 10, 1970
Paid-in Capital:	¥440 million
Web Site:	http://www.np-l.co.jp
Representative:	President Satoru Tanada
Principal Products and Commodities:	Imported logs (softwood, hardwood) Lumber products, Glued lumber Plywood, Pulpwood, Woodchips Wastepaper, Insulation materials
Fiscal 2004 Net Sales (including intragroup sales):	¥84.5 billion



Nippon Paper Lumber Co., Ltd.

>> **Business Environment** New housing starts in Japan during 2004 rose 2.5% over 2003. Strong activity in the markets for lumber and housing materials in 2003 continued into the first half of 2004, but a slowdown in activity in the second half of 2004 led to a decline in prices for housing materials. With an absence of positive factors to stimulate demand, such as tax reductions for housing loans, we are taking a guarded view of future housing demand and expecting competition in the industry to intensify.

>> **Company Strengths** Leveraging the reliability, financial strength, and corporate planning strength that comes with being part of the Nippon Paper Group, we are growing as the top company in the industry with the ability to manage lumber resources efficiently and effectively in our activities ranging from cultivating forests to marketing housing and paper-manufacturing materials, while working to utilize waste materials. More than 170 lumber professionals make various proposals to users through a national network of marketing bases.

>> **Performance in Fiscal 2004** In fiscal 2004, we pushed forward with marketing activities, shifting our focus from logs to lumber products and construction materials. We made efforts to expand sales of recycling products and products made from recycled materials such as woodchips, including scrap woodchips, wastepaper, and insulation materials made from wastepaper. As a result, both sales and income rose in comparison with fiscal 2003, with net sales increasing 14% and ordinary income edging up 3%.

>> **Outlook** We are expecting severe and rapidly changing conditions to continue, hindered by a leveling-off in housing demand. Within such an environment, fortifying marketing activities in major metropolitan areas experiencing high demand is of the utmost importance. We will open a new logistics center in the Kanto area in October 2005, and enhance our product line targeting the Tokyo metropolitan area. We are advancing in our efforts to establish a recycling-oriented business model to alleviate environmental impact, and will work to strengthen our lumber and paper-related recycling business.

CSR

In order to promote corporate social responsibility (CSR) in management, the Nippon Paper Group established the CSR Committee in 2003, with the Corporate Ethics Subcommittee, the Social Contribution Subcommittee, the Safety & Health Subcommittee, the Product Safety Subcommittee, and the Environment Subcommittee under its umbrella. In addition the Group newly established the Raw Materials Subcommittee in October 2004, making a total of six subcommittees through which we conduct CSR activities.

The CSR Committee is composed of presidents and directors of major subsidiary companies, and deliberates on important matters related to CSR, while subcommittees control activities related to their particular fields of specialty.

The CSR Office is also in place as a division responsible for control and supervision of the entire scheme of the Group's CSR.

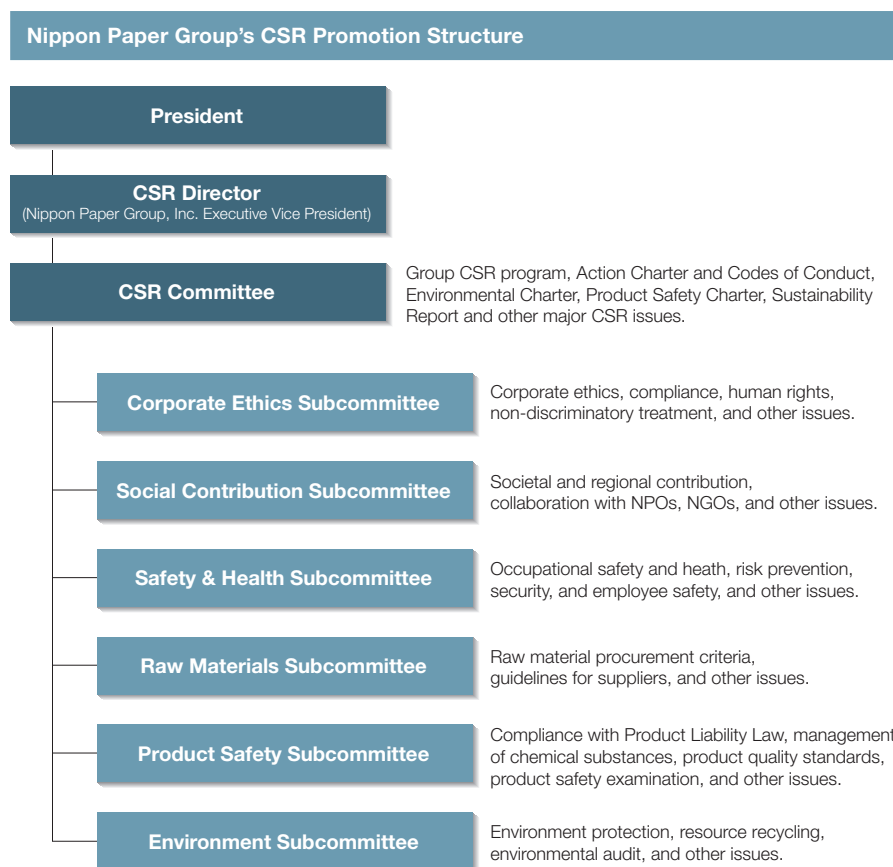
Based upon this scheme, we have identified the proactive accomplishment of total CSR including corporate ethics as an important management issue, and are working to promote Group CSR activities as a corporation that broadly supports industry, culture and local communities.

Protection of Personal Information

In April 2005, the Law for Privacy Protection came into full force, and social concerns regarding protection of personal information continues to heighten. At Nippon Paper Group, Inc. and major subsidiaries in order to comply with legal standards related to protection of personal information and other regulations, we have formulated policies concerning the protection of personal information of customers, business partners, employees and other stakeholders that is utilized in business activities. We have also distributed to employees our document, the Manual for Handling Personal Information, that is based upon the content of the policies and requirements of the Law for Privacy Protection. This manual promotes understanding by laying out what sort of concrete actions must be and must not be taken in response to the new law.

Introductory Seminar on Becoming a Volunteer "BORAMADO*"

The Social Contribution Subcommittee is working to create programs for social contribution under the three themes of "Applying our businesses and specialties," "Utilizing the Company forest land," and "Supporting employee participation in volunteer activities." As an example of the latter, Nippon Paper Group opened an introductory seminar called the "BORAMADO*" for Group employees. In the first part of the seminar, volunteer organization that we had invited introduced their activities. In the second part of the program, employees could freely interact at booths opened by the organizations, and took part in activities including



affixing stickers in local languages to books that were to be sent to children in Asian nations, and learning to handle wheelchairs properly. The Social Contribution Subcommittee will continue working to make Group employees feel more at ease about participating in volunteer activities.

**BORAMADO* is a term coined to denote programs for introducing volunteers.

Explanatory Meeting on Environmental Safety

At the Iwakuni Mill of Nippon Paper Industries Co., Ltd. and the Iwakuni Works of Nippon Paper Chemicals Co., Ltd., we held our second explanatory meeting on environmental safety in September 2004, with participation by local associations and public administrators from the area around the Mills. The Iwakuni Mill has hosted environmental safety explanatory meetings since 2003, with the aim of disclosing to local residents and public administrators information related to environmental conservation and safety assurance initiatives at the Mill. First, a tour of the primary manufacturing facilities and environmental equipment was taken, and then followed by explanations of PRTR result and other environmental data, and of efforts on behalf of environment and safety. A lively question and answer session followed, enabling us to further deepen mutual understanding and trust relationships with local residents and public administrators. We will continue to host these explanatory meetings regularly, actively conduct disclosure of information, and build better communication with local communities.

CSR Seminars for Personnel Responsible for Raw Materials/Trading

In September 2004, we had a CSR seminar with an invited outside lecturer for personnel responsible for raw materials and trading. The session included teaching and drills on the importance of supply chain management (SCM) in CSR, and the condition of Group SCM activities. Participants included the personnel responsible for related areas at Nippon Paper Industries Co., Ltd., Nippon Daishowa Paperboard Co., Ltd., CRECIA Corporation, NIPPON PAPER-PAK CO., LTD., Nippon Paper Chemicals Co., Ltd.,

Nippon Paper Lumber Co., Ltd., San-Mic Shoji Co., Ltd. and Nippon Paper Development Co., Ltd. The first half of the seminar was a lecture which the participants enthusiastically received as being related to everyday operations. During the second half, participants broke into three groups and put current SCM conditions at the Company into a diagram, extracting risks and issues and discussing the direction that these activities should take in the future. Awareness of global SCM trends and current SCM conditions at the Company was enhanced, making this a meaningful training session.

Safety of Products and Services

To ensure the safety of its all products and services, Nippon Paper Group formulated the Philosophy and Basic Policy on Product Safety in October 2004. Nippon Paper Group offers safe products and services as part of its social responsibilities, and will continue to conduct activities throughout the entire Group aimed at earning the highest trust of customers and enhancing social contributions.

Installation of Biomass Power Generation Plants

Steam used in the manufacturing processes and in electricity production at paper mills is primarily generated through coal boilers or recovery boilers that use black liquor* for fuel, with a portion generated by the use of heavy oil boilers. Nippon Paper Group will reduce the amount of heavy oil used and the resulting carbon dioxide emissions from fossil fuels by replacing existing heavy oil boilers with biomass boilers. The Nakoso Mill of Nippon Paper Industries Co., Ltd. already began use of a biomass boiler that utilizes wood scraps for its primary fuel, and a steam turbine power generator from October 2004. In addition, the Company plans to construct new biomass power generators that run primarily on wood scraps at its Mills in Ishinomaki, Fuji and Iwakuni, with completion planned between 2006 and 2008.

*Black liquor is effluent generated during the pulp manufacturing process.

Corporate Governance

Nippon Paper Group, Inc. considers improving the transparency of our operations and conducting equitable corporate activities toward shareholders, investors, customers, suppliers, local communities and all of our diverse stakeholders to be matters of the utmost importance. As a pure holding company, Nippon Paper Group, Inc. acts as the control center for Group management, promoting growth strategies for each Group company, and monitoring Group companies. We believe that fulfilling disclosure responsibilities to our stakeholders is the foundation of corporate governance. We also aim to instill thorough compliance by monitoring each Group company.

Corporate Governance Structure

Nippon Paper Group has clearly defined the organization and roles within it, with governance by the Group headquarters separate from execution of operations at each Group company. In enforcing governance, we take a minimal approach to influencing the business execution of Group companies, and in principle promote their freedom, independence and self-responsibility. In addition, Investor Relations

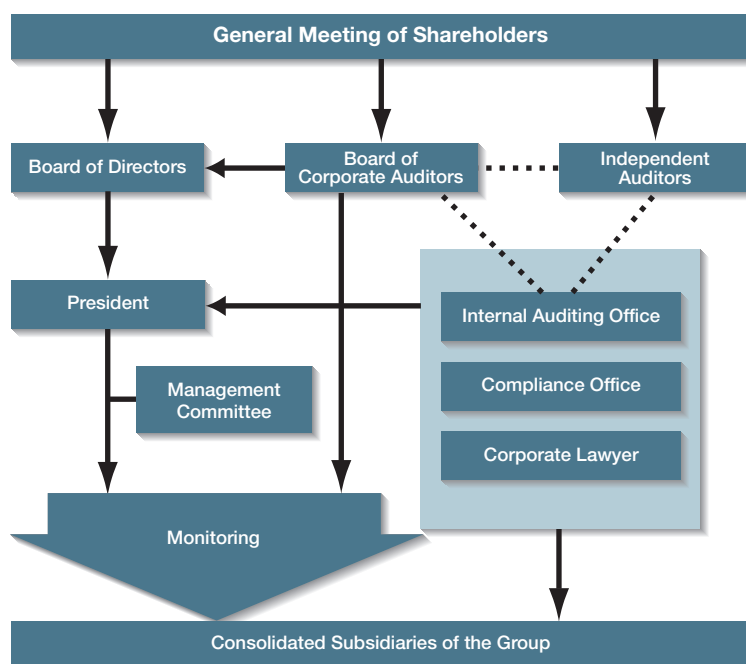
has been established as a body under direct control of the President, so that the views of capital markets regarding management are relayed directly to top management.

In the Company's articles of incorporation, the number of directors is set as 10. Currently, the Company has nine internal directors and no outside directors. The Board of Directors determines matters pertaining to the basic policies, rules and articles of incorporation for Nippon Paper Group, Inc. and Group management, as well as other important management-related issues. At the same time, the Board of Directors is positioned as the body for monitoring business execution. Aside from the Board of Directors, a Management Committee composed of all directors and corporate auditors including the Chairman meets at least once per month. In addition to promoting thorough compliance, the Management Committee deliberates regarding basic policies and strategies related to the management of Nippon Paper Group, Inc. and Group companies, and regarding important matters related to execution of operations at Group companies.

In addition, a Meeting of Affiliate Company Presidents is held one time every three months. There, the Presidents of the Group's eight core companies gather to exchange opinions on management issues at each company, and confirm progress toward achieving goals of the Medium-Term Business Plan.

The Company is employing a corporate auditors system in accordance with statutory regulations related to the Commercial Code of Japan. As of September 2005, the Company has two internal corporate auditors and two outside corporate auditors. Outside corporate auditors are selected from candidates who are not former members of the Company or Group companies.

In principle, the Board of Corporate Auditors meets once a month before the Board of Directors and examines the legality and appropriateness of proposed measures. Corporate Auditors participate in important meetings such as the Board of Directors, the Management Committee and the Meeting of Affiliate Company Presidents, and closely



examine the business execution activities of directors by expressing opinions and inspecting important documents. Moreover, Corporate Auditors conduct interviews with directors and employees, and carry out on-site inspections at subsidiary companies. Corporate Auditors provide feedback on results of inspections, promote reform of indicated items, and report important issues to directors.

Because Nippon Paper Group, Inc. is a pure holding company, the Internal Auditing Office within the Financial Division at subsidiary companies Nippon Paper Industries

Co., Ltd. and Nippon Daishowa Paperboard Co. Ltd. conduct internal audits of their own operations and of operations at related companies.

The Company employs Ernst & Young ShinNihon to carry out an accounting audit in accordance with the Securities and Transaction Law, and as an accounting auditor in accordance with the Commercial Code of Japan. There are no particular interests between the Company and Ernst & Young ShinNihon or its staff who carry out accounting audits.

Interview with Mr. Yoshinari Inoue, Senior Corporate Auditor, concerning auditing activities at Nippon Paper Group, Inc.

Q. What are the unique features of auditing activities at Nippon Paper Group, Inc.?

A. As a Board of Corporate Auditors of a holding company, we have a responsibility for oversight of the entire Group. We are focusing on points such as the condition of the entire Group's systems for governance and compliance with laws and regulations, and on how business risks are being handled. We also keep a watchful eye on whether or not all divisions of Nippon Paper Industries, to which the Company is outsourcing its operations and services, are conducting business activities with a group management mentality.



Q. How are you relating with auditing activities at Group companies?

A. We visit consolidated subsidiaries and conducted audits together with corporate auditors at each company. During the two years of fiscal 2003 and 2004, we carried out audits at 42 domestic and overseas companies, including visits to manufacturing facilities and other primary business sites. We also issue directives to related companies and related divisions for reform of areas requiring improvement, and monitor the implementation of improvements.

Q. You have a broad area to cover in oversight of the entire Group, don't you?

A. That is correct. That is why we hold three meetings a year of the Nippon Paper Group, Inc. Auditors Information Network, which is composed of 20 subsidiary companies that have full-time corporate auditors, and serves to strengthen ties between Group company auditors. At the meetings, participants report on auditing plans and activities at each company, hold study meetings led by legal professionals, enlighten each other and collaborate to improve Group oversight. Administrative Meetings of the Nippon Paper Group, Inc. Auditors Information Network are also held on a monthly basis, at which Corporate Auditors from Nippon Paper Group, Inc., Nippon Paper Industries, and Nippon Daishowa Paperboard gather to inform each other regarding auditing activities and to discuss the operation of the Auditors Information Network. In addition, we place importance on exchange between the Internal Auditing Office of Nippon Paper Industries and the independent auditors, and promote cooperation between them.

Directors and Corporate Auditors

(AS OF JUNE 29, 2005)



(from left to right) Yoshio Haga, Tetsuji Horikawa, Keisuke Ito, Iwao Nakajima, Masatomo Nakamura, Takahiko Miyoshi, Tsuyoshi Yamashita, Toshio Inoue, Masaru Motomura

Chairman and Representative Director

Takahiko Miyoshi

President and Representative Director

Masatomo Nakamura

President and Representative Director of Nippon Paper Industries Co., Ltd. as an additional post

Executive Vice President and Representative Director

Iwao Nakajima

*Assistant to the President, specializing in CSR
Executive Vice President and Representative Director of Nippon Paper Industries Co., Ltd. as an additional post*

Directors

Keisuke Ito

Managing Director and General Manager of the Financial Division of Nippon Paper Industries Co., Ltd. as an additional post

Tsuyoshi Yamashita

Managing Director and General Manager of the Personnel & General Affairs Division of Nippon Paper Industries Co., Ltd. as an additional post

Tetsuji Horikawa

President and Representative Director of Nippon Daishowa Paperboard Co., Ltd. as an additional post

Toshio Inoue

President and Representative Director of Nippon Paper Chemicals Co., Ltd. as an additional post

Yoshio Haga

Director, General Manager of the Corporate Planning Division and General Manager of the Corporate Planning Department of Nippon Paper Industries Co., Ltd. as an additional post

Masaru Motomura

Director, General Manager of the Subsidiaries and Affiliated Companies Division and General Manager of the Subsidiaries and Affiliated Companies Department of Nippon Paper Industries Co., Ltd. as an additional post

Senior Corporate Auditor

Yoshinari Inoue

Corporate Auditor

Hirotoishi Ishikawa

Corporate Auditor of Nippon Daishowa Paperboard Co., Ltd. as an additional post

Outside Corporate Auditors

Takashi Kawahara

Corporate Auditor of Nippon Paper Industries Co., Ltd. as an additional post

Naoki Yanagida

Corporate Auditor of Nippon Paper Industries Co., Ltd. as an additional post

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Consolidated 4-year Summary

Nippon Paper Group, Inc. and Consolidated Subsidiaries

FOR THE YEAR:	Millions of yen				Thousands of U.S. dollars (Note 2)
	Full FY2001 (Note 1) March 30, 2001–March 31, 2002	FY2002 April 1, 2002–March 31, 2003	FY2003 April 1, 2003–March 31, 2004	FY2004 April 1, 2004–March 31, 2005	FY2004 April 1, 2004–March 31, 2005
Net sales	¥1,211,422	¥1,165,450	¥1,192,649	¥1,179,696	\$11,025,196
Cost of sales	919,859	892,906	919,602	914,384	8,545,645
Operating income	42,422	50,450	55,679	65,231	609,636
Ordinary income	28,563	39,671	50,665	62,801	586,925
Net income (loss)	(636)	4,880	24,258	24,350	227,570
Total assets	1,721,745	1,630,126	1,637,366	1,529,975	14,298,832
Total current assets	517,698	455,445	476,649	443,177	4,141,841
Property, plant and equipment, net	941,428	924,597	900,013	843,346	7,881,738
Total investments and other assets	262,618	250,083	260,703	243,450	2,275,234
Liabilities and minority interests in consolidated subsidiaries	1,314,376	1,221,923	1,207,744	1,087,097	10,159,785
Total shareholders' equity	407,369	408,202	429,621	442,876	4,139,028
Interest-bearing debt	903,336	851,311	842,278	766,139	7,160,178
Depreciation	87,144	83,223	81,259	74,971	700,664
Capital investment	69,512	76,904	57,423	55,353	517,318
Free cash flow	13,221	56,804	14,425	82,132	767,589
PER SHARE DATA:	Yen				U.S. dollars
Net income (loss)					
Basic	(590.30)	4,283.53	22,025.22	21,996.96	205.58
Diluted (Note 3)	—	4,137.37	21,132.64	21,107.50	197.27
Total shareholders' equity	377,308.99	374,133.23	392,140.80	404,369.11	3,779.15
Cash dividends	8,000.00	8,000.00	8,000.00	8,000.00	74.77
RATIOS:					
Operating income to net sales (%)	3.5	4.3	4.7	5.5	
Net income (loss) to net sales (%)	(0.1)	0.4	2.0	2.1	
Return on equity (ROE) (%)	(0.2)	1.2	5.8	5.6	
Return on invested capital (ROIC) (%)	3.4	4.2	4.9	5.9	
Equity ratio (%)	23.7	25.0	26.2	28.9	
Return on assets (ROA) (%)	2.6	3.2	3.8	4.7	
Debt/Equity ratio (times)	2.1	2.0	1.9	1.7	
Number of employees	17,153	15,662	14,987	13,774	

Notes: 1. Full fiscal year 2001 is the total of the first accounting period (from March 30, 2001 to September 30, 2001) and the second accounting period (from October 1, 2001 to March 31, 2002).

2. Amounts in U.S. dollars are included solely for the convenience. The rate of ¥107 = U.S.\$1.00, the approximate rate of exchange in effect on March 31, 2005, has been used.

3. Diluted net income per share in full fiscal year 2001 is not stated because of basic net loss per share.

Interest-bearing debt = Short-term borrowings + Long-term debt
 Free cash flow = Cash flows from operating activities + Cash flows from investing activities
 Return on equity (ROE) = Net income / Average shareholder's equity × 100

Return on invested capital (ROIC) = (Ordinary income + Interest expense) / (Total shareholder's equity + Interest-bearing debt) × 100
 Return on assets (ROA) = (Ordinary income + Interest expense) / Total assets × 100
 Debt/Equity ratio = (Interest-bearing debt – Cash and cash equivalents) / Total shareholder's equity × 100

Consolidated Financial Review

Nippon Paper Group, Inc. and Consolidated Subsidiaries

SUMMARY

During fiscal 2004, ended March 31, 2005, the Japanese economy continued its recovery in the first half of the fiscal year, supported by increases in exports and capital investment, strong sales of digital home appliances and other signs of recovery in personal consumption. In the second half of the fiscal year, however, a slowdown in exports was coupled with inventory adjustments in IT-related products, and the overall economy entered a period of moderate adjustment and leveling off.

In the paper industry, recovery in the overall economy and effects from the Athens Olympics helped domestic demand during calendar year 2004 outpace demand in 2003 by 2.1%. In the paperboard industry, firm demand for processed-food applications led to an increase in demand of 0.8% compared with 2003, in spite of some negative effects due to unseasonable weather. This marked the second consecutive year of increases for paper and paperboard demand. On the other hand, high prices for raw materials and fuels such as heavy oil, coal and woodchips continued to hinder progress, causing the severe business environment to persist.

Under these conditions, the Nippon Paper Group continued to progress with its First Medium-Term Business Plan and its reinforcement measures, including the reduction of variable costs and total labor costs, and the fortifying of the marketing structure for paper. These are all designed to firm up the business foundation of the Group to establish a highly profitable earnings structure on a consistent basis.

Net Sales, Costs, Expenses and Net Income

Confronted by the aforementioned operating environment, consolidated net sales in fiscal 2004 decreased 1.1%, or ¥12,952 million, compared with fiscal 2003 to ¥1,179,696 million.

In fiscal 2004, cost of sales edged down 0.6% to ¥914,384 million and comprised 77.5% of total net sales. Selling, general and administrative (SG&A) expenses amounted to ¥200,080 million, a decline of 8.0% compared with fiscal 2003. As a ratio of net sales SG&A expenses were 17.0%. Accounting for these factors, operating income climbed 17.2% to ¥65,231 million, while the ratio of operating income to net sales was 5.5%, an improvement of 0.8 of a percentage point.

For fiscal 2004, other income and expenses resulted in a net expense of ¥18,425 million. The major components were interest expense of ¥8,679 million, provision for doubtful receivables of ¥8,339 million, sup-

plementary retirement benefits of ¥6,134 million, and loss on restructuring of ¥4,997 million. Interest expense declined ¥2,432 million reflecting the reductions of interest-bearing debt, and refinancing initiatives that provided favorable interest rates on a portion of existing debt. The loss on restructuring is attributed to reorganization of the logs, lumber and building materials business conducted by subsidiary companies.

As a result, ordinary income advanced 24.0% compared with fiscal 2003 to ¥62,801 million. Income before income taxes and minority interests in consolidated subsidiaries totaled ¥46,805 million, an increase of 28.2%. Net income edged up 0.4% year on year to ¥24,350 million.

Net income per share was ¥21,996.96 compared with ¥22,025.22 fiscal 2003. Net income per diluted share was ¥21,107.50 against ¥21,132.64 in fiscal 2003. In connection with the return of profit to shareholders and investors, we strive to deliver acceptable returns by strengthening the Group's management and operating platforms, increasing its earnings power, and enhancing corporate value.

Accordingly, management strives to ensure stable dividends in the context of the Group's operating performance and retained earnings required for continuous growth. Taking into account these and other factors, we declared a full-year dividend of ¥8,000 per common share for fiscal 2004.

REVIEW OF OPERATIONS

Pulp and Paper Division

Looking at the Group's results in the paper business, steady advertising activity related to Upper House Elections and the Athens Olympics helped domestic sales volume of newsprint to remain on par with fiscal 2003 levels. Domestic sales volume of printing paper, primarily coated paper, in fiscal 2004 topped fiscal 2003 results. Contributing factors included robust demand for commercial printing surrounding digital home appliances, travel brochures and catalogs, and strong sales of new products at Nippon Paper Industries. We implemented sales price revisions for printing and business communication paper from autumn of 2004, aiming to pass on price increases for raw materials and fuels, which could not be completely absorbed by cost cutting measures.

Our domestic sales volume of paperboard remained on the same level with fiscal 2003 levels, with the summertime heat wave leading to strong sales to the beverage and digital home appliance industries. Effects from

several typhoons and earthquakes, which caused sluggish demand in fruit and vegetable applications and food-industry applications, offset these positive factors, however. Sales prices for linerboard in Japan remained at the same level as October 2003, when prices were revised.

In the household tissue business, we made positive efforts to respond to customer needs, implementing a campaign to commemorate the 40th anniversary since the release of Kleenex® tissue in Japan. Despite these efforts, increasingly severe competition caused large-scale decreases in sales prices for tissue and toilet paper, and sales volume fell below fiscal 2003 levels.

In response to these conditions, we worked to implement plans to improve earnings strength. As a result, net sales for fiscal 2004 decreased 2.2% compared with fiscal 2003 to finish at ¥870,360 million, while operating income increased 14.3% to ¥47,269 million. From fiscal 2004, the electricity supply business was shifted from the Pulp and Paper Division to the Other Division, and fiscal 2003 figures are adjusted for comparison purpose.

Paper-Related Division

Sales volume of liquid-packaging cartons, represented by PURE-PAK®, rose compared with fiscal 2003, boosted by effects from the summertime heat wave and by strong demand for tea and soy-based drinks resulting from greater concern about health issues.

We are seeing steady progress in rebuilding the production system after merging the six corrugated board companies in the Group into

one in October 2003. Marketing policies prioritizing profitability led to a slight decrease in sales volume compared with fiscal 2003, while sales prices remained at the same level as in December 2003, when prices were revised.

In chemical products, sales of chlorinated polyolefin for paint applications, and of ultrafine powdered cellulose for health food applications remained strong.

In the dissolving pulp business, rayon-related demand both in Japan and in export markets was solid, and sales results were strong.

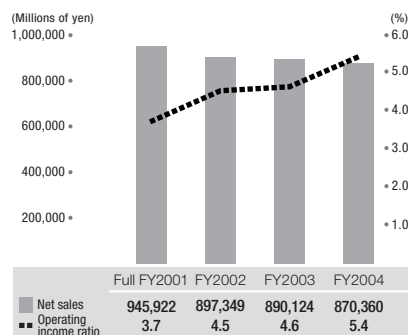
In the functional materials business, display materials such as optical film for liquid crystal panels and transfer film for projection televisions underwent rapid growth, and sales volume increased compared with fiscal 2003.

As a result of the above factors, net sales in the Paper-Related Division increased 2.3% compared with fiscal 2003, finishing at ¥126,592 million, and operating income surged 66.1% to ¥8,286 million.

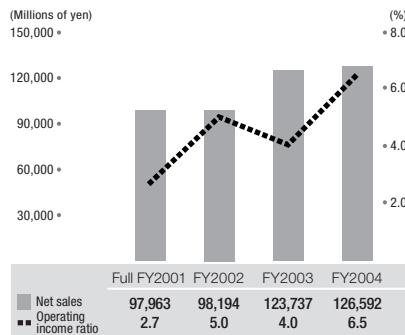
Housing and Construction Materials Division

In the Housing and Construction Materials Division, an increase in new housing starts led to a steady rise in net sales. Despite continued cost cutting measures, intensifying competition and depressed prices led to a decrease in operating income compared with fiscal 2003. As a result, net sales rose 1.9% compared with fiscal 2003 to ¥95,236 million, while operating income dropped 11.1% to ¥2,339 million.

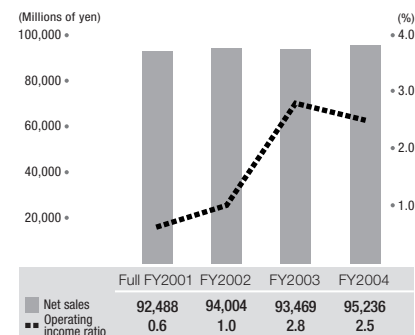
Pulp and Paper Division
Net sales and operating income ratio



Paper-Related Division
Net sales and operating income ratio



Housing and Construction Materials Division
Net sales and operating income ratio



Other Division

In the soft drink and other beverage business, effects from the numerous typhoons that hit Japan were offset by strong sales of major brands including Coca-Cola®, GEORGIA®, SOKENBICHA® and AQUARIUS®, as well as by progress in selling new health-related beverages, and sales volume increased year on year. Performance also remained solid in the logistics, leisure and other businesses. In addition, the electricity supply business of Nippon Paper Industries' Kushiro Mill commenced operations from October 2004. As a result of the above, net sales in the Other Division rose 2.6% from fiscal 2003 to ¥87,506 million, and operating income increased 9.6% to ¥7,336 million.

FINANCIAL POSITION

As of March 31, 2005, total assets stood at ¥1,529,975 million, a decrease of 6.6% from the end of fiscal 2003.

Total current assets also declined ¥33,471 million to ¥443,177 million. The principal component was deferred tax assets, which stood at ¥3,911 million, a drop of ¥13,988 million.

In property, plant and equipment, capital expenditure for the fiscal year fell below depreciation. Accordingly, property, plant and equipment decreased ¥56,666 million to ¥843,346 million. Total investments and other assets declined ¥17,253 million to ¥243,450 million. During fiscal 2004, investments in securities decreased due to a drop in stock prices. As a result, investments in securities as of March 31, 2005 stood at ¥85,483 million, down ¥7,352 million compared with the end of fiscal 2003.

The total of current and long-term liabilities dropped ¥121,690 million to ¥1,063,453 million. This was primarily attributed to the decline in bonds and long-term loans payable to ¥291,560 million, a decrease of ¥75,390 million, and in short-term loans payable and commercial paper to ¥318,920 million, a decrease of ¥44,012 million. Interest-bearing debt as of March 31, 2005 stood at ¥766,139 million, a decline of ¥76,139 million compared with the end of fiscal 2003.

In principle, we maintain a flexible funds procurement policy. Debt is incurred after due consideration of the most appropriate and advantageous terms and conditions. In general, we raise funds through the issue of corporate bonds, commercial paper, and debt finance from leading financial institutions. Proceeds are applied as working capital and for major capital expenditure.

Minority interests in consolidated subsidiaries as of March 31, 2005 stood at ¥23,644 million, an increase of ¥1,043 million.

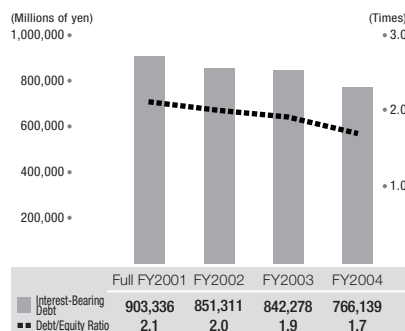
Total shareholders' equity climbed ¥13,255 million as of the end of fiscal 2004 to ¥442,876 million. Principal movements were attributed to net income and the payment of cash dividends. As a result, retained earnings rose ¥15,608 million to ¥133,653 million.

As a result of these and other factors, the equity ratio increased from 26.2% to 28.9%. In terms of market capitalization, the equity ratio declined from 37.1% to 35.4%.

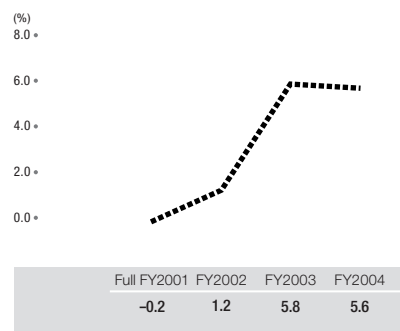
CASH FLOWS

Cash and cash equivalents (hereinafter referred to "cash") at the end of

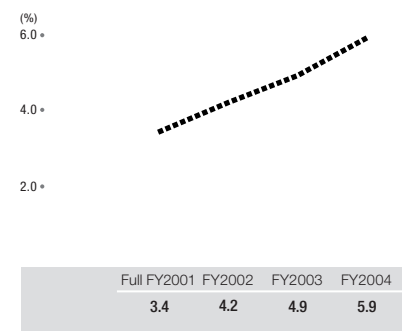
Interest-Bearing Debt and Debt/Equity Ratio



Return on Equity (ROE)



Return on Invested Capital (ROIC)



the fiscal year ended March 31, 2005 decreased 15.9% compared with fiscal 2003, to ¥18,181 million. Factors included cash used in investing activities for the purchase of property, plant and equipment, primarily related to capital expenditures in the Pulp and Paper Division. The outflow of cash was partially offset by proceeds from sales of property, plant and equipment, and by reduction of cash on hand.

Cash flows according to activity were as follows.

Cash Flows from Operating Activities

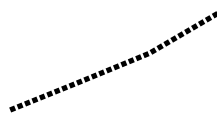
Cash provided by operating activities totaled ¥108,195 million, an increase of ¥21,106 million, or 24.2%, compared with fiscal 2003. The primary factor underlying the increase was the ¥23,467 million reduction in the payment associated with the decrease in payables, which had accumulated in relation to payables for integrating payable terms and conditions on the merger of Nippon Paper Industries and Daishowa Paper Manufacturing in April 2003.

Cash Flows from Investing Activities

Cash used in investing activities totaled ¥26,062 million, a decrease of ¥46,601 million, or 64.1% compared with fiscal 2003. Primary factors underlying the decrease included an increase of ¥15,240 million in proceeds from sales of property, plant and equipment; short-term loans going from a decrease of ¥5,599 million to an increase of ¥4,624 million; a reduction of ¥9,649 million in purchases of property, plant and equipment; and an increase of ¥6,904 million in proceeds from sales of marketable securities.

Return on Assets (ROA)

(%)
5.0 •
4.0 •
3.0 •
2.0 •
1.0 •



Full FY2001	FY2002	FY2003	FY2004
2.6	3.2	3.8	4.7

Cash Flows from Financing Activities

Cash used in financing activities totaled ¥86,009 million, an increase of ¥57,179 million, or 198.3%, compared with fiscal 2003. The primary factor underlying the increase was progress in reducing long-term debt and other interest-bearing debt.

Changes in the Group's cash flow indicators were as follows.

	Full FY2001	FY2002	FY2003	FY 2004
Equity ratio (%)	23.7	25.0	26.2	28.9
Equity ratio on a market capitalization base (%)	39.3	29.6	37.1	35.4
Years for debt redemption (years)	8.5	6.6	9.7	7.1
Interest coverage ratio	6.7	9.8	8.0	12.6

Notes: Equity ratio = Total shareholders' equity / Total assets × 100

Equity ratio on a market capitalization base = Market capitalization of shares / Total assets × 100

Years for debt redemption = Interest-bearing debt / Operating cash flows

Interest coverage ratio = Operating cash flows / Interest paid

- Indicators are all calculated based upon financial figures on a consolidated basis.
- Market capitalization of shares is calculated by multiplying the closing price of shares on the final trading day of the period by the number of shares outstanding at period end (not including treasury stock).
- Cash flows from operating activities as indicated in the consolidated statements of cash flows are utilized in calculations including operating cash flows. Interest-bearing debt includes all liabilities on the consolidated balance sheets for which the Company is paying interest. Concerning interest paid, the amount shown for "interest paid" on the consolidated statements of cash flow is utilized.
- The periods March 30, 2001-September 30, 2001 and October 1, 2001-March 31, 2002 are irregular periods and are counted as full fiscal 2001.

BUSINESS RISKS

Risks that may impact Group performance and/or financial position are as follows.

(1) Product demand and market trends

The Nippon Paper Group is involved in business activities including its core Pulp and Paper Division, and its Paper-Related Division, Housing and Construction Materials Division, and Other Division. Products of

Equity Ratio

(%)
30.0 •
20.0 •
10.0 •



Full FY2001	FY2002	FY2003	FY2004
23.7	25.0	26.2	28.9

these divisions are subject to risks related to changes in demand based upon economic conditions, and to risks related to changes in product sales prices based upon market trends. Such changes may affect business results and/or financial position.

(2) Changes in manufacturing conditions

The Group conducts production schedules based primarily upon forecasts that take into account both demand and current manufacturing equipment capacity. While regular inspections and servicing of all equipment is carried out to prevent incidents, the Group is subject to risks of decrease in capacity to supply products, which may be affected by factors such as decrease of operating rate in case of interruptions of manufacturing lines or trouble related to procurement of raw materials and fuels. In the event that such risks occur, business results and/or financial position may be affected.

(3) Currency exchange fluctuations

The Group is subject to risks regarding currency exchange fluctuations related to its import and export operations. Payments for imports of raw materials and fuels such as woodchips, heavy oil, coal, chemicals and other products exceed revenue from exports of products. Accordingly, in cases when the yen depreciates against foreign currencies, business results are negatively affected.

(4) Changes in raw material and fuel prices

The Group is involved in the business of purchasing raw materials and fuels such as woodchips, wastepaper, heavy oil, coal, chemicals and other products to manufacture and sell paper, pulp and other products. Accordingly, the Group is subject to risks surrounding changes in raw material and fuel prices on the international and domestic markets, and such changes may affect business results and/or financial position.

(5) Share prices

Because the Group holds marketable stock primarily in partner companies and affiliate companies, business results and/or financial position may be affected by changes in stock prices. In addition, changes in stock prices may cause changes in the amounts of pension expenses through changes in pension assets.

(6) Interest rates

The Group is subject to the risk of fluctuating interest rates due to a portion of interest-bearing debt being calculated according to variable interest rates. Changes in those interest rates, therefore, may affect business results and/or financial position.

(7) Overseas business

The Group is involved in overseas businesses such as the manufacturing and sale of pulp and paper, afforestation and other businesses in markets including North America, Northern Europe, China and Australia. Though the Group takes preventive measures against overseas business risks, in the event that unforeseen circumstances arise, business results and/or financial position may be affected.

(8) Legal issues

While the Group makes every effort to conduct business in compliance with laws and regulations, it is nonetheless subject to risks surrounding litigation in relation to its domestic and overseas business activities. In the event of such litigation, business results and/or financial position may be affected.

(9) Impairment of fixed assets

The Group owns a number of fixed assets including manufacturing equipment and land. In the event that such fixed assets decrease in value, business results and/or financial position may be affected.

(10) Other changes in the business environment

In addition to the items mentioned above, the Group is subject to changes in the business environment attributable to contingent events. Such changes may affect business results and/or financial position.

Consolidated Balance Sheets

Nippon Paper Group, Inc. and Consolidated Subsidiaries

	Millions of yen		Thousands of U.S. dollars (Note 3)
	March 31, 2004	March 31, 2005	March 31, 2005
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	¥ 21,624	¥ 18,181	\$ 169,916
Marketable securities (Note 13)	42	210	1,963
Receivables:			
Notes and accounts receivable:			
Trade	247,289	237,944	2,223,776
Unconsolidated subsidiaries and affiliates	16,072	12,282	114,785
Other	13,635	11,469	107,187
Loans receivable from unconsolidated subsidiaries and affiliates	13,489	12,162	113,664
Allowance for doubtful receivables	(2,048)	(1,999)	(18,682)
Inventories (Note 4)	134,616	131,834	1,232,093
Deferred tax assets (Note 8)	17,900	3,911	36,551
Other current assets (Note 7)	14,027	17,181	160,570
Total current assets	476,649	443,177	4,141,841
PROPERTY, PLANT AND EQUIPMENT (Note 6):			
Land	254,684	244,036	2,280,710
Buildings and structures	464,934	450,839	4,213,449
Machinery and equipment	1,872,601	1,838,858	17,185,589
Construction in progress	23,969	16,912	158,056
Other	21,218	21,042	196,654
	2,637,409	2,571,689	24,034,477
Less accumulated depreciation	(1,737,395)	(1,728,343)	(16,152,738)
Property, plant and equipment, net	900,013	843,346	7,881,738
INVESTMENTS AND OTHER ASSETS:			
Investments in and advances to unconsolidated subsidiaries and affiliates	87,246	87,430	817,103
Investments in securities (Notes 6 and 13)	92,835	85,483	798,907
Deferred tax assets (Note 8)	15,977	11,608	108,486
Other assets (Note 6)	114,191	110,549	1,033,168
Allowance for doubtful receivables	(49,547)	(51,621)	(482,439)
Total investments and other assets	260,703	243,450	2,275,234
TOTAL ASSETS (Note 14)	¥ 1,637,366	¥ 1,529,975	\$ 14,298,832

See notes to consolidated financial statements.

	Millions of yen		Thousands of U.S. dollars (Note 3)
	March 31, 2004	March 31, 2005	March 31, 2005
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Short-term borrowings (Note 5):			
Loans payable and commercial paper	¥ 362,933	¥ 318,920	\$ 2,980,561
Unconsolidated subsidiaries and affiliates	876	795	7,430
Current portion of long-term debt (Notes 5 and 6):			
Bonds and loans payable	111,518	154,862	1,447,308
Notes and accounts payable:			
Trade (Note 6)	108,354	108,584	1,014,804
Unconsolidated subsidiaries and affiliates	27,211	23,318	217,925
Other	78,315	66,789	624,196
Accrued income taxes (Note 8)	6,992	7,199	67,280
Other current liabilities (Note 8)	30,216	23,016	215,103
Total current liabilities	726,418	703,486	6,574,636
LONG-TERM LIABILITIES:			
Long-term debt (Notes 5 and 6):			
Bonds and loans payable	366,950	291,560	2,724,860
Accrued retirement benefits (Note 7)	72,064	60,038	561,103
Deferred tax liabilities (Note 8)	13,422	5,374	50,224
Other long-term liabilities	6,287	2,993	27,972
Total long-term liabilities	458,724	359,966	3,364,168
MINORITY INTERESTS IN CONSOLIDATED SUBSIDIARIES	22,601	23,644	220,972
CONTINGENT LIABILITIES (Note 12)			
SHAREHOLDERS' EQUITY (Notes 9 and 17):			
Common stock:			
Authorized — 3,000,000 shares;			
Issued — 1,105,235.63 shares in 2005 and 2004	55,730	55,730	520,841
Capital surplus	252,447	252,443	2,359,280
Retained earnings	118,044	133,653	1,249,093
Unrealized holding gain on other securities	15,427	13,181	123,187
Translation adjustments	(6,525)	(6,382)	(59,645)
	435,123	448,626	4,192,766
Less treasury stock, at cost:			
10,669.76 shares in 2005 and 10,163.81 shares in 2004	(5,502)	(5,749)	(53,729)
Total shareholders' equity	429,621	442,876	4,139,028
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	¥1,637,366	¥1,529,975	\$14,298,832

See notes to consolidated financial statements.

Consolidated Statements of Income

Nippon Paper Group, Inc. and Consolidated Subsidiaries

	Millions of yen		Thousands of U.S. dollars (Note 3)
	Fiscal year ended March 31, 2004	Fiscal year ended March 31, 2005	Fiscal year ended March 31, 2005
NET SALES (Note 14)	¥1,192,649	¥1,179,696	\$11,025,196
COST OF SALES (Notes 14 and 16)	919,602	914,384	8,545,645
GROSS PROFIT	273,047	265,312	2,479,551
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (Notes 14 and 16)	217,367	200,080	1,869,907
OPERATING INCOME (Note 14)	55,679	65,231	609,636
OTHER INCOME (expense):			
Interest expense	(11,112)	(8,679)	(81,112)
Interest and dividend income	2,561	2,473	23,112
Net gain on sales of investments in securities	498	2,967	27,729
Net gain (loss) on sales and disposal of property, plant and equipment	(3,698)	4,327	40,439
Equity in earnings of affiliates	3,207	1,993	18,626
Loss on devaluation of investments in securities	(725)	(941)	(8,794)
Provision for doubtful receivables	(258)	(8,339)	(77,935)
Gain on subsidies	680	—	—
Gain on return of substitutional portion of Welfare Pension Fund Plan	5,433	—	—
Loss on restructuring	(6,054)	(4,997)	(46,701)
Supplementary retirement benefits	(7,157)	(6,134)	(57,327)
Other, net	(2,535)	(1,094)	(10,224)
	(19,161)	(18,425)	(172,196)
INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS IN CONSOLIDATED SUBSIDIARIES	36,517	46,805	437,430
INCOME TAXES:			
Current	9,564	8,930	83,458
Deferred	1,334	12,154	113,589
	10,898	21,084	197,047
MINORITY INTERESTS IN CONSOLIDATED SUBSIDIARIES	(1,359)	(1,370)	(12,804)
NET INCOME	¥ 24,258	¥ 24,350	\$ 227,570
		Yen	U.S. dollars (Note 3)
AMOUNTS PER SHARE:			
Net income:			
Basic	¥22,025.22	¥21,996.96	\$ 205.58
Diluted	21,132.64	21,107.50	197.27
Cash dividends	8,000.00	8,000.00	74.77

See notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

Nippon Paper Group, Inc. and Consolidated Subsidiaries

	Millions of yen						
	Number of shares of issued common stock	Common stock	Capital surplus	Retained earnings	Unrealized holding gain (loss) on other securities	Translation adjustments	Less treasury stock at cost
Balance at March 31, 2003	1,105,235.63	¥55,730	¥252,964	¥112,668	¥ (743)	¥(4,391)	¥(8,025)
Disposition of treasury stock	—	—	(517)	—	—	—	—
Cash dividends paid	—	—	—	(13,094)	—	—	—
Bonuses to directors and statutory auditors	—	—	—	(198)	—	—	—
Net income	—	—	—	24,258	—	—	—
Net change during the year	—	—	—	—	16,170	(2,134)	2,523
Adjustments for inclusion or exclusion of certain subsidiaries in/from consolidation	—	—	—	(5,591)	—	—	—
Balance at March 31, 2004	1,105,235.63	55,730	252,447	118,044	15,427	(6,525)	(5,502)
Disposition of treasury stock	—	—	(3)	—	—	—	—
Cash dividends paid	—	—	—	(8,762)	—	—	—
Bonuses to directors and statutory auditors	—	—	—	(202)	—	—	—
Net income	—	—	—	24,350	—	—	—
Adjustments for merger of consolidated subsidiary and unconsolidated subsidiary	—	—	—	178	—	—	—
Net change during the year	—	—	—	—	(2,246)	144	(247)
Adjustments for exclusion of certain subsidiaries from consolidation	—	—	—	44	—	—	—
Balance at March 31, 2005	1,105,235.63	¥55,730	¥252,443	¥133,653	¥13,181	¥(6,382)	¥(5,749)

	Thousands of U.S. dollars (Note 3)						
	Common stock	Capital surplus	Retained earnings	Unrealized holding gain (loss) on other securities	Translation adjustments	Less treasury stock at cost	
Balance at March 31, 2004	\$520,841	\$2,359,318	\$1,103,215	\$144,178	\$(60,981)	\$(51,421)	
Disposition of treasury stock	—	(28)	—	—	—	—	
Cash dividends paid	—	—	(81,888)	—	—	—	
Bonuses to directors and statutory auditors	—	—	(1,888)	—	—	—	
Net income	—	—	227,570	—	—	—	
Adjustments for merger of consolidated subsidiary and unconsolidated subsidiary	—	—	1,664	—	—	—	
Net change during the year	—	—	—	(20,991)	1,346	(2,308)	
Adjustments for exclusion of certain subsidiaries from consolidation	—	—	411	—	—	—	
Balance at March 31, 2005	\$520,841	\$2,359,280	\$1,249,093	\$123,187	\$(59,645)	\$(53,729)	

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Nippon Paper Group, Inc. and Consolidated Subsidiaries

	Millions of yen		Thousands of U.S. dollars (Note 3)
	Fiscal year ended March 31, 2004	Fiscal year ended March 31, 2005	Fiscal year ended March 31, 2005
OPERATING ACTIVITIES			
Income before income taxes and minority interests in consolidated subsidiaries	¥ 36,517	¥ 46,805	\$ 437,430
Adjustments to reconcile income before income taxes and minority interests in consolidated subsidiaries to net cash provided by operating activities:			
Depreciation	81,259	74,971	700,664
Amortization of consolidation account adjustment	2,299	2,028	18,953
Increase (decrease) in allowance for doubtful receivables	(212)	9,107	85,112
Decrease in accrued retirement benefits	(1,438)	(10,945)	(102,290)
Decrease in allowance for losses on guarantees	(522)	—	—
Interest and dividend income	(2,561)	(2,473)	(23,112)
Interest expense	11,112	8,679	81,112
Equity in earnings of affiliates	(3,207)	(1,993)	(18,626)
Net gain on sales of investments in securities	(498)	(2,967)	(27,729)
Net (gain) loss on sales and disposal of property, plant and equipment	3,698	(4,327)	(40,439)
Loss on devaluation of investments in securities	725	941	8,794
Gain on return of substitutional portion of Welfare Pension Fund Plan	(5,433)	—	—
Supplementary retirement benefits	7,157	6,134	57,327
Loss on restructuring	6,054	4,997	46,701
Bonuses paid to directors and statutory auditors	(223)	(219)	(2,047)
Changes in operating assets and liabilities:			
Receivables	(7,169)	13,869	129,617
Inventories	4,939	895	8,364
Payables	(32,582)	(9,114)	(85,178)
Other	13,624	(5,736)	(53,607)
	113,539	130,655	1,221,047
Interest and dividends received	2,786	2,724	25,458
Interest paid	(10,929)	(8,601)	(80,383)
Payment of supplementary retirement benefits	(4,755)	(8,321)	(77,766)
Expenditures for restructuring	(2,587)	(2,951)	(27,579)
Income taxes paid	(10,965)	(5,308)	(49,607)
Net cash provided by operating activities	87,089	108,195	1,011,168

	Millions of yen		Thousands of U.S. dollars (Note 3)
	Fiscal year ended March 31, 2004	Fiscal year ended March 31, 2005	Fiscal year ended March 31, 2005
INVESTING ACTIVITIES			
Purchases of time deposits	¥ (294)	¥ (168)	\$ (1,570)
Withdrawals of time deposits	651	192	1,794
Proceeds from sales of marketable securities	173	31	290
Purchases of property, plant and equipment	(66,321)	(56,672)	(529,645)
Proceeds from sales of property, plant and equipment	2,350	17,591	164,402
Purchases of investments in other securities	(7,044)	(1,678)	(15,682)
Proceeds from sales of investments in other securities	3,146	10,050	93,925
Proceeds from sales of a subsidiary's stock resulting in change in scope of consolidation	323	3,230	30,187
Decrease (increase) in short-term loans	(5,599)	4,624	43,215
Long-term loans made	(2,924)	(6,385)	(59,673)
Collection of long-term loans	1,756	1,927	18,009
Other, net	1,118	1,193	11,150
Net cash used in investing activities	(72,664)	(26,062)	(243,570)
FINANCING ACTIVITIES			
Decrease in short-term borrowings	(9,095)	(42,788)	(399,888)
Proceeds from issuance of long-term debt	134,277	75,200	702,804
Repayment of long-term debt	(139,082)	(107,602)	(1,005,626)
Purchases of treasury stock	(77)	(262)	(2,449)
Proceeds from sales of treasury stock	413	38	355
Cash dividends paid	(13,544)	(9,054)	(84,617)
Principal payments under finance lease obligations	(1,720)	(1,540)	(14,393)
Net cash used in financing activities	(28,830)	(86,009)	(803,822)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	244	113	1,056
DECREASE IN CASH AND CASH EQUIVALENTS	(14,160)	(3,763)	(35,168)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	35,187	21,624	202,093
(DECREASE) INCREASE DUE TO INCLUSION OR EXCLUSION OF CERTAIN SUBSIDIARIES IN/FROM CONSOLIDATION	597	(82)	(766)
INCREASE DUE TO MERGER OF UNCONSOLIDATED SUBSIDIARIES	—	403	3,766
CASH AND CASH EQUIVALENTS AT END OF YEAR	¥ 21,624	¥ 18,181	\$ 169,916

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Nippon Paper Group, Inc. and Consolidated Subsidiaries March 31, 2005

1. Description of Business

Based on a resolution approved at the ordinary general meeting of shareholders held on June 29, 2004, Nippon Unipac Holding changed its name to Nippon Paper Group, Inc. (the "Company") from October 1, 2004.

The Company was established as a business combination on March 30, 2001 by a transfer of shares of common stock from the shareholders of both Nippon Paper Industries Co., Ltd. (the "former Nippon Paper") and Daishowa Paper Manufacturing Co., Ltd. ("Daishowa Paper") to the Company in accordance with the procedures stipulated in the Commercial Code of Japan. As a result of this stock transfer, the former Nippon Paper and Daishowa Paper became wholly-owned subsidiaries of the Company. In addition, the Company acquired ownership of 100% of the shares of Japan Paperboard Industries Co., Ltd. as a result of an exchange of shares on October 1, 2002.

On April 1, 2003, the new Nippon Paper Industries Co., Ltd. ("Nippon Paper") was established following the merger of the former Nippon Paper and Daishowa Paper, and Japan Paperboard Industries Co., Ltd. changed its name to Nippon Daishowa Paperboard Co., Ltd. Under this business structure, the paper and paperboard businesses, which are our core businesses, were combined, restructured, and launched under a new structural plan. The paper business belonged to Nippon Paper and the paperboard business belonged to Nippon Daishowa Paperboard Co., Ltd.

2. Summary of Significant Accounting Policies

(a) Basis of Preparation

The accompanying consolidated financial statements of the Company and consolidated subsidiaries are prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and are compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan.

The Company has prepared the consolidated statements of shareholders' equity and certain additional information for the purpose of inclusion in this report although such statements and information are not customarily prepared in Japan.

Certain amounts in the financial statements of the fiscal year ended March 31, 2004 have been reclassified to conform to the presentation of the fiscal year ended March 31, 2005.

As permitted, amounts of less than one million yen have been omitted. As a result, the totals shown in the accompanying consolidated financial statements (both in yen and U.S. dollars) do not necessarily agree with the sums of the individual amounts.

(b) Consolidation

The accompanying consolidated financial statements include the accounts of the Company and all subsidiaries over which it exerts substantial control either through majority ownership of voting stock and/or by other means. All significant intragroup balances and transactions have been eliminated in consolidation.

In the consolidation of the former Nippon Paper and Daishowa Paper, the Company comprehensively applied the pooling-of-interest method to the former Nippon Paper and its subsidiaries as the acquiring group, and the purchase method to Daishowa Paper and its subsidiaries as the acquired group, after considering the ratio for the share transfer of each company as well as certain other factors.

Certain foreign subsidiaries are consolidated on the basis of fiscal periods ending December 31, a closing date which differs from that of the Company; however, the necessary adjustments have been made if the effect of the difference is deemed material.

Investments in equity method affiliates (companies over which the Company has the ability to exercise significant influence) are stated at cost plus equity in their undistributed earnings or losses. Consolidated net income includes the Company's equity in the current net income or loss of such companies after the elimination of unrealized intragroup profits.

All assets and liabilities of the consolidated subsidiaries are revaluated at fair value on the date of acquisition, if applicable, and the excess of cost over the underlying net assets is amortized over a period of five years on a straight-line basis if such excess is material, or charged to income when incurred if immaterial.

Goodwill arising from the application of the purchase method is being amortized over a period of twenty years on a straight-line basis. Goodwill is included in other assets in the consolidated balance sheets.

(c) Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments, generally with original maturities of three months or less, which are readily convertible to known amounts of cash and are so near maturity that they present only an insignificant risk of any changes in their value resulting from interest-rate fluctuation.

(d) Securities

The Company and consolidated subsidiaries have adopted an accounting standard for financial instruments which requires securities to be classified into three categories: trading, held-to-maturity or other securities, as follows:

- (i) trading securities are carried at fair value although the Company and consolidated subsidiaries had no such securities at either March 31, 2005 or 2004;
- (ii) held-to-maturity securities are carried at cost and amortized by the straight-line method; and
- (iii) marketable securities classified as other securities are carried at fair value with any changes in unrealized holding gain or loss, net of the applicable income taxes, included directly in shareholders' equity. Non-marketable securities classified as other securities are carried at cost.

(e) Inventories

Inventories are stated at cost determined principally by the moving average method or the average method.

(f) Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is, in general, computed mainly by the declining-balance method over the estimated useful lives of

the respective assets, except for new buildings acquired after March 31, 1998 on which depreciation is calculated by the straight-line method. Significant renewals and betterments are capitalized at cost. Maintenance and repairs are charged to income as incurred.

(g) Leases

Noncancelable leases of the domestic consolidated subsidiaries are accounted for as operating leases (whether such leases are classified as operating or finance leases) except that lease agreements which stipulate the transfer of ownership of the leased assets to the lessee are accounted for as finance leases.

(h) Foreign Currency Translation

All assets and liabilities denominated in foreign currencies other than those hedged by forward foreign exchange contracts etc. are translated into yen at the current rates. All revenues and expenses associated with foreign currencies are translated at the rates of exchange prevailing when such transactions were made. Translation gain or loss is credited or charged to income currently.

The balance sheet accounts of the foreign consolidated subsidiaries and affiliates are translated into yen at the rates of exchange in effect at their balance sheet dates, except for the components of shareholders' equity which are translated at their historical exchange rates. Revenue and expense accounts are translated at the average rate of exchange in effect during the fiscal year. The Company has presented translation adjustments as a component of shareholders' equity and minority interests in consolidated subsidiaries in the accompanying consolidated financial statements.

(i) Retirement Benefits

Accrued retirement benefits for employees at March 31, 2005 have been provided mainly at an amount calculated based on the retirement benefit obligation less the fair value of the pension plan assets as of March 31, 2005, as adjusted for unrecognized actuarial gain or loss, and unrecognized prior service cost. The retirement benefit obligation is attributed to each fiscal year by the straight-line method over the estimated remaining years of service of the eligible employees.

Actuarial gain or loss is amortized in the years following the year in which the gain or loss is recognized primarily by the straight-line method over periods (10 years through 15 years) which are shorter than the average estimated remaining years of service of the eligible employees.

Prior service cost is being amortized as incurred by the straight-line method over periods (5 years through 15 years) which are shorter than the average estimated remaining years of service of the eligible employees.

See Note 7 for the method of accounting for the separation of the substitutional portion of the obligation from the corporate portion of the benefit obligation under the Welfare Pension Fund Plan.

In addition, directors and statutory auditors of the Company and its consolidated subsidiaries are customarily entitled to lump-sum payments under an unfunded retirement benefit plan. Provisions for retirement allowances for these officers are accounted based on the rules of the Company and its consolidated subsidiaries.

(j) Research and Development Costs

Research and development costs are charged to income as incurred.

(k) Derivatives

Certain consolidated subsidiaries have entered into various derivatives transactions in order to manage certain risks arising from adverse fluctuation in foreign currency exchange rates and interest rates. Unrealized gain or loss is principally deferred as an asset or a liability. Receivables and payables hedged by qualified forward foreign exchange contracts are translated at their corresponding contract rates.

(l) Income Taxes

The Company and consolidated subsidiaries have adopted tax-effect accounting in accordance with an accounting standard which requires recognition of income taxes by the liability method. Under the liability method, deferred tax assets and liabilities are determined based on the difference between the amounts for financial reporting purposes and the tax bases of the assets and liabilities, and are measured using the enacted tax rates and laws which will be in effect when the differences are expected to reverse.

(m) Appropriation of Retained Earnings

Under the Commercial Code of Japan, the appropriation of retained earnings with respect to a given fiscal period is made by resolution of an ordinary general meeting of shareholders held subsequent to the close of the fiscal period and the accounts for such period, therefore, do not reflect such appropriations. See Note 17.

The Commercial Code of Japan provides that an amount equal to at least 10% of the amounts to be disbursed as distributions of earnings be appropriated to the legal reserve until the sum of the additional paid-in capital and the legal reserve equals 25% of the common stock account. The Code also stipulates that, to the extent that the sum of the additional paid-in capital account and the legal reserve exceeds 25% of the common stock account, the amount of any such excess is available for appropriation by resolution of the shareholders.

(n) Amounts per Share

Basic net income per share is computed based on the net income available for distribution to shareholders of common stock and the weighted-average number of shares of common stock outstanding during the fiscal year. Diluted net income per share is computed based on the net income available for distribution to the shareholders and the weighted-average number of shares of common stock outstanding during each fiscal year after giving effect to the dilutive potential of shares of common stock to be issued upon the conversion of convertible bonds.

Cash dividends per share represent the cash dividends declared as applicable to the respective fiscal year.

3. U.S. Dollar Amounts

Amounts in U.S. dollars are included solely for the convenience of the reader. The rate of ¥107 = U.S.\$1.00, the approximate rate of exchange in effect on March 31, 2005, has been used. This translation should not be construed as a

representation that yen have been, could have been, or could in the future be, converted into U.S. dollars at the above or any other rate.

4. Inventories

Inventories at March 31, 2005 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Merchandise and finished products	¥ 77,337	¥ 73,935	\$ 690,981
Work in process	15,568	15,326	143,234
Raw materials and supplies	41,709	42,573	397,879
	¥134,616	¥131,834	\$1,232,093

5. Short-Term Borrowings and Long-Term Debt

At March 31, 2005 and 2004, short-term borrowings consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Loans from banks	¥283,933	¥252,920	\$2,363,738
Loans from unconsolidated subsidiaries and affiliates	876	795	7,430
Commercial paper	79,000	66,000	616,822
	¥363,809	¥319,716	\$2,988,000

Loans from banks are unsecured and generally represent 365-day notes. The weighted-average interest rates of the short-term bank loans outstanding at March 31, 2005 and 2004 were 0.53% and 0.56%, respectively.

Long-term debt at March 31, 2005 and 2004 is summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Loans from banks, insurance companies and others at rates ranging from 5.65% to 0.619% due through 2034:			
With collateral	¥ 146,954	¥ 95,876	\$ 896,037
Without collateral	169,014	194,547	1,818,196
0.81% unsecured corporate bonds in yen due 2010	20,000	20,000	186,916
0.50% unsecured corporate bonds in yen due 2007	20,000	20,000	186,916
0.91% unsecured corporate bonds in yen due 2008	20,000	20,000	186,916
0.51% unsecured corporate bonds in yen due 2006	10,000	10,000	93,458
0.89% unsecured corporate bonds in yen due 2009	—	30,000	280,374
2.975% unsecured corporate bonds in yen due 2005 (consolidated subsidiary)	25,000	25,000	233,645
2.075% unsecured corporate bonds in yen due 2004 (consolidated subsidiary)	15,000	—	—

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
2.12% unsecured corporate bonds in yen due 2004 (consolidated subsidiary)	20,000	—	—
0.2% unsecured exchangeable bonds in yen due 2006 (consolidated subsidiary)	31,000	31,000	289,720
1.66% unsecured corporate bonds in yen due 2005 (consolidated subsidiary)	1,500	—	—
	478,468	446,423	4,172,178
Less current portion	(111,518)	(154,862)	(1,447,308)
	¥ 366,950	¥ 291,560	\$ 2,724,860

Exchangeable bonds issued by a consolidated subsidiary, unless previously redeemed, are exchangeable into shares of common stock of the Company as follows:

	Current exchange price per share	Exchange period (up to and including)
0.2% exchangeable bonds due 2006	¥645,000	March 30, 2006

At March 31, 2005, if all the outstanding exchangeable bonds had been exchanged, approximately 48 thousand new shares of the Company would have been issuable.

Under the provisions of this issue, the exchange price is subject to adjustment in certain cases which include stock splits.

Long-term debt maturities subsequent to March 31, 2005 are summarized as follows:

Fiscal years ending March 31,	Millions of yen	Thousands of U.S. dollars
2006	¥154,862	\$1,447,308
2007	28,618	267,458
2008	59,750	558,411
2009	56,270	525,888
2010 and thereafter	146,921	1,373,093
	¥446,423	\$4,172,178

6. Pledged Assets

Assets pledged as collateral for notes and accounts payable—trade of ¥82 million (\$766 thousand), the current portion of long-term debt of ¥8,565 million (\$80,047 thousand), and long-term debt of ¥87,310 million (\$815,981 thousand) at March 31, 2005 were as follows:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Property, plant and equipment, at net book value	¥472,319	¥447,939	\$4,186,346
Investments in securities	15,836	470	4,393
Other assets	254	—	—
	¥488,409	¥448,409	\$4,190,738

7. Retirement Benefits

Certain consolidated subsidiaries have defined benefit plans, i.e., corporate pension fund plans, Welfare Pension Fund Plans, tax-qualified pension plans and lump-sum payment plans, covering substantially all employees who are entitled to lump-sum or annuity payments, the amounts of which are determined by reference to their basic rates of pay, length of service, and the conditions under which termination occurs.

The following table sets forth the funded and accrued status of the plans, and the amounts recognized in the consolidated balance sheets at March 31, 2005 and 2004 for the consolidated subsidiaries' defined benefit plans:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Retirement benefit obligation	¥(217,628)	¥(197,253)	\$(1,843,486)
Plan assets at fair value	124,191	127,411	1,190,757
Unfunded retirement benefit obligation	(93,437)	(69,842)	(652,729)
Unrecognized actuarial loss	29,094	26,352	246,280
Unrecognized prior service cost	(673)	(10,870)	(101,589)
Net retirement benefit obligation	(65,016)	(54,360)	(508,037)
Prepaid pension cost	4,838	3,414	31,907
Accrued retirement benefits	¥ (69,854)	¥ (57,774)	\$ (539,944)

In addition, accrued benefits for directors and statutory auditors of the Company and its consolidated subsidiaries in amounts of ¥2,263 million (\$21,150 thousand) and ¥2,209 million have been included in accrued retirement benefits at March 31, 2005 and 2004, respectively.

The components of retirement benefit expenses for the fiscal years ended March 31, 2005 and 2004 are outlined as follows:

	Millions of yen		Thousands of U.S. dollars
	Fiscal year ended March 31, 2004	Fiscal year ended March 31, 2005	Fiscal year ended March 31, 2005
Service cost	¥ 7,552	¥ 5,983	\$ 55,916
Interest cost	6,920	5,156	48,187
Expected return on plan assets	(1,924)	(2,040)	(19,065)
Amortization of unrecognized actuarial loss	5,643	2,547	23,804
Amortization of unrecognized prior service cost	3	(242)	(2,262)
Gain on return of the substitutional portion of Welfare Pension Fund Plan	(5,433)	—	—
Settlement gain on defined contribution pension plan	—	(334)	(3,121)
Total	¥12,761	¥11,069	\$103,449

In addition to the above, supplementary retirement benefits of ¥6,153 million (\$57,505 thousand) and ¥7,157 million were recorded for the fiscal years ended March 31, 2005 and 2004, respectively. Supplementary retirement benefits have been included in other expense except for ¥19 million (\$178 thousand) which have been included in selling, general and administrative expenses for the fiscal year ended March 31, 2005.

Nippon Paper received approval from the Minister of Health, Labor and Welfare in the fiscal year ended March 31, 2004 with respect to its application for exemption from the obligation for benefits related to future employee services under the substitutional portion of the Welfare Pension Fund Plan. In accordance with the transitional provision stipulated in Study Report No. 13 of the Accounting System Committee of the Japanese Institute of Certified Public Accountants, "Practical Guidelines for Accounting for Retirement Benefits," Nippon Paper accounted for the separation of the substitutional portion from the corporate portion of the benefit obligation under its Welfare Pension Fund Plan as of the date of approval for the exemption, assuming that the transfer to the Japanese government of the substitutional portion of the benefit obligation and related pension plan assets had been completed as of the date. As a result, Nippon Paper recognized a gain of ¥5,433 million for the fiscal year ended March 31, 2004. The pension assets to be transferred were calculated at ¥33,729 million for Nippon Paper at March 31, 2004.

In January 2005, Nippon Paper received approval from the Minister of Health, Labor and Welfare with respect to its application for exemption from the obligation for the payment of benefits related to past employee services under the substitutional portion of the Welfare Pension Fund Plan.

In April 2005, a certain consolidated subsidiary converted a portion of its defined benefit pension plan to a defined contribution pension plan and accounted for the transfer as settlement of the pension plan and recognized settlement gain on certain pension plan of ¥334 million (\$3,121 thousand) pursuant to Financial Accounting Standards Implementation Guidance No. 1, "Accounting for Transfers between Retirement Benefit Plans" issued by Accounting Standards Board of Japan.

The assumptions used in accounting for the above plans were as follows:

	Fiscal year ended March 31, 2004	Fiscal year ended March 31, 2005
Discount rate	mainly 2.5%	mainly 2.5%
Expected rate of return on plan assets	mainly 2.0%	mainly 2.0%

8. Income Taxes

The Company and its domestic consolidated subsidiaries are subject to a number of taxes based on earnings, i.e. corporation tax, inhabitants' taxes and enterprise tax, which, in the aggregate, resulted in the statutory tax rates of approximately 40.7% and 42.1% for the fiscal years ended March 31, 2005 and 2004, respectively.

The effective tax rates reflected in the consolidated statements of income for the fiscal years ended March 31, 2005 and 2004 differ from the statutory tax rates for the following reasons:

	Fiscal year ended March 31, 2004	Fiscal year ended March 31, 2005
Statutory tax rates	42.1%	40.7%
Effect of:		
Permanent differences—entertainment expenses	2.7	2.1
Non-taxable dividends received	1.1	0.9
Equity in earnings of affiliates	(3.7)	(1.8)
Amortization of consolidation account adjustment	2.6	1.7
Inhabitants' per capita taxes	1.9	0.6
Provision of valuation allowance	3.8	14.0
Recognition of devaluation loss for a consolidated subsidiary and affiliates	(20.3)	(12.8)
Other, net	(0.4)	(0.4)
Effective tax rates	29.8%	45.0%

The significant components of the deferred tax assets and liabilities held by the Company and its consolidated subsidiaries at March 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Deferred tax assets:			
Accrued bonuses	¥ 4,075	¥ 3,999	\$ 37,374
Accrued enterprise tax	570	993	9,280
Accrued allowance for doubtful receivables	11,850	10,658	99,607
Accrued retirement benefits	34,755	30,819	288,028
Accrued officers' retirement benefits	582	899	8,402
Accrual for loss on investment securities	1,970	2,992	27,963
Devaluation loss on a consolidated subsidiary and affiliates	—	7,794	72,841
Tax loss carryforwards	21,148	13,851	129,449
Unrealized profit eliminated in consolidation	4,971	2,115	19,766
Other	5,661	3,083	28,813
	85,586	77,207	721,561
Valuation allowance	(16,024)	(22,553)	(210,776)
	69,561	54,653	510,776

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Deferred tax liabilities:			
Tax reserves	(8,166)	(8,908)	(83,252)
Accumulated depreciation	(1,191)	(1,337)	(12,495)
Valuation differences on land, etc.	(27,919)	(24,163)	(225,822)
Investments in other securities	(11,280)	(9,428)	(88,112)
Other	(550)	(672)	(6,280)
	(49,108)	(44,510)	(415,981)
Net deferred tax assets	¥ 20,453	¥ 10,143	\$ 94,794

Deferred tax liabilities included in other current liabilities at March 31, 2005 and 2004 accounted to ¥3 million (\$28 thousand) and ¥2 million, respectively.

9. Shareholders' Equity

In accordance with the Commercial Code of Japan (the "Code"), the Company has provided a legal reserve, which is included in retained earnings. The Code provides that an amount equal to at least 10% of the amount to be disbursed as distributions of earnings be appropriated to the legal reserve until the total of such reserve and the capital surplus account equals 25% of the common stock account. The legal reserve amounted to ¥432 million (\$4,037 thousand) at both March 31, 2005 and 2004.

The Code stipulates that neither capital surplus nor the legal reserve is available for dividends. But if the total amount of capital surplus and the legal reserve exceeds 25% of the common stock account, the excess may be distributed to the shareholders either as a return of capital or as dividends subject to the approval of the shareholders.

The Code stipulates that neither capital surplus nor the legal reserve may be used to reduce or eliminate a deficit by resolution of the shareholders or may be transferred to common stock by resolution of the Board of Directors.

10. Supplemental Cash Flow Information

Assets and liabilities excluded from the consolidated balance sheet at March 31, 2005 as a result of sale of a certain subsidiary were as follows:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Current assets	¥ 3,008		\$ 28,112
Non-current assets	13,217		123,523
Total assets	¥16,226		\$151,645
Current liabilities	¥ 2,971		\$ 27,766
Non-current liabilities	1,130		10,561
Total liabilities	¥ 4,102		\$ 38,336

11. Leases

(a) As Lessee

- (i) The following pro forma amounts represent the amounts equivalent to the acquisition costs, accumulated depreciation and net book value of the leased assets at March 31, 2005 and 2004, which would have been reflected in the balance sheets if finance lease accounting had been applied to the finance leases currently accounted for as operating leases:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Amount equivalent to acquisition costs:			
Machinery and equipment	¥9,888	¥9,264	\$86,579
Amount equivalent to accumulated depreciation:			
Machinery and equipment	¥5,101	¥4,952	\$46,280
Amount equivalent to net book value:			
Machinery and equipment	¥4,786	¥4,312	\$40,299

Lease expenses relating to finance leases accounted for as operating leases for the fiscal years ended March 31, 2005 and 2004 amounted to ¥1,591 million (\$14,869 thousand) and ¥1,783 million, respectively.

The pro forma depreciation of the finance leases accounted for as operating leases for the fiscal years ended March 31, 2005 and 2004 amounted to ¥1,591 million (\$14,869 thousand) and ¥1,783 million, respectively, and were computed by the straight-line method over the respective lease terms of the assets accounting nil residual value.

Future minimum lease payments (including the interest portion thereon) subsequent March 31, 2005 for finance leases accounted for as operating leases are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Fiscal years ending March 31:		
2006	¥1,440	\$13,458
2007 and thereafter	3,075	28,738
Total	¥4,516	\$42,206

- (ii) Future minimum lease payments subsequent to March 31, 2005 for non-cancelable operating leases are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Fiscal years ending March 31:		
2006	¥1,449	\$13,542
2007 and thereafter	777	7,262
Total	¥2,227	\$20,813

(b) As Lessor

- (i) The following amounts represent the acquisition costs, accumulated depreciation and net book value of the leased assets relating to finance leases accounted for as operating leases at March 31, 2005 and 2004:

	Millions of yen		Thousands of U.S. dollars
	March 31, 2004	March 31, 2005	March 31, 2005
Acquisition costs:			
Machinery and equipment	¥127	¥5	\$47
Accumulated depreciation:			
Machinery and equipment	¥113	¥3	\$28
Net book value:			
Machinery and equipment	¥ 14	¥2	\$19

Lease income relating to finance leases accounted for as operating leases in the accompanying consolidated financial statements totaled ¥12 million (\$112 thousand) and ¥19 million for the fiscal years ended March 31, 2005 and 2004, respectively. Depreciation of the assets leased under finance leases accounted for as operating leases totaled ¥12 million (\$112 thousand) and ¥19 million for the fiscal years ended March 31, 2005 and 2004, respectively.

Future minimum lease income (including the interest portion thereon) subsequent to March 31, 2005 for finance leases accounted for as operating leases is summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Fiscal years ending March 31:		
2006	¥ 36	\$ 336
2007 and thereafter	144	1,346
Total	¥181	\$1,692

- (ii) Future minimum lease income subsequent to March 31, 2005 for noncancelable operating leases is summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Fiscal years ending March 31:		
2006	¥33	\$308
2007 and thereafter	57	533
Total	¥91	\$850

12. Contingent Liabilities

The consolidated subsidiaries had the following contingent liabilities at March 31, 2005:

	Millions of yen	Thousands of U.S. dollars
As guarantors of indebtedness of unconsolidated subsidiaries, affiliates and others	¥31,320	\$292,710

13. Securities

(a) (i) Marketable securities classified as held-to-maturity debt securities and other securities at March 31, 2005 are summarized as follows:

Marketable held-to-maturity debt securities

	Millions of yen			Thousands of U.S. dollars		
	March 31, 2005					
	Carrying value	Estimated fair value	Unrealized gain (loss)	Carrying value	Estimated fair value	Unrealized gain (loss)
Securities whose fair value exceeds their carrying value:						
Government bonds	¥270	¥270	¥ 0	\$2,523	\$2,523	\$ 0
Corporate bonds	100	100	0	935	935	0
Subtotal	370	371	1	3,458	3,467	9
Securities whose carrying value exceeds their fair value:						
Government bonds	10	10	(0)	93	93	(0)
Subtotal	10	10	(0)	93	93	(0)
Total	¥380	¥381	¥ 1	\$3,551	\$3,561	\$ 9

Marketable other securities

	Millions of yen			Thousands of U.S. dollars		
	March 31, 2005					
	Cost	Carrying value	Unrealized gain (loss)	Cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their cost:						
Equity securities	¥25,323	¥47,880	¥22,556	\$236,664	\$447,477	\$210,804
Subtotal	25,323	47,880	22,556	236,664	447,477	210,804
Securities whose cost exceeds their carrying value:						
Equity securities	4,873	4,024	(848)	45,542	37,607	(7,925)
Subtotal	4,873	4,024	(848)	45,542	37,607	(7,925)
Total	¥30,196	¥51,905	¥21,708	\$282,206	\$485,093	\$202,879

(ii) Sales of securities classified as other securities amounted to ¥9,868 million (\$92,224 thousand) with an aggregate gain of ¥6,293 million (\$58,813 thousand) and loss of ¥28 million (\$262 thousand) for the fiscal year ended March 31, 2005.

(iii) The redemption schedule at March 31, 2005 for securities with maturity dates classified as other securities and held-to-maturity debt securities is summarized as follows:

	Millions of yen			Thousands of U.S. dollars		
	March 31, 2005					
	Due in one year or less	Due after one year through five years	Due after five years	Due in one year or less	Due after one year through five years	Due after five years
Government bonds	¥ 10	¥270	¥—	\$ 93	\$2,523	\$—
Corporate bonds	200	75	—	1,869	701	—
Total	¥210	¥345	¥—	\$1,963	\$3,224	\$—

(iv) Non-marketable securities classified as held-to-maturity debt securities and other securities at March 31, 2005 are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
	March 31, 2005	March 31, 2005
Carrying value		
Held-to-maturity debt securities:		
Unlisted bonds	¥ 175	\$ 1,636
Subtotal	175	1,636
Other securities:		
Unlisted equity securities	32,229	301,206
Other	1,002	9,364
Subtotal	33,232	310,579
Total	¥33,407	\$312,215

- (b) (i) Marketable securities classified as held-to-maturity debt securities and other securities at March 31, 2004 are summarized as follows:

Marketable held-to-maturity debt securities

	Millions of yen		
	March 31, 2004		
	Carrying value	Estimated fair value	Unrealized gain (loss)
Securities whose fair value exceeds their carrying value:			
Government bonds	¥ 10	¥ 10	¥ 0
Corporate bonds	100	100	0
Other	0	0	0
Subtotal	110	110	0
Securities whose carrying value exceeds their fair value:			
Government bonds	270	269	(0)
Other	42	42	—
Subtotal	312	311	(0)
Total	¥423	¥422	¥(0)

Marketable other securities

	Millions of yen		
	March 31, 2004		
	Cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their cost:			
Equity securities	¥24,312	¥51,602	¥27,290
Other	1,858	3,223	1,365
Subtotal	26,170	54,825	28,655
Securities whose cost exceeds their carrying value:			
Equity securities	10,219	8,729	(1,490)
Subtotal	10,219	8,729	(1,490)
Total	¥36,389	¥63,555	¥27,165

- (ii) Sales of securities classified as other securities amounted to ¥3,057 million with an aggregate gain of ¥729 million and loss of ¥28 million for the fiscal year ended March 31, 2004.

- (iii) The redemption schedule at March 31, 2004 for securities with maturity dates classified as other securities and held-to-maturity debt securities is summarized as follows:

	Millions of yen		
	March 31, 2004		
	Due in one year or less	Due after one year through five years	Due after five years
Government bonds	¥ —	¥280	¥—
Corporate bonds	—	100	—
Other debt	42	—	—
Total	¥42	¥380	¥—

- (iv) Non-marketable securities classified as held-to-maturity debt securities and other securities at March 31, 2004 are summarized as follows:

	Millions of yen
	March 31, 2004
	Carrying value
Other securities:	
Unlisted equity securities	¥29,754
Other	1,002
Total	¥30,757

14. Segment Information

(a) Business segments

The Company and its consolidated subsidiaries are primarily engaged in the manufacture and sales of products in three major industry segments: pulp and paper division, paper related division and housing and construction materials division. The results of their other businesses are reported in the "Other division."

The business segment information of the Company and its consolidated subsidiaries for the fiscal years ended March 31, 2005 and 2004 is summarized as follows:

Millions of yen							
Fiscal year ended March 31, 2005							
	Pulp and paper division	Paper related division	Housing and construction materials division	Other division	Total	Eliminations or corporate	Consolidated
(i) Sales and operating income							
Sales to third parties	¥ 870,360	¥126,592	¥ 95,236	¥ 87,506	¥1,179,696	¥ —	¥1,179,696
Intragroup sales and transfers	12,801	8,954	38,726	38,373	98,855	(98,855)	—
Total sales	883,161	135,547	133,963	125,880	1,278,552	(98,855)	1,179,696
Operating expenses	835,891	127,261	131,624	118,543	1,213,320	(98,855)	1,114,464
Operating income	¥ 47,269	¥ 8,286	¥ 2,339	¥ 7,336	¥ 65,231	¥ —	¥ 65,231
(ii) Assets, depreciation and capital expenditures							
Total assets	¥1,118,556	¥111,871	¥ 79,862	¥103,213	¥1,413,502	¥116,472	¥1,529,975
Depreciation	62,803	5,146	1,275	5,746	74,971	—	74,971
Capital expenditures	40,470	8,264	1,472	5,147	55,353	—	55,353

Thousands of U.S. dollars							
Fiscal year ended March 31, 2005							
	Pulp and paper division	Paper related division	Housing and construction materials division	Other division	Total	Eliminations or corporate	Consolidated
(i) Sales and operating income							
Sales to third parties	\$ 8,134,206	\$1,183,103	\$ 890,056	\$ 817,813	\$11,025,196	\$ —	\$11,025,196
Intragroup sales and transfers	119,636	83,682	361,925	358,626	923,879	(923,879)	—
Total sales	8,253,841	1,266,794	1,251,991	1,176,449	11,949,084	(923,879)	11,025,196
Operating expenses	7,812,065	1,189,355	1,230,131	1,107,879	11,339,439	(923,879)	10,415,551
Operating income	\$ 441,766	\$ 77,439	\$ 21,860	\$ 68,561	\$ 609,636	\$ —	\$ 609,636
(ii) Assets, depreciation and capital expenditures							
Total assets	\$10,453,794	\$1,045,523	\$ 746,374	\$ 964,607	\$13,210,299	\$1,088,523	\$14,298,832
Depreciation	586,944	48,093	11,916	53,701	700,664	—	700,664
Capital expenditures	378,224	77,234	13,757	48,103	517,318	—	517,318

Millions of yen							
Fiscal year ended March 31, 2004							
	Pulp and paper division	Paper related division	Housing and construction materials division	Other division	Total	Eliminations or corporate	Consolidated
(i) Sales and operating income							
Sales to third parties	¥ 890,124	¥123,737	¥ 93,469	¥ 85,317	¥1,192,649	¥ —	¥1,192,649
Intragroup sales and transfers	12,189	10,913	38,043	37,477	98,624	(98,624)	—
Total sales	902,313	134,651	131,513	122,795	1,291,273	(98,624)	1,192,649
Operating expenses	860,950	129,663	128,881	116,098	1,235,594	(98,624)	1,136,970
Operating income	¥ 41,363	¥ 4,987	¥ 2,632	¥ 6,696	¥ 55,679	¥ —	¥ 55,679
(ii) Assets, depreciation and capital expenditures							
Total assets	¥1,247,483	¥116,874	¥ 81,777	¥ 99,694	¥1,545,829	¥ 91,536	¥1,637,366
Depreciation	68,300	5,332	1,379	6,247	81,259	—	81,259
Capital expenditures	44,767	6,091	1,277	5,286	57,423	—	57,423

(b) Geographic segments

Since the sales recognized by companies located in Japan constituted 90% or more of consolidated sales for the fiscal years ended March 31, 2005 and 2004, geographical segment information has not been presented.

(c) Overseas sales

Since overseas sales represented less than 10% of consolidated sales for the years ended March 31, 2005 and 2004, no disclosure of overseas segment information has been presented.

15. Derivatives

Certain subsidiaries have entered into interest-rate swap and interest-rate cap agreements to reduce their interest expense or their exposure to adverse fluctuation in interest rates relating to loans and bonds payable.

The amounts presented below exclude the forward foreign exchange contracts entered into to hedge receivables and payables denominated in foreign currencies which have been translated and are reflected at their corresponding contracted rates in the accompanying consolidated balance sheets.

Summarized below are the contract amounts and estimated fair value of the consolidated subsidiaries' derivatives positions at March 31, 2005 and 2004:

	Millions of yen				Thousands of U.S. dollars			
	March 31, 2004		March 31, 2005		March 31, 2005			
	Contract amount	Estimated fair value	Contract amount	Estimated fair value	Contract amount	Estimated fair value	Contract amount	Estimated fair value
Interest-rate swaps:								
Receive/variable; pay/fixed	¥ 50	¥ (0)	¥ —	¥ —	\$ —	\$ —		
Receive/fixed; pay/variable	5,000	138	3,500	72	32,710	673		
Interest-rate caps:								
To buy	¥8,000	¥ 0	¥ —	¥ —	\$ —	\$ —		

The following methodologies and assumptions were used by certain consolidated subsidiaries in estimating the fair value of their derivatives positions:

Interest-rate swaps and interest-rate caps:

Estimated fair value as provided by the respective financial institutions

16. Research and Development Costs

Included in cost of sales and selling, general and administrative expenses were ¥7,563 million (\$70,682 thousand) and ¥7,121 million of research and development costs for the fiscal years ended March 31, 2005 and 2004, respectively.

17. Subsequent Events

(a) The following appropriations of retained earnings of the Company, which have not been reflected in the accompanying consolidated financial statements for the fiscal year ended March 31, 2005, were approved at an ordinary general meeting of shareholders held on June 29, 2005:

	Millions of yen	Thousands of U.S. dollars
Year-end cash dividends (¥4,000.00 = U.S.\$37.383 per share)	¥4,379	\$40,925
Bonuses to directors	49	458
	¥4,428	\$41,383

(b) Issuance of bonds

- (1) Based on a resolution approved at the Board of Directors meeting held on March 28, 2005, the Company launched its 6th issue of unsecured corporate bonds of ¥20 billion guaranteed by Nippon Paper Industry Co., Ltd. on April 25, 2005:
 - (2) Interest rate: 1.10% per year
 - (3) Issued price: ¥100 par value
 - (4) Date of issue: April 25, 2005
 - (5) Maturity date: April 25, 2012 (these are 7-year bonds)

Report of Independent Auditors



■ Certified Public Accountants

Hibiya Kokusai Bldg.
2-2-3, Uchisaiwai-cho
Chiyoda-ku, Tokyo 100-0011, Japan
C.P.O. Box 1196, Tokyo 100-8641, Japan

■ Phone: +81-(0)3 3503-1100

Fax: +81-(0)3 3503-1197

The Board of Directors
Nippon Paper Group, Inc.

We have audited the accompanying consolidated balance sheets of Nippon Paper Group, Inc. and consolidated subsidiaries as of March 31, 2005 and 2004, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Nippon Paper Group, Inc. and consolidated subsidiaries at March 31, 2005 and 2004, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

Supplemental Information

As described in Note 17, the Company issued its 6th issue of unsecured bonds on April 25, 2005 based on a resolution of the Board of Directors at a meeting held on March 28, 2005.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2005 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3.

Ernst & Young ShinNihon

June 29, 2005

Domestic Networks

Nippon Paper Industries Co., Ltd.

- | | | |
|-----------------------------|----------------------------|---------------------------------|
| ① Kushiro Mill (Hokkaido) | ⑤ Ishinomaki Mill (Miyagi) | ⑨ Fushiki Mill (Toyama) |
| ② Asahikawa Mill (Hokkaido) | ⑥ Iwanuma Mill (Miyagi) | ⑩ Iwakuni Mill (Yamaguchi) |
| ③ Yufutsu Mill (Hokkaido) | ⑦ Nakoso Mill (Fukushima) | ⑪ Komatsushima Mill (Tokushima) |
| ④ Shiraoi Mill (Hokkaido) | ⑧ Fuji Mill (Shizuoka) | ⑫ Yatsushiro Mill (Kumamoto) |

Nippon Daishowa Paperboard Co., Ltd.

- ⑬ Nippon Daishowa Paperboard Tohoku Co., Ltd. (Akita)
 ⑭ Nippon Daishowa Paperboard Kanto Co., Ltd. Soka Mill (Saitama)
 ⑮ Nippon Daishowa Paperboard Kanto Co., Ltd. Ashikaga Mill (Tochigi)
 ⑯ Nippon Daishowa Paperboard Yoshinaga Co., Ltd. (Shizuoka)
 ⑰ Nippon Daishowa Paperboard Nishinippon Co., Ltd. Geibo Mill (Hiroshima)
 ⑱ Nippon Daishowa Paperboard Nishinippon Co., Ltd. Kochi Mill (Kochi)

CRECIA Corporation

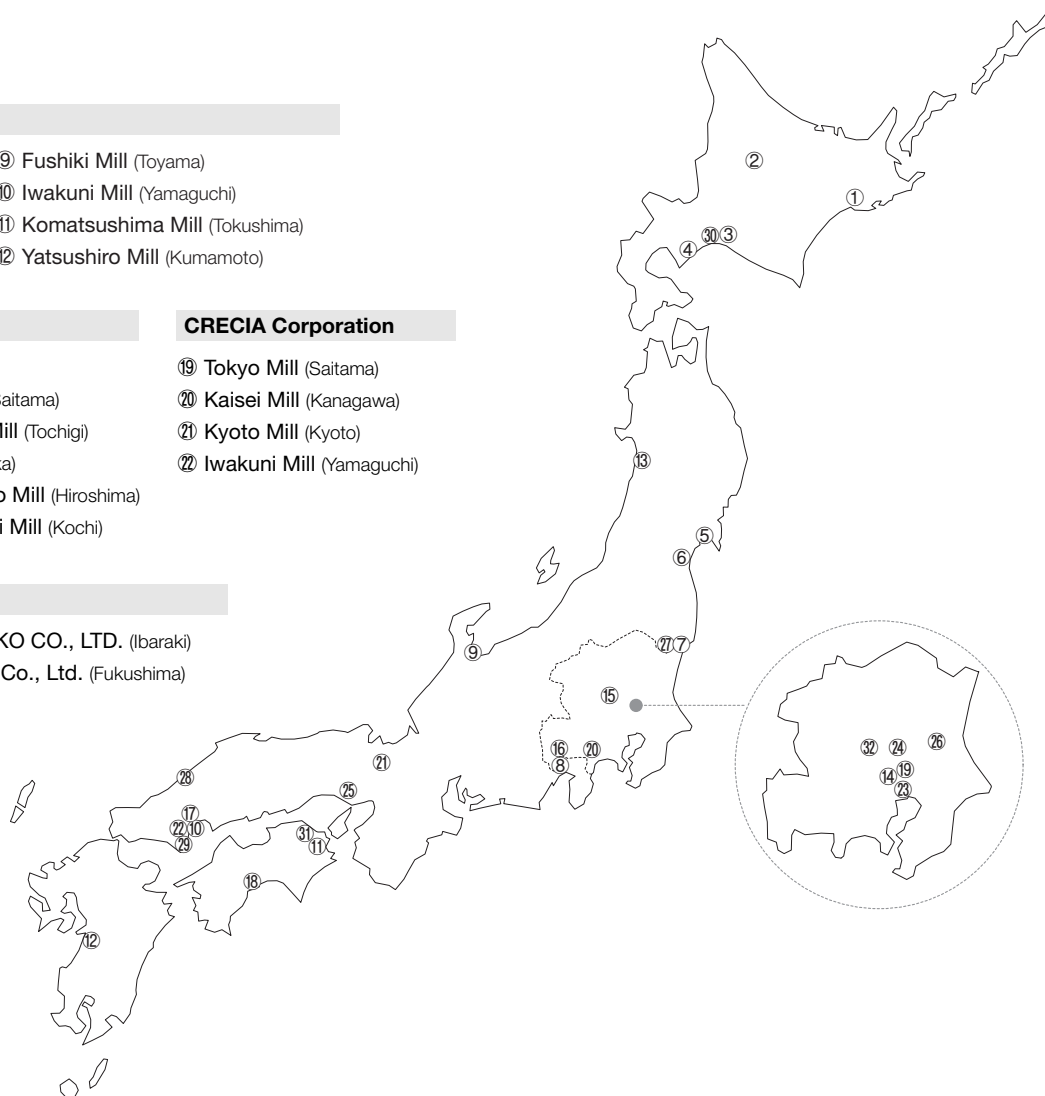
- ⑲ Tokyo Mill (Saitama)
 ⑳ Kaisei Mill (Kanagawa)
 ㉑ Kyoto Mill (Kyoto)
 ㉒ Iwakuni Mill (Yamaguchi)

NIPPON PAPER-PAK CO., LTD.

- | | |
|---------------------------------------|-------------------------------------|
| ㉓ SOKA PAPER-PAK CO., LTD. (Saitama) | ㉖ ISHIOKA KAKO CO., LTD. (Ibaraki) |
| ㉔ EGAWA PAPER-PAK CO., LTD. (Ibaraki) | ㉗ Nakoso Film Co., Ltd. (Fukushima) |
| ㉕ MIKI PAPER-PAK CO., LTD. (Hyogo) | |

Nippon Paper Chemicals Co., Ltd.

- ㉘ Gotsu Works (Shimane)
 ㉙ Iwakuni Works (Yamaguchi)
 ㉚ Yufutsu Works (Hokkaido)
 ㉛ Komatsushima Works (Tokushima)
 ㉜ Higashimatsuyama Works (Saitama)



Pulp and Paper Division

Nippon Paper Industries Co., Ltd.
 Shin-Yuraku-cho building
 1-12-1 Yuraku-cho, Chiyoda-ku, Tokyo 100-0006, Japan
 Tel: +81-(0)3-3218-8000 Fax: +81-(0)3-3216-4753

Nippon Daishowa Paperboard Co., Ltd.
 Nihonbashi Asahi Seimeikan
 2-1-3 Nihonbashi, Chuo-ku, Tokyo 103-0027, Japan
 Tel: +81-(0)3-3242-7311 Fax: +81-(0)3-3242-7312

CRECIA Corporation
 Shinjuku Square Tower
 6-22-1 Nishishinjuku, Shinjuku-ku,
 Tokyo 163-1105, Japan
 Tel: +81-(0)3-5323-0260 Fax: +81-(0)3-5323-0263

Paper-Related Division

NIPPON PAPER-PAK CO., LTD.
 Iidabashi Rainbow Building
 11 Ichigaya-Funagawara-cho, Shinjuku-ku,
 Tokyo 162-0826, Japan
 Tel: +81-(0)3-3269-8631 Fax: +81-(0)3-3267-6587

Nippon Paper Chemicals Co., Ltd.
 JS Ichigaya Building
 5-1 Goban-cho, Chiyoda-ku, Tokyo 102-0076, Japan
 Tel: +81-(0)3-5216-9111 Fax: +81-(0)3-5216-8516

Housing and Construction Materials Division

Nippon Paper Lumber Co., Ltd.
 Keitoku Building
 1-9-5 Oji, Kita-ku, Tokyo 114-8552, Japan
 Tel: +81-(0)3-5390-2011 Fax: +81-(0)3-5390-2020

Overseas Networks

Overseas Offices

■ Pulp and Paper Division

Nippon Paper Industries Co., Ltd.

China Office

Room 1607A, C Seats, Orient International Plaza,
No.85 Lou Shan Guan Road, Shanghai, 200336
China
Tel: +86-21-6278-7581 Fax: +86-21-6278-7582

Longview Office

P.O. Box 699, 3001 Industrial Way, Longview,
WA 98632, U.S.A.
Tel: +1-360-636-7110 Fax: +1-360-423-1514

Concepción Office

Cochrane 361, Concepción, Chile
Tel: +56-41-244-300 Fax: +56-41-259-541

Pietermaritzburg Office

c/o The Central Timber Co-operative Ltd.,
171 Burger Street, Pietermaritzburg 3201,
Republic of South Africa
Tel: +27-33-3924-215 Fax: +27-33-3426-410

Europe Office

World Trade Center, Strawinskylaan 705, 1077 XX
Amsterdam Z.O., Netherlands
Tel: +31-20-5711-878 Fax: +31-20-5711-879

■ Housing and Construction Materials Division

Nippon Paper Lumber Co., Ltd.

Vancouver Office

Suite 1140-1040, West Georgia Street,
Vancouver, B.C. V6E 4H1, Canada
Tel: +1-604-873-5358 Fax: +1-604-689-2853

Major Overseas Subsidiaries and Affiliates

■ Asia and Oceania

China

Shouguang Liben Paper Making Co., Ltd.

595 Shengcheng Road, Shouguang, Shandong,
262700, China
Tel: +86-536-215-8412 Fax: +86-536-215-8417

Shanghai JP Co., Ltd.

173 Hongcao Road(S), Shanghai, 200233, China
Tel: +86-21-6408-9900 Fax: +86-21-6408-6677

Zhejiang Jingxing Nippon Paper Co., Ltd.

Pinghu Zhejiang, 314214, China
Tel: +86-573-597-8658 Fax: +86-573-597-8000

Everweath Paper Industries (Shanghai) Co., Ltd.

2 Xinjie Road, Xin Qiao Township Industrial Park,
Song Jiang, Shanghai, 201612, China
Tel: +86-21-5764-5189 Fax: +86-21-5764-5118

Nippon Paper Industries Trading (Shanghai) Co., Ltd.

- **Shanghai office**
Room 1607B, C Seats, Orient International Plaza,
No.85 Lou Shan Guan Road, Shanghai, 200336,
China
Tel: +86-21-6209-3972 Fax: +86-21-6208-9476

- **Beijing office**

Room 1003, Avic, No. 10B Central Road, East 3rd
Ring Road, Chaoyang District, Beijing, 100022,
China
Tel: +86-10-6566-7148 Fax: +86-10-6566-7145

Australia

South East Fibre Exports Pty. Ltd.

P.O. Box 189, Jews Head, Edrom Road, Eden,
N.S.W. 2551, Australia
Tel: +61-2-6496-0222 Fax: +61-2-6496-1204

Nippon Paper Treefarm Australia Pty. Ltd.

Level 6,456 Lonsdale Street, Melbourne,
VIC 3000, Australia
Tel: +61-3-9252-2700 Fax: +61-3-9642-2705

WA Plantation Resources Pty. Ltd.

Level 5, BGC Centre, 28 The Esplanade Perth, WA
6000, Australia
Tel: +61-8-9420-8300 Fax: +61-8-9322-7895

Malaysia

N.A.K. Manufacturing (M) Sdn. Bhd.

Lot 19-11, Bersatu Industrial Complex, Kawasan
Perindustrian Balakong, 43200 Cheras, Selangor
Darul Ehsan, Malaysia
Tel: +60-3-9074-7896 Fax: +60-3-9074-7889

■ North and South America

U.S.A.

North Pacific Paper Corporation

P.O. Box 2069, 3001 Industrial Way, Longview,
WA 98632, U.S.A.
Tel: +1-360-636-6400 Fax: +1-360-423-1514

Nippon Paper Industries USA Co., Ltd.

P.O. Box 271, 1815 Marine Drive, Port Angeles,
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Canada

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Daishowa-Marubeni International Ltd.

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B.C. V6C 3A8, Canada
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Chile

Volterra S.A.

Cochrane 361, Concepción, Chile
Tel: +56-41-244-300 Fax: +56-41-259-541

■ Europe

Finland

Juho Thermal Oy

P.O. Box 92, FIN-27501 Kauttua, Finland
Tel: +358-2-8393-2900 Fax: +358-2-8393-2419

■ Africa

South Africa

Nippon-SC Tree Farm S.A. (Pty) Ltd.

JHI House, 11 Cradock Avenue, Rosebank,
Johannesburg 2196, South Africa
Tel: +27-11-880-4310 Fax: +27-11-788-1435

Investor Information

Name

Nippon Paper Group, Inc.

Code No.

3893

Securities Traded

Tokyo Stock Exchange, Osaka Securities Exchange and Nagoya Stock Exchange

Total Number of Outstanding Stocks Issued

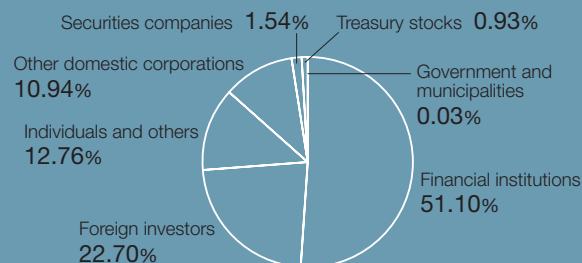
1,105,235.63

Major Shareholders (10 Largest)

Name	Number of Shares Held (Shares)	Voting Stake (%)
Japan Trustee Services Bank, Ltd. (Trust Account)	113,003	10.4
The Master Trust Bank of Japan, Ltd. (Trust Account)	72,936	6.7
Nippon Life Insurance Company	33,733	3.1
Mizuho Corporate Bank, Ltd.	31,314	2.9
Mitsui Life Insurance Company Limited	22,589	2.1
Mizuho Bank, Ltd.	21,467	2.0
The Chase Manhattan Bank, N.A. London	20,571	1.9
Daio Paper Corporation	20,409	1.9
Sumitomo Mitsui Banking Corporation	19,938	1.8
State Street Bank and Trust Company 505103	18,214	1.7
Total Voting Stake of 10 Largest Major Shareholders		34.5

(Note) Shares held less than one share have been omitted.

Percentage of Shares Held by Shareholder Type



Fiscal Year-End

March 31

Ordinary General Meeting of Shareholders

Within three months from the day following the fiscal year-end

Administrative Office of Transfer Agent

Stock Transfer Agency Department
The Chuo Mitsui Trust and Banking Company, Limited
2-8-4 Izumi, Suginami-ku, Tokyo 168-0063
Tel: +81-(0)3-3323-7111

Independent Auditor

Ernst & Young ShinNihon

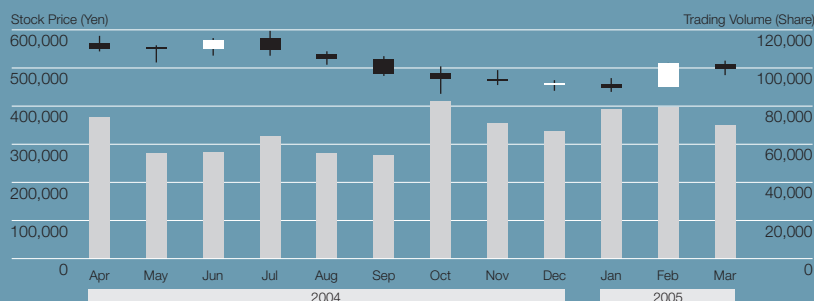
IR Contact

Nippon Paper Group, Inc. Investor Relations
Shin-Yuraku-cho building
1-12-1 Yuraku-cho, Chiyoda-ku, Tokyo 100-0006, Japan
Tel: +81-(0)3-3218-9345 Fax: +81-(0)3-3216-5662
URL <http://www.np-g.com/ir/>
fujimori@np-g.com

Sustainability Report Information

Sustainability Report 2005 (English version) to be issued in January 2006
(Inquiries)
Nippon Paper Group, Inc. CSR office
Tel: +81-(0)3-3218-9321 Fax: +81-(0)3-3216-1366
URL <http://www.np-g.com/csr/>

Stock Price and Trading Volume



Disclaimer Regarding Forward-Looking Statements

Statements contained in this annual report regarding current plans, outlooks, strategies and beliefs of Nippon Paper Group, Inc. and the group companies, other than those of historical fact, are forward-looking statements or forecasts based on the management assumptions of the Nippon Paper Group, Inc. and the group companies 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 Companies' actual future performance and results may be affected by changes in a number of factors and thus may differ materially from those described therein.

The Paper Used for This Report

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GROUP

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