Annual Report 2007

Fiscal Year Ended March 31, 2007

Corporate Data (As of March 31, 2007)

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Tokyo Office	JR Shinagawa East Bldg., 2-18-1, Konan, Minato-ku, Tokyo 108-0075, Japan Phone: 81-3-6716-0111 Facsimile: 81-3-6716-0200
Fiscal Year-End Date	March 31 on an annual basis
Date of Founding	October 25, 1924
Date of Establishment	February 11, 1934
Paid-in Capital	¥28,023 million
Number of Shares of Common Stock Issued	263,813 thousand
Number of Shareholders	15,080
Major Shareholders	Japan Trustee Services Bank, Ltd. The Master Trust Bank of Japan, Ltd. State Street Bank and Trust Company Matsushita Electric Industrial Co., Ltd. Sumitomo Mitsui Banking Corporation Trust & Custody Services Bank, Ltd. Northern Trust Company The Bank of New York Mitsui Sumitomo Insurance Co., Ltd. Nippon Life Insurance Company
Number of Subsidiaries and Affiliated Companies	Subsidiaries: 190 Affiliates: 17
Number of Employees	33,480 (Consolidated)
Stock Exchange Listings	Tokyo, Osaka, Nagoya, Fukuoka, Sapporo
Advertising Method	The Company uses the electronic advertising method, posting advertisements on its website (http://www.daikin.co.jp/e/koukoku/). However, when electronic advertising is not possible due to technical problems or other circumstances, the Company will post advertisements in the *Nikkei Shimbun.*
Shareholder Register Administrator	Daiko Shoken Business Co., Ltd. 2-4-6, Kitahama, Chuo-ku, Osaka 541-8583, Japan
Ordinary General Meeting of Shareholders	June
Auditor	Deloitte Touche Tohmatsu

Contents

Profile	1
At a Glance	2
To Our Shareholders	4
Interview with the President	8
Review of Operations	14
Financial Section	23
Five-Year Summary	23
Financial Review	24
Consolidated Balance Sheets	28
Consolidated Statements of Income	30
Consolidated Statements of Changes in Equity	31
Consolidated Statements of Cash Flows	32
Notes to Consolidated Financial Statements	33
Independent Auditors' Report	49

Forward-Looking Statements

This annual review contains statements regarding the future plans and strategies of Daikin Industries, Ltd. (the Company), as well as the Company's future performance. These statements are not statements of past facts but are based on judgments made by the Company on the basis of information known at the time. Therefore, readers should refrain from drawing conclusions based only on these statements regarding the future performance of the Company. The actual future performance of the Company may be influenced by economic trends, strong competition in the industrial sectors where it conducts its operations, foreign currency exchange rates, and changes in taxation and other systems. For these reasons, these forward-looking statements are subject to latent risk and uncertainty.

Profile

Founded in 1924, Daikin Industries, Ltd., has grown to become a leading producer of air-conditioning systems and fluoro-chemical products. Today, as the world has become a single global market and we face megacompetition, we are stepping up our efforts to expand our operations globally and continue to meet new challenges.

In addition, in our oil hydraulics and electronics divisions, we are combining our advanced technology and R&D capabilities in fields outside our core businesses to create innovative products and systems that contribute to industry and to the lives of our customers.

In fiscal 2007, ended March 31, 2007, Daikin prepared and began to implement a new strategic management plan, FUSION 10, with the goal of building on all its accomplishments to date to achieve major breakthroughs in performance. Under FUSION 10, we are aiming to maximize our corporate value as a "global and excellent company" by implementing our priority strategies and working to strengthen our corporate position and performance through innovation.

In fiscal 2007, Daikin's consolidated net sales rose to a record-high ¥912.1 billion, and the Company's operating income reached the record-high level of ¥80.9 billion. In view of this, *Newsweek* magazine ranked Daikin 365th among the world's top 500 companies and 90th among Japan-based companies. Daikin's products are also steadily earning greater recognition throughout the world, as reflected in the recent decision to give the HVAC&R Technology Innovation Award* to the Company's mainstay high-value-added URURU & SALALA air-conditioning system products.

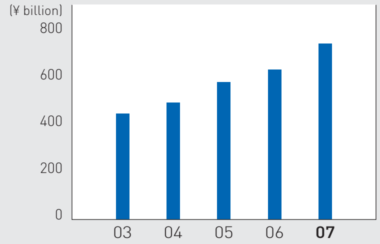
* HVAC&R represents "heating, ventilation, air conditioning & refrigeration." Sponsored by a prestigious Italian magazine specializing in air conditioning and building facilities, *Costruire Impianti*, the HVAC&R Technology Innovation Award is given to products that have been on the market for less than three years.

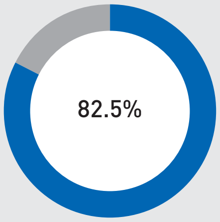
At a Glance

Net Sales

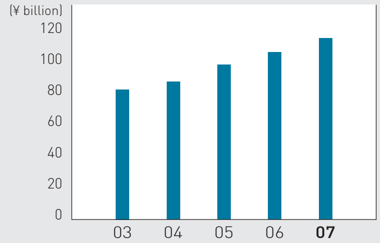
Percentage of Net Sales

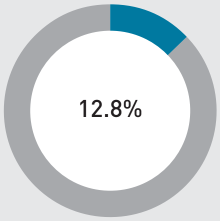
Air Conditioning



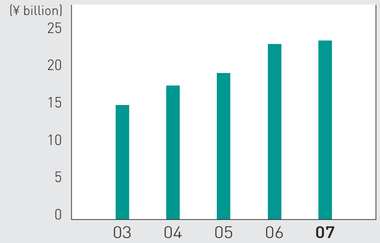


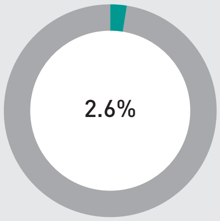
Chemicals



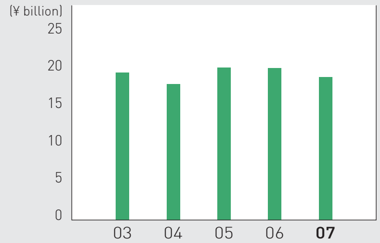


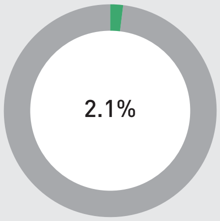
Oil Hydraulics





Defense





Electronics

Major Products & Services	Description
• Room air-conditioning systems • Air cleaners • Dehumidifiers • Packaged air-conditioning systems • Medium- and low-temperature air-conditioning systems • Marine-type container refrigeration • Water-chilling units • Absorption refrigerators • Air-handling units	Since becoming the first in Japan to manufacture packaged air-conditioning systems, in 1951, Daikin has supported comfortable living based on the strengths of technologies that it has itself nurtured as the world's sole manufacturer to create a full line of products from refrigerants to air conditioners.
• Fluorocarbons • Fluoroplastics • Fluoroelastomers • Fluorinated oils • Oil- and water-repellent products • Mold release agents • Pharmaceuticals and intermediates • Semiconductor-etching products • Dry air suppliers	In 1933, Daikin was the first in Japan to engage in research on fluorinated refrigerants. Today, our activities range from research and development to commercialization, and we offer a lineup of more than 1,800 fluorine compounds.
• Pumps and motors • Control valves • Stack valves • Positioning motors • Oil-cooling units • Power packages • Hydrostatic transmissions • Centralized lubrication units and systems	Daikin's unique hydraulic technologies are contributing to the development of industry by unleashing the potential of power control.
• Warheads • Aircraft parts • Home-use oxygen therapy equipment	Daikin's superior machining and quality control technologies are used in the production of aircraft parts, defense-related products, and other industries where high levels of precision and performance are critical.
• Network management systems • Computer graphics systems • DVD-authoring systems • CAD/CAM/CAE systems	From our unique graphics technologies to the conception of total network environments, Daikin provides a host of next-generation solutions.

To Our Shareholders

Maximizing Corporate Value

Based on its management philosophy, the Daikin Group is working to overcome various challenges related to the upgrading of its technological base in a manner that enables the Group to provide products, materials, and services of superlative quality and thereby continually provide customers with maximum convenience and amenity. At the same time, the Group is thoroughly applying capitalistic principles in its efforts to maximize its corporate value. The Daikin Group's action policies are designed to ensure the Group undertakes fair competition and conforms to the highest standards of business ethics, discloses and explains appropriate information on its operations in a timely manner, proactively works to protect the global environment, and dynamically contributes to local communities. We are doing our utmost to ensure these policies are applied conscientiously throughout our operations. We are also doing our best to promote information sharing within the Group and maintain the organizational flexibility required to respond to special challenges as means of further increasing the sophistication of Daikin's excellent tradition of "flat & speedy management," augmenting overall Group profitability, and expanding Group business operations.

Noriyuki Inoue
Chairman of the Board and CEO

Our Group Philosophy

1. Create New Value by Anticipating the Future Needs of Customers
2. Contribute to Society with World-Leading Technologies
3. Realize Future Dreams by Maximizing Corporate Value
4. Think and Act Globally
5. Be a Flexible and Dynamic Group
1) Flexible Group Harmony
2) Build Friendly Yet Competitive Relations with Our Business Partners to Achieve Mutual Benefit
6. Be a Company That Leads in Applying Environmentally Friendly Practices
7. With Our Relationship with Society in Mind, Take Action and Earn Society's Trust
1) Be Open, Fair, and Known to Society
2) Make Contributions That Are Unique to Daikin to Local Communities
8. The Pride and Enthusiasm of Each Employee Are the Driving Forces of Our Group
1) The Cumulative Growth of All Group Members Serves as the Foundation for the Group's Development
2) Pride and Loyalty
3) Passion and Perseverance
9. Be Recognized Worldwide by Optimally Managing the Organization and Its Human Resources, under Our Flat & Speedy Management System
1) Participate, Understand, and Act
2) Offer Increased Opportunities to Those Who Take On Challenges
3) Demonstrate Our Strength as a Team Composed of Diverse Professionals
10. An Atmosphere of Freedom, Boldness, and "Best Practice, Our Way"

With an eye to further strengthening its corporate governance systems, the Daikin Group is continually emphasizing measures aimed at "upgrading capabilities for management system innovation that facilitates strategic management perspectives and speedy management decisions," "promoting flat & speedy management at the Group level as well as other distinctive Daikin policies for managing human resources and organizational systems," "creating virtual companies to encourage comprehensive emphasis on corporate-value-oriented management policies and self-responsibility management practices," and "achieving stable management based on open and transparent responsiveness to stakeholders."

Start of the FUSION 10 Strategic Management Plan

We have drafted a new strategic management plan—FUSION 10—that covers the five years from fiscal 2007 through fiscal 2011 and begun implementing various measures in line with this plan's challenging goals of preparing for a major performance surge.

The plan also calls for the Daikin Group to proactively move toward becoming a truly excellent global company and maximizing its corporate value by:

(1) attaining the global No. 1 position as a comprehensive air-conditioning and refrigeration manufacturer,
(2) acting as a leader of creative changes and using exclusive technologies to undertake innovation and the creation of new value, and
(3) building a profit structure and financial position that are resiliently strong and highly efficient in regard to capital.

The most fundamental aspect of the plan is a "people-oriented management" approach to ensuring that everyone in the Daikin Group has a good understanding of the Group's management philosophy so that all Group employees can concertedly maximize the effectiveness of their contributions to implementing the philosophy and dynamically driving the Group's global business development.

In January 2007, Daikin acquired 100% of the outstanding shares of Malaysia-based O.Y.L. Industries Bhd (OYL). According with our plans to speedily attain the global No. 1 position as a comprehensive air-conditioning and refrigeration manufacturer, this move is expected to generate a large amount of synergies and mutual-reinforcement relationships among previous and new members of the Daikin Group. In addition to considerably increasing the scale of the Daikin Group's operations, the acquisition gives the Group solid platforms for expanding the geographic scope of its operations in the U.S. market and NIEs' markets and for establishing a new business model centering on the provision of solutions proposals covering a comprehensive range of fields, including large-scale commercial (applied) air-conditioning systems as well as maintenance, repair, and engineering services. In these various ways, the acquisition is helping consolidate the Daikin Group's foundation for attaining the global No. 1 position.

During the past year, Daikin has focused on expanding its own operations and on realizing various potential synergies between its operations and those of OYL units. Having created 49 working groups with a total of almost 300 members to intensively focus on realizing these synergies, we have concretely manifested a greater amount of synergies than originally anticipated at the time of the OYL acquisition. This increase in synergistic benefits is projected to reduce the time period required to earn back the cost of our investment to eight years.

In fiscal 2008, we are strategically emphasizing measures to:

- expand the net sales of existing businesses in existing regions, centered on Europe and China,
- utilize synergies with OYL to strengthen business in large-scale commercial (applied) air-conditioning systems and business in North American markets,
- enter the promising markets of such NIEs as Middle Eastern countries, India, and Brazil,
- expand such new businesses as freezing and low-temperature business and room-heating business,

- promote greater development of products that contribute to environmental protection and meet the needs of next-generation markets, and
- greatly reduce costs and thereby offset sharp rises in raw materials procurement prices.

During fiscal 2007—the first year of the FUSION 10 plan—I believe that Daikin got the plan off to a strong start, recording its 13th consecutive year of increased operating income and ordinary income and 7th consecutive year of record-high net sales and operating income.

We are intent on realizing the FUSION 10 goals of expanding business related to Daikin's special technologies and products, realizing synergies with OYL, and attaining the global No. 1 position as a comprehensive air-conditioning and refrigeration manufacturer.

Additional Surge in Financial Ratio Management

To maximize its market capitalization, Daikin is promoting "financial ratio (ROA, ROE, etc.) management" and proactively taking measures to expand its operations and strengthen its operating structures. Specifically, the Company is emphasizing its performance regarding such indicators as free cash flow (FCF), Daikin Value Added (DVA, an in-house-developed metric), return on assets (ROA), and return on equity (ROE). Top emphasis is given to FCF, a primary source of corporate value, and we are striving to create additional cash flow through such moves as those to lower levels of receivables and inventories.

To maximize the effectiveness with which we employ our FCF, we are proactively investing it in projects aimed at sharply heightening the sophistication of our technological base, which is a primary source of our competitiveness, as well as farsighted projects to augment our business infrastructure and obtain additional resources from external sources. All these investments are designed to support a rapid surge in our global business development.

In fiscal 2007, our acquisition of 100% of OYL shares and other projects depressed FCF to negative levels, but DVA shot up ¥6.5 billion from the previous fiscal year, and ROA and ROE were 5.9% and 12.3%, respectively.

To fund the repayment of debt shouldered to acquire OYL, Daikin increased its capital through a public stock offering in May 2007.

Besides expanding its air-conditioning operations, Daikin is striving to contribute to a performance surge through measures aimed at quickly restoring high profit levels in fluorochemicals business, accelerating the restructuring of oil hydraulics and special equipment business, and boosting the efficiency of administrative and support departments. We are also moving forward relentlessly with efforts to increase the sophistication of our technologies and bolster our human resources and training programs as well as to further step up our corporate social responsibility systems aimed at ensuring the Group maintains a record of consistently rigorous legal compliance, superlative standards of business ethics, highly safe operations, and outstanding contributions to environmental protection. In these ways, we are doing our utmost to live up to the expectations of all our stakeholders.

I hope shareholders will heartily approve of our ambitious plans and dynamic efforts to maximize shareholder benefits.

June 29, 2007

Noriyuki Inoue

Noriyuki Inoue
Chairman of the Board and CEO

At a Glance
To Our Shareholders
Interview with the President
Review of Operations
Financial Section

Yukiyoshi Okano
President and COO, Member of the Board

During fiscal 2007, the Daikin Group recorded record-high levels of consolidated net sales and operating income for the seventh consecutive fiscal year. It also completed the acquisition of O.Y.L. Industries Bhd (OYL). Currently, the Group is striving to maximize the leveraging of synergies with OYL as it begins the full-scale development of business in the North American air-conditioning market in line with its FUSION 10 strategic management plan. The Group is relentlessly moving forward along the path toward maximizing its corporate value as a truly excellent and global company.

Q1: Could you describe conditions in your operating environment during fiscal 2007 and your response to those conditions?

A: During the year, the global economy was affected by the stubbornly high level of oil prices, and a worldwide slump in stock prices during May and June temporarily increased the downward pressure on economic conditions. On the other hand, demand increased in IT-related markets, and the economic dynamism of China and other Asian countries had a supportive effect on the generally positive economic trends seen worldwide.

In Japan, adverse weather conditions and other factors depressed personal consumption, but strong corporate performance spurred expanded capital investment, and the healthy world economy stimulated exports. As a result, the trend toward recovery continued.

Amid these conditions, the Daikin Group operated in line with its strategic emphasis on ensuring capabilities for addressing new challenges and thereby preparing for a future surge in performance. Our approach has been to avoid excessive focus on the past and promote responsiveness to the major changes currently under way in society as well as the structural changes seen in many markets. These changes are presenting us with important business development opportunities, and we are doing our best to implement bold new business strategies that take full advantage of those opportunities and create a solid foundation for a performance surge. One of the major strategic initiatives we took during the year was our acquisition of OYL.

Fiscal 2007 was also a very important year insofar as it was the first year of the FUSION 10 strategic management plan, which covers the period through March 31, 2011.

Q2: How was Daikin's performance during fiscal 2007?

A: Daikin worked hard to expand its mainstay air-conditioning business by promoting greater sales of highly distinctive, high-value-added products in Japan and responding to opportune market conditions overseas, particularly in Europe and China. We also were quite successful in expanding our fluoroplastic business in the Japanese and Chinese markets. These were the main factors that boosted Daikin's consolidated net sales to ¥912.1 billion, up 15.0% from the level in the previous fiscal year.

Our emphasis on promoting domestic and overseas sales of highly distinctive products and on implementing comprehensive cost-cutting programs enabled us to considerably improve our profitability. On a consolidated basis, Daikin's operating income amounted to ¥80.9 billion, up 20.7% from the previous fiscal year, and ordinary income totaled ¥78.5 billion, up 14.3%. Net income rose 12.1%, to ¥45.6 billion.

Fiscal 2007 was the 13th consecutive year in which the Daikin Group recorded increased operating income and ordinary income. It was the seventh consecutive year in which the Group attained record-high levels of both net sales and operating income. Moreover, it was a highly significant year in terms of the globalization of our operations, as the share of net sales generated overseas surpassed sales in Japan for the first time, rising to 52%.

Our ability to boost profitability during fiscal 2007 faster than originally projected also represented a strong start toward the attainment of our FUSION 10 targets.

Moreover, our activities have been highly appraised by outside observers. Our stock price has reached record-high levels, and we have consistently earned high rankings by credit-rating companies and various media entities.

From whatever perspective you choose, it is evident that Daikin Group employees are working industriously and demonstrating outstanding effectiveness in bringing about various kinds of positive changes in Group operations. The aggregate power of each employee's dynamic contributions makes me highly confident about Daikin's future.

Q3: Why did you revise FUSION 10 and what are the plan's new targets?

A: Since our decision to acquire OYL, we have placed strategic emphasis on drafting and implementing plans that maximize the synergies that we can generate in the process of integrating OYL with Daikin. As a result, we now have plotted a course designed to make the most of the two companies' complementary capabilities and thereby enable the two companies to grow and develop considerably more vigorously than they would be capable of independently. This new strategic emphasis has led to the revision of both numerical targets and strategic plans within FUSION 10.

Currently, FUSION 10 includes five main themes: (1) considerably expanding global sales, beginning with the full-scale development of operations in North America,

(2) building global business in large-scale commercial (applied) air-conditioning systems markets, (3) maximizing synergies related to development, manufacturing, and procurement operations, (4) developing global servicing business, and (5) expanding and strengthening low-temperature/ freezing equipment and filter equipment business.

Based on our plans to implement measures related to these themes, we intend to increase the annual level of our consolidated net sales to the ¥1,700-billion to ¥1,800-billion range by fiscal 2011 while boosting our operating income rate to above the 10% mark.

On the other hand, we have not changed the fundamental concepts or direction of FUSION 10, and we are maintaining our efforts to realize the original FUSION 10 goal of "maximizing corporate worth to become a truly global and excellent company."

Q4: The acquisition of OYL is expected to further accelerate Daikin's global expansion. What is the outlook for Daikin's growth in the crucial North American market?

A: As industrial restructuring proceeds on a global level, Daikin has taken the initiative in acquiring OYL. We expect this move to strengthen the global competitiveness of our air-conditioning operations.

The North American air-conditioning product market is the world's largest, accounting for roughly 30% of global demand. Ducted air-conditioning products, usually single indoor units, are the mainstream air-conditioning products in North America, and the market for Japanese-style ductless air-conditioning systems is not large. However, we believe that the increasing prominence in recent years of energy conservation and environmental protection issues is presenting great opportunities to stimulate rising demand in North America for Daikin ductless air-conditioning products characterized by outstanding energy efficiency and low noise levels. To take full advantage of this opportunity, we can draw on the capabilities of McQuay International in the OYL Group, which offers a highly promising means of gaining a strong foothold. We are seeking to become a major market player by integrating the operations of Daikin and McQuay so that we can offer a product lineup that encompasses both applied and variable refrigerant volume (VRV) ductless products.

Currently, the ductless air-conditioning product market in North America is expanding more quickly than anticipated. We plan to differentiate ourselves from other companies in that market on the basis of our conscientiously meticulous, Japanese-style after-sales services with respect to maintenance and repairs. By offering such service along with high-value-added products, we expect the Daikin Group to steadily expand its presence in North America.

At the same time, by providing McQuay's U.S. manufacturing facilities with Daikin's high-quality manufacturing know-how, we expect to achieve productivity gains along with cost reductions.

Q5: How are Daikin's operations in Europe and Asia?

A: In Europe, we are planning a concentrated influx of McQuay applied air-conditioning marketing staff—beginning with the key European markets of France, Italy, and Spain—who will be handling their operations in a manner that enables the integrated operation of manufacturing and marketing units. As for residential-use air-conditioning products, the addition of reasonably priced, OYL-manufactured items will enable us to offer a product lineup ranging from premium to very affordable products.

Regarding markets in the Asia and Oceania region, particularly China, we are planning to expand our base of business in VRV products to encompass a growing volume of business in the applied market and light commercial market (the light commercial market includes residential-use, commercial-use, and unitary products). Our applied marketing operations will be integrated with those of McQuay so that we can develop and expand a comprehensive range of applied product business.

We are also undertaking proactive business development campaigns in such emerging markets as those of Russia, India, and Middle Eastern countries.

Annual sales in the worldwide comprehensive air-conditioning and refrigeration market—defined as including ductless, applied, cold storage, and refrigeration products—currently amount to roughly ¥8 trillion. Having acquired OYL, we believe we are now strongly positioned to overcome challenges from competing companies as we begin the full-scale expansion of our operations in this market.

Q6: As Daikin proceeds with its global expansion, how is it responding to the various regulatory environments and other special characteristics of different markets?

A: The Japanese market has developed to the point where competition is generally focused on superior functions and other high-value-added product characteristics.

When selecting air-conditioning products, Japanese consumers pay considerable attention to energy conservation performance, and quite sophisticated technologies are required to satisfy the requirements of those consumers with respect to the maintenance of optimal humidity levels and comfortable temperatures.

In contrast, the Asia and Oceania region generally has a hot and humid climate that encourages consumers to give more attention to the durability and affordability of air-conditioning products than to sophisticated performance features. In view of such future trends as those regarding the introduction of CO_2 emission restrictions, however, we expect the appeal of environment-friendly Daikin Group products in the region to rise.

In the United States, although ducted air-conditioning products are standard, it is possible that rising emphasis on environmental protection will lead to changes in regulations and other factors influencing air-conditioning product market trends. We believe there are good grounds for expecting an increase in the U.S. demand for ductless air-conditioning products.

The European market is noteworthy for having regulations that are relatively strict by global standards, such as the Restriction of the Use of Certain Hazardous Substances (RoHS) directive. Moreover, there is a quite diverse variety of regulations.

It is expected that concern regarding the progress of global warming and other factors will impel a general trend toward increasingly strict regulations in all these markets. At the same time, we expect the Daikin Group to still further increase the sophistication of the kind of technologies that will be required to comply with strict environmental protection regulations.

The FUSION 10 strategic management plan calls for Daikin to be a leader regarding environmental protection, and the Company's Environmental Action Plan 2010 provides detailed prescriptions for concrete measures to increase our contribution to environmental protection. The Daikin Group's management philosophy also demands that Daikin show leadership with respect to environmental protection. Moreover, we believe realizing our goal of taking the global No. 1 position in the air-conditioning field requires us to be the No. 1 company in the field of environmental protection. We are confident that we can build an extremely strong position in the global market by providing people throughout the world with outstanding environment-friendly products.

Q7: Heat pump and inverter technologies are important parts of Daikin's core technological strengths. What are your plans for making the most of these technologies in the future?

A: Currently, preventing global warming is an important issue throughout the world. Daikin's Group management philosophy calls for the Company to take the lead in promoting greater emphasis on environment friendliness throughout global society. Our goal of being the global No. 1 company in the air-conditioning field also requires us to further improve our environmental technologies to ensure we are among the world's top companies with respect to the environment friendliness of each aspect of our operations and products.

In this regard, the most important point is products' energy efficiency—specifically, the use of inverter technology to create energy-saving products. I believe it is Daikin's mission to create such products and promote their diffusion throughout the world.

It is particularly important to supply products with increasingly high levels of energy efficiency in North America, which has a high level of per capita energy consumption, as well as in China and other emerging air-conditioning markets, in which per capita energy consumption is projected to sharply increase.

Daikin also can make an important contribution to reducing CO_2 emissions by promoting a shift away from fuel-burning heating and hot water systems that are standard throughout most of the world and toward high-efficiency heat pump and hot water systems.

For example, while gas boilers and similar fuel-burning systems are standard in Europe, Daikin began marketing Altherma heat pump systems in Europe in fiscal 2007, and these systems have become increasingly popular there. Replacing one fuel-burning system with a heat pump system can reduce CO_2 emissions by up to 50%, so a worldwide shift to heat pump systems could generate huge benefits regarding the prevention of global warming.

We are also developing non-fluoron air-conditioning products and various other kinds of innovative new technologies that facilitate increasingly effective environmental protection efforts. Daikin is aiming to be a company that contributes to the prevention of global warming in all its activities.

Q8: What kind of cost reductions do you think are achievable based on synergies with OYL?

A: First, by mutually providing support with respect to product development and technologies, I believe the two companies can develop products more efficiently.

For example, OYL is now able to replace some of the compressors it uses with Daikin compressors, and Daikin can provide OYL with support regarding inverter technologies. On the other hand, Daikin can commercialize new low-cost products more quickly by basing product development programs on existing items within OYL's product lineup.

As for productivity increases, just by enabling the two companies to make use of each other's manufacturing lines, we are seeking to reduce manufacturing-related capital investments by roughly ¥9.0 billion in the three years from fiscal 2007. Moreover, the Daikin Group can leverage OYL's business volume to gain greater price-negotiating power when procuring components and materials. By using our new leverage to purchase general-use components as well as custom-made components that are relatively inexpensive but still offer high quality and by taking various initiatives to realize similar synergies based on economies of scale, we are aiming to reduce annual procurement costs approximately ¥2.0 billion in 2008.

Regarding service-related operations, we will be taking measures to introduce Japanese standards of "quick, accurate, and cordial responsiveness" at all OYL-affiliated bases, and we are also planning to integrate the two companies' service networks to create a worldwide network of approximately 250 bases, or approximately twice the number of bases currently in Daikin's service network. By upgrading our service capabilities, we will position ourselves to sharply expand our business based on maintenance and repair contracts, thereby strengthening our foundation for building applied solutions business.

Q9: Please tell us about the profit-pillar and growth-driver businesses expected to support Daikin's corporate development in the future.

A: Our profit pillar strategy centers on the use of synergies with OYL to dynamically expand our air-conditioning business. We are aiming to attain the global No. 1 position as a comprehensive air-conditioning and refrigeration product manufacturer in fiscal 2011.

One example of our growth-driver businesses might be our business in the low-temperature and refrigeration product field. To date, we have mainly developed such business involving marine-type shipping container refrigeration systems, low-temperature air-conditioning systems, multi-unit freezer systems, and combini packs (integrated freezing-refrigeration-air-conditioning systems). Because of a projected worldwide surge in the distribution of foods and other products requiring controlled temperatures, we are anticipating that the global market for related low-temperature and refrigeration products will increase to ¥2 trillion in the near future.

Within the OYL Group is J&E Hall International, a venerable U.K.-based freezer and refrigeration system manufacturer that was established in 1875 and has a strong reputation for outstanding technologies and engineering capabilities. We want to make good use of J&E Hall's technologies to propel a major surge of business development, particularly in the land-type shipping container freezer systems field, where Daikin is relatively weak. In November 2006, we created a new unit—the Low Temperature Business Division—that is responsible for expanding low-temperature business worldwide. By realizing synergies with J&E Hall and taking various business initiatives, we are aiming to expand our annual net sales in the low-temperature/refrigeration business field to the ¥100.0 billion mark by fiscal 2011.

Q10: Please give us an overview of the outlook for Daikin's operations in fiscal 2008.

A: While there are some risk factors, the global economy is expected to maintain stable growth against the backdrop of sustained strong economic conditions in Asia. In Japan, it is anticipated that the expansionary economic trend will continue on the strength of such factors as expected robust corporate capital investments as well as a boost to personal consumption as Japanese baby boomers retire and receive lump-sum retirement bonuses.

In view of this, the Daikin Group has adopted a "breakthrough advance" policy for 2007 and is assiduously implementing diverse initiatives based on the FUSION 10 strategic management plan as well as additional initiatives designed to maximize the amount of synergies we create between Daikin and OYL Group companies. The Daikin Group is concertedly doing its utmost to realize a dramatic breakthrough of progress in its business development, and we are expecting our efforts to generate positive results.

More specifically, we will be working to expand our market share in Europe and emphasize strategic measures that leverage synergies with OYL as we undertake such new measures as those aimed at establishing a full-scale presence in Middle Eastern countries, India, and other NIEs. We are also working to realize new business themes, including those related to ultra-differentiated products designed for next-generation air-conditioning product markets, while concurrently striving to augment our overall competitive strength through measures to reduce costs and further enhance product dependability.

For fiscal 2008 as a whole, on a consolidated basis, we are currently projecting that Daikin will generate net sales of ¥1,280.0 billion, up 40.3% from the previous fiscal year. Our profitability targets are for operating income of ¥97.0 billion, up 19.8%; ordinary income of ¥88.0 billion, up 12.1%; and net income of ¥51.0 billion, up 11.8%.

Q11: On May 31, 2007, Daikin increased its capital through a public stock offering. Why did you choose to increase your capital at this time, and do you expect the capital increase to contribute to higher profitability in the future?

A: Among the various goals that we are striving to achieve by fiscal 2011 in line with our FUSION 10 plan are attaining the global No. 1 position as a comprehensive air-conditioning and refrigeration product manufacturer. To achieve this ambitious goal, we will have to undertake M&A transactions in a timely manner, and it will be crucial for us to have a comprehensive financial strategy designed to maintain capabilities for acquisitions and other strategic expansion measures.

In fiscal 2007, we invested ¥246.1 billion to acquire Malaysia-based OYL, which is an important pillar of our strategy for expanding operations in China and North America as well as a key production base with regard to responding to price-competition challenges. As a result of this acquisition, Daikin's dependence on interest-bearing debt will temporarily be elevated. We have thus increased our capital as a means of reducing our debt dependence and augmenting our capabilities for further dynamic measures to globalize and expand the scale of our operations.

In the future, we will endeavor to quickly enhance our financial position through such measures as those to prioritize our investments and expeditiously recover invested funds. On the other hand, we intend to continue proactively undertaking investments and will therefore continue to require considerable funding. The capital increase is an effective means of meeting these various needs.

Q12: Please explain your basic ideas in regard to the best ways to meet the expectations of shareholders and investors.

A: The Daikin Group is relentlessly implementing total-market-value-oriented management policies as it pursues the goal of "meeting the expectations of stockholders, investors, and other stakeholders with respect to performance enhancement and rising corporate value." We have improved our performance in 13 consecutive fiscal years. Our stock price has approximately quintupled during those 13 years, and our total market valuation at March 31, 2007, exceeded ¥1 trillion.

Regarding shareholder returns, we have established a fundamental policy of maintaining our ratio of dividends to net assets at a level of 2% or higher. We are seeking to keep dividend levels stable while making appropriate adjustments based on a comprehensive appraisal of such factors as consolidated performance, financial condition, and funding needs.

As for internal reserves, Daikin is seeking to further strengthen its financial position while also making strategic investments designed to accelerate the development of global operations, progressively upgrade IT tools, and upgrade competitiveness.

Dividends applicable to fiscal 2007 amounted to ¥28 per share (¥14 per share interim dividend and ¥14 per share year-end dividend), up ¥6 per share from the previous fiscal year.

We hope for shareholders' continued understanding and support.

June 29, 2007

Yukiyoshi Okano

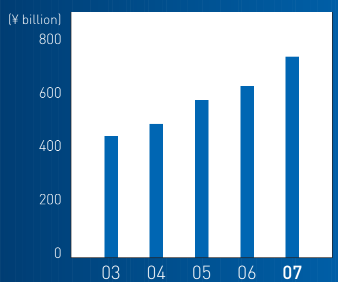
Yukiyoshi Okano
President and COO, Member of the Board

On August 7, 2007, the Company announced a revised projection of consolidated performance in fiscal 2008, which anticipates net sales of ¥1,320.0 billion, operating income of ¥117.0 billion, and ordinary income of ¥109.0 billion. The projection of net income for the fiscal year is unchanged.

Air Conditioning

The Japanese Market

Net Sales



Note: Including the Japanese and global markets

Operating Environment and Performance in Fiscal 2007

In fiscal 2007, ended March 31, 2007, Japanese demand for residential air-conditioning systems was below the fiscal 2006 level, reflecting such nationwide weather situations as the delayed end of the spring-summer rainy season and the unusual coldness of the preceding winter. However, Daikin actively promoted such high-value-added products as URURU & SALALA air-conditioning systems—which feature sophisticated humidifying and dehumidifying capabilities, have already cleared the energy saving standards Japan will introduce from 2010, and are considered to be the industry's No. 1 product in terms of energy-saving performance—and was able to increase its sales volume for such products. This and a January 2007 move to increase new product selling prices by 10% to 15% enabled the Company to keep its net sales at approximately the same level as in the previous fiscal year.

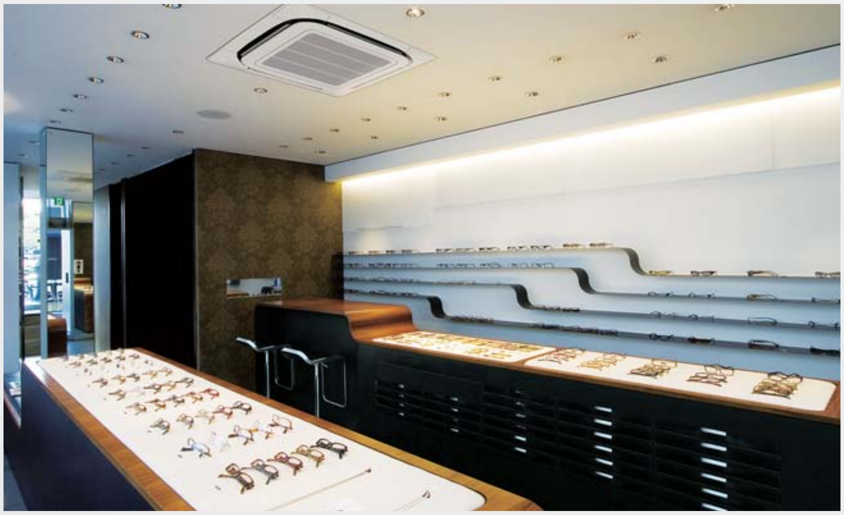
In the commercial air-conditioning system market, demand for package air-conditioning systems fell below the fiscal 2006 level. Daikin emphasized efforts to promote such highly differentiated products as the Ve-up Q multiple air-conditioning system for office buildings, which enables sales outlets and users to rapidly replace units using existing piping, and the Round Flow ZEAS system for shops and stores. These efforts and other marketing promotion activities centered on proposals presented to marketing agencies and users stimulated replacement demand and boosted overall sales volume to above the level in the previous fiscal year. This and measures taken in November 2006 to boost selling prices by an average of 15% supported a rise in net sales to above the level in the previous fiscal year.

Thanks to these initiatives, we increased our domestic sales of air-conditioning systems to 4% above the fiscal 2006 level, to ¥353.6 billion.

In addition, the Company increased its share of both residential and commercial product markets, and its overall market share reached a record-high level.

Thorough Cost Reductions

Although it took the step of implementing price increases against the backdrop of soaring copper, aluminum, and other raw materials prices, Daikin was able to improve its performance, reflecting the effectiveness of its strategies regarding the



provision of high-value-added, highly differentiated products, such as ultrahigh-energy-efficiency room air-conditioning systems, and the stimulation of replacement demand through the proposal of efficient renovation solutions.

In addition to previously emphasized cost-cutting measures, Daikin is seeking to implement still-more-thorough cost-cutting measures, including such measures as the global procurement activities of Daikin and Malaysia-based O.Y.L. Industries Bhd (OYL), develop common components for use worldwide, internalize the manufacture of additional functional components, and optimize the prices of procured components. Regarding components and materials containing considerable amounts of copper, we are working to replace copper items with steel or aluminum items and considering the use of new materials and new processing methods. In these and other ways, we are comprehensively marshalling the efforts of Daikin Group development, procurement, and manufacturing technology units and suppliers to initiate thorough cost-reduction measures.

Realizing a Surge in Eco Cute Business

In its "real solution proposal activities," Daikin is seeking to provide users with information on environmental protection, energy conservation, and comfortable living environments while providing marketing agents with information on customer needs and profitability-enhancing measures. In addition to strengthening capabilities for making proposals, the Company is further leveraging its specialized technical and installation-related strengths to promote sales of various high-value-added products that meet diverse customer needs, including products sold inclusive of installation costs as well as such products as the industry's first "peace-of-mind leases," which provide for all repairs during the lease period to be provided free of charge.

Operations centered on Eco Cute hot water supply systems that use the natural refrigerant CO_2 have grown to be an important business within this segment, second only to residential and commercial air-conditioning business. In November 2006, Daikin greatly expanded and strengthened the Daikin Group's Eco Cute-related units and systems. Plans call for drawing on the abundant experience and know-how Daikin has accumulated in air-conditioning operations as it creates new strategies for promoting growth in hot water supply system business. We are seeking to realize a sharp rise in the market share of Eco Cute products.

We will continue relentlessly striving to make Daikin the undisputed top brand in the field of air conditioning.

Air Conditioning

The Global Market

Operating Environment and Performance in Fiscal 2007

While Daikin's air-conditioning operations in Europe were negatively affected by unseasonable weather during the first half of fiscal 2007, the Company recorded strong sales of both residential and commercial air-conditioning systems during the latter half of the year in such countries as France and Italy. As a result, total sales of air-conditioning systems in Europe were up considerably from the fiscal 2006 level.

In the United States, Daikin established a marketing company in November 2005 that has begun creating a market for the kind of ductless air-conditioning systems sold in Japan. To date, the Company's mainstay product in the United States is a multiple air-conditioning system for office buildings, and sales of this product are growing smoothly.

Growth in the Chinese market was slowed by factors including measures taken to restrain real estate investment, which had been overheated. However, Daikin effectively elicited demand through measures to develop marketing agencies and also promoted greater sales in regional cities, enabling a considerable rise in its net sales.

Daikin also recorded robust sales of both residential and commercial air-conditioning systems in Australia and a large rise in sales of residential air-conditioning systems in Thailand.

As a result, sales in the overseas air-conditioning business climbed 32%, to ¥399.0 billion. This is the first time that Daikin's air-conditioning business sales overseas have exceeded the level of domestic sales.

Additional Proactive Business Development in Europe and North America

To make itself the No. 1 company in the European market for air-conditioning systems by an overwhelming margin, Daikin is seeking to realize a sharp rise in sales of commercial air-conditioning systems in countries where it is already relatively strong, such as Italy and Spain, and thereby thoroughly strengthen its business base.

Daikin recognizes that the implementation in Europe of such strict regulations as the Restriction of the Use of Certain Hazardous Substances (RoHS) and Waste from Electric and Electronic Equipment (WEEE) directives is creating conditions that will facilitate contributions from the Company's most outstanding technologies. Air-conditioning systems with inverter-driven, variable-speed motors are from 40% to 60% more energy efficient than those with single-speed motors. Moreover, CO_2 emissions from heat-pump hot water systems are 60% less than those from fuel-burning systems. Particularly popular are the Altherma heating/hot water systems Daikin has developed for the European market; sales of these products amounted to ¥3.0 billion in fiscal 2007, and we are seeking to increase this figure to ¥10.0 billion in fiscal 2008.

In the United States, Daikin is aiming to more than double the sales volume

of its multiple air-conditioning systems for office buildings during fiscal 2008, to above the 1,600-unit mark. Moreover, in view of strong demand for water-cooling-type equipment in the northeast and southeast portions of the North American market, the Company intends to move forward with measures to further develop those and other market segments through the supply of water-cooling multiple air-conditioning systems for office buildings.

The acquisition of OYL has enabled Daikin to expand its product lineup with the addition of the large-scale (applied) air-conditioning systems of OYL Group member McQuay International, and the Company has therefore established a presence in the applied market. Accordingly, Daikin is emphasizing measures to utilize McQuay's marketing routes and strengthen McQuay's proposal-based marketing capabilities while concurrently striving to stimulate North American demand for ductless air-conditioning products.

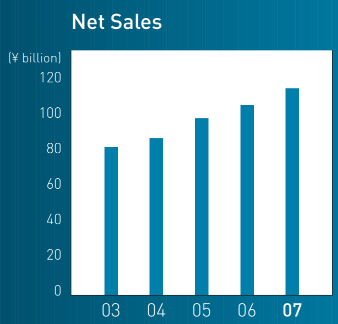
Becoming the Top Company in the Asia-Oceania Region

Besides continuing its previous efforts to expand sales of high-end commercial air-conditioning products in China, the OYL acquisition has positioned Daikin to address a growing range of needs in the Chinese markets for applied and commodity-type products as well as to dynamically expand the scope of its marketing operations to include interior regions in addition to previously covered coastal regions. Moreover, Daikin can now focus on more-tightly focused product and region segments of Chinese markets and further augment its marketing measures aimed at special needs in individual market segments. As a result of such initiatives, Daikin anticipates that it will continue to expand its operations in China and advance toward its goal of being the top air-conditioning product manufacturer in China.

Stable growth is also projected in the air-conditioning product markets of other areas within the Asia and Oceania region. In response to firm demand for applied products, plans call for increasing sales through the broader marketing of a comprehensive range of OYL products. In Australia, Daikin has completed local systems for the manufacture, marketing, and servicing of ducted room air-conditioning products that are unique in the Australian market. This is expected to enable the Company to quickly consolidate its position as the No. 1 brand in Australia.

Regarding Vietnam, Indonesia, and other Asian NIEs, Daikin is clarifying its business strategies and working to strengthen its marketing capabilities. In line with the FUSION 10 goal of boosting net sales in the Asia and Oceania region to above the ¥100 billion mark, Daikin is taking various measures, including those aimed at effectively integrating its marketing networks with those of OYL, aimed at capturing the top market shares of each country's market.

Chemicals



Operating Environment and Performance in Fiscal 2007

Among Daikin's achievements in chemical operations during fiscal 2007 was a sales increase in the fluorochemical sector. In addition to a rise in demand for semiconductor-related products and other products, the increase reflected the strength of chemical sales in Japan, which were positively affected by such trends as a rise in corporate capital investments, as well as growing demand in China and rising sales in North America and Europe. In the chemical products sector, sales of water and oil repellents declined but higher sales of such high-performance materials as surface-enhancement products and pharmaceutical intermediates supported growth in overall sales. Sales in the fluorocarbon gases sector decreased owing to a drop in sales to Asian markets.

As a result, chemical business sales climbed 8.5% from the previous year, to ¥116.5 billion. Operating income advanced 12.2%, to ¥12.1 billion.

Emphasizing Informational Awareness, Safety, and Quality

Daikin intends to further step up its efforts to gather information on users' needs and wants and to monitor competing companies' activities and market trends. The Company expects this emphasis on informational awareness to quickly lead to concrete progress in expanding business operations.

Particularly in the United States, which has the largest market for fluorochemicals, plans call for Daikin America Inc. and other Daikin Group units to further improve their grasp of customer needs and market trends as a means of increasing the Group's market share.

In China, Daikin already has large-scale business in polytetrafluoroethylene (PTFE) and has begun working to establish similar large-scale operations in repellent agents, fluororubber materials, and products for use in LAN cables. At plants, the Company is proceeding with measures to promote workers' acquisition of multiple types of skills as well as to make effective use of workers' expertise while also strengthening and expanding the marketing network and implementing other strategies aimed at augmenting marketing capabilities.

Daikin is giving strong emphasis to the safety of plant operations. In addition to further intensifying the safety promotion previously initiated, the Company is implementing programs designed to make strongly emphasizing safety an integral part of the Daikin Group's culture.

Ensuring high levels of product quality is another key emphasis of Daikin's strategy for the global expansion of chemicals operations. In addition to related efforts being made in Japan, the Company has given its chemical business units responsibility for monitoring and solving quality-related issues at Group plants throughout the world. Amid intensifying global competition, China-based companies are establishing a presence in Japanese markets, and Daikin believes it crucial to position itself to compete with such companies based on overwhelming quality advantages as well as world-class cost-competitiveness. Regarding its manufacturing operations in Japan, Daikin is striving to accelerate its manufacturing system reform programs to realize large cost reductions while also promoting the progressive optimization of materials procurement from a global perspective.

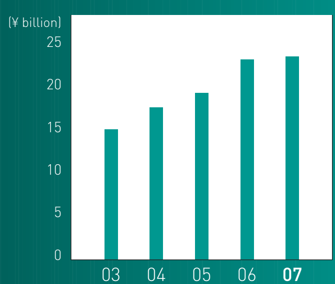
Boosting Product Competitiveness and Establishing New Basis Strengths

From 2007, Daikin's chemicals business strategy is emphasizing the themes of "further strengthening business in repellent agents," "maintaining the No. 1 position in the global market for NEOFLON™ fluorinated ethylene propylene (FEP) insulated LAN cable," and "accelerating the global expansion of fluororubber materials business." The Company considers upgrading product competitiveness to be the key to success regarding each of these themes. Based on programs that promote greater collaboration among Daikin Group marketing, R&D, and manufacturing units throughout the world, Daikin is striving to accelerate the launch of large-scale new products and the development and commercialization of compounds and downstream products.

As means of promoting the attainment of the FUSION 10 targets of "maintaining the global No. 1 position in fluorochemicals business" and "expanding the scope of chemicals business centered on fluorochemicals to create operations that generate a ¥1 trillion market," Daikin is moving forward with the joint development of fluoro-silicon compounds with U.S.-based Dow Corning Corporation with an eye to commercializing the molding and processing applications of these compounds. Plans call for Daikin to selectively undertake additional projects aimed at compounding fluorochemicals with other elements to create large-scale new businesses, with the medium-to-long-term goal of establishing additional core business fields.

Oil Hydraulics

Net Sales



Operating Environment and Performance in Fiscal 2007

Regarding oil hydraulics equipment for industrial machinery, amid robust demand for mainstay machine tool-related products, Daikin increased its market share through the promotion in Japan and other Asian countries of such highly differentiated products as inverter oil hydraulics units and the Oil Con Series of oil and water cooling systems with high-precision temperature control capabilities, and the Company's sales rose to above the fiscal 2006 level. The Company also increased its sales in the field of oil hydraulics equipment for construction machinery, supported by the continued strength of demand in the United States and China.

By creating hybrid hydraulic systems that incorporate motor inverter technologies, Daikin is progressively making fundamental reforms that are shifting the focus from power control products to power motion control (PMC) products with diverse functions for controlling power and position. Using its new technologies to launch unique products not available from competing companies, the Company is steadily expanding its business base.

Emphasizing PMC and Hybrid Products

In fiscal 2008, Daikin is aiming to establish an unshakable position as the No. 1 manufacturer of hybrid oil hydraulics equipment for industrial machinery. In addition, to further strengthen its business base in operations centered on PMC products, the Company is working to use its hybrid oil hydraulics equipment products to earn a higher share of Japan's huge industrial machinery market as a whole rather than focusing on that market's hybrid oil hydraulics equipment segment. To achieve this, Daikin is upgrading its proposal-based marketing capabilities through such measures as those to augment sales engineering and system engineering functions.

In addition, Daikin is continuing to develop conventional oil hydraulics equipment products and reduce the cost of manufacturing such products so that it can offer a broad line of products. In this way, the Company is building peerless capabilities for presenting customers with proposals for systems with optimal combinations of diverse products with complementary characteristics.

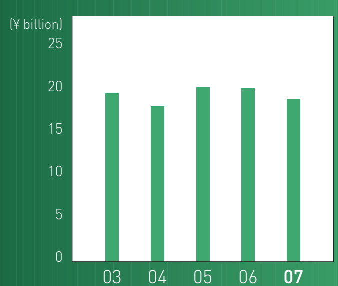
Global Expansion and New Business Development

Global expansion is the key to growth in oil hydraulics equipment business. As conventional oil hydraulics equipment products currently continue to dominate the Chinese market, Daikin is seeking to quickly select a business model for operations in China that involves the creation of an additional pillar of operations in conventional oil hydraulics equipment products and may entail the establishment of a local marketing company. The Company also plans to undertake the global development of molding equipment business by using related technologies developed in Japan and Taiwan to concurrently expand operations in European and South Korean markets.

In addition, Daikin is beginning the full-scale development of its new core interior permanent magnet (IPM) motor technologies that enable high-efficiency motors based on magnet torque and reluctance torque. Plans call for using these technologies to further improve the energy efficiency of hybrid oil hydraulics systems and for accelerating moves aimed at using the technologies to create new businesses outside the scope of current operations.

Defense

Net Sales



Operating Environment and Performance in Fiscal 2007

To secure sustainable development and growth into the future in its defense business, Daikin is continuing to press steadily ahead with its conventional defense operations in addition to actively pursuing activities pertaining to products for the civil sector, including home-use oxygen therapy equipment and civil aircraft components. In fiscal 2007, Daikin took a major step forward in expanding civil sector business by beginning mass production of Eco Cute hot water storage tank units. The Company also implemented thorough cost-cutting measures and other steps to enhance its competitiveness in civil aircraft component manufacturing, which is the core of its commissioned manufacturing operations.

Regarding defense business, while demand for artillery shells and other products is declining as a result of cuts in frontline equipment stipulated by the defense planning outline approved by the Japanese Cabinet at the end of 2004, Daikin's new rifle grenades have been highly evaluated and were chosen to receive the Japan Defense Procurement Structure Improvement Cooperation Award. This product will be contributing to performance from fiscal 2008. Daikin has also moved forward with measures to strengthen the profitability of its defense business through reorganization measures that promote greater efficiency in the utilization of personnel and facilities.

Expanding Civil Sector Business

Plans call for further increasing emphasis on Daikin defense business units' collaboration with other Daikin units as well as with outside entities. Particularly regarding civil sector business, the manufacture of hot water storage tank units will naturally entail greater cooperation with Daikin's air-conditioning equipment manufacturing departments. Regarding home-use oxygen therapy equipment, various kinds of cooperation are being arranged to facilitate the development of oxygen concentration units that are considerably smaller and lighter than previously. In commissioned manufacturing operations, Daikin is striving to arrange subcommissioned work within the Company, shrink civil aircraft component delivery lead time periods, further reduce costs, and realize additional improvements regarding processing precision, while also endeavoring to make all aspects of commissioned manufacturing operations more responsive to customer requirements. To achieve these goals, the Company is considering the possibility of collaboration with engine component manufacturers and other outside entities with leading-edge technologies.

Among strategic measures planned for fiscal 2008 are efforts to select additional new civil sector business themes to be developed in conjunction with defense business development efforts as a means of promoting the overall steady growth of operations in the defense business segment. Daikin is seeking to arrange for cooperation with outside entities that facilitates its efforts to leverage core technologies related to explosives and detonator design to create high-value-added products in the safety and disaster prevention fields.

Electronics

Operating Environment and Performance in Fiscal 2007

Daikin's electronics operations center on the marketing of such systems as the visual R&D knowledge-management systems for corporate R&D departments—unique products that combine accounting ledger, work flow, and database functions—and IT network administration systems that facilitate the integrated management and monitoring of network elements all the way down to the level of individual PC terminals. In accordance with Daikin's "selection and concentration" policy and goal of promoting solutions business, electronics segment units are striving to develop their operations while strongly emphasizing product marketability and product differentiation.

Overall sales in the electronics segment decreased in fiscal 2007, reflecting the impact of moves by universities and government bodies to reduce their budgets for graphic work stations and large-scale servers, but Daikin's efforts to focus marketing activities on relatively profitable products supported a considerable rise in profitability during the year.

In the future, plans call for emphasizing the continued development of core business centered on visual R&D systems and IT network management systems.

Daikin's visual R&D systems support the visual perception of engineering-accounting work flow systems and design processes. Such engineering-accounting work flow systems have been proven to be the most appropriate kind of system for addressing needs related to technical issues as well as the accumulation, analysis, and reuse of quality-related and experimental data. Moreover, needs for such systems are rising steadily due to the growing number of companies that are strategically emphasizing the goal of improving performance with respect to product quality, prices, and delivery dates.

Daikin's IT network management systems help comprehensively manage IT resources, including individual PC terminals, thereby meeting the growing needs of companies seeking to comply with the Japanese version of the Sarbanes-Oxley Act and increase the rigor of their IT security. For example, the Company's *PNDA* is the only Japanese-language agentless* IT system management and monitoring system available as of June 2007. Daikin plans to continue emphasizing product differentiation and the deft use of marketing agencies' marketing routes as it proactively works to promote greater sales of its IT network management systems.

In addition, to lay the foundations for future growth in electronics business over the medium-to-long term, Daikin is addressing additional development themes, such as those related to streaming educational customer relationship management (CRM) systems.

New Product Launches and Alliances

In network business, Daikin launched a LAN quarantine system, the *EQWAC Quarantine System for Apresia*, in June 2006. This system defends corporate LAN systems from viral infections by preventing the LAN systems from connecting with PCs that do not feature the latest security measures. This new product incorporates the Apresia confirmation switch of Hitachi Cable Co., Ltd., and adds security confirmation functions to Daikin's EQWAC comprehensive IT resource management system.

With respect to new development themes, in September 2006 Daikin arranged an alliance with South Korea-based DideoNET Co., Ltd., regarding high-quality video transmission technologies. Based on this alliance, Daikin has already developed and begun marketing its corporate-use *Internet Video Transmission System Pack* product, which incorporates DideoNET's *SEEMEDIA* high-quality video transmission technology.

*Agentless systems are systems that do not require the installation of special software on PC terminals.

Five-Year Summary

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31/March 31

	Millions of yen				
	2007	2006	2005	2004	2003
Net sales:	**¥912,128**	¥792,857	¥728,880	¥625,718	¥572,413
Air conditioning	**752,560**	641,657	589,275	501,186	453,850
Chemicals	**116,493**	107,411	99,612	88,492	83,576
Others	**43,075**	43,789	39,993	36,040	34,987
Operating income	**80,939**	67,077	60,897	47,988	44,789
Income before income taxes and minority interests	**83,313**	67,540	63,802	43,787	36,561
Net income	**45,619**	40,709	38,747	28,611	21,591
Per share of common stock (in yen):					
Basic net income*	**¥173.42**	¥154.25	¥146.76	¥108.18	¥81.48
Diluted net income	**173.34**	154.21			
Cash dividends applicable to the year	**28.00**	22.00	18.00	14.00	12.00
Total assets	**¥1,164,575**	¥719,382	¥617,874	¥536,379	¥475,760
Total equity	**413,121**	343,492	274,122	235,771	205,101
Net property, plant and equipment	**238,319**	196,485	170,209	149,790	145,579
Number of employees	**33,480**	21,747	19,310	17,077	15,845

* Calculated on the basis of the weighted average number of common shares outstanding during each year

In fiscal 2007, ended March 31, 2007, consolidated net sales amounted to ¥912,128 million, an increase of 15.0% from the previous fiscal year, and the seventh consecutive year of growth in net sales. This reflected the Air Conditioning Division's efforts to promote sales of highly differentiated, value-added products in Japan and a trend of large sales expansion in overseas markets, particularly in Europe and China, that was sustained from the previous fiscal year. Other factors contributing to the rise in consolidated net sales included growth in the Chemicals Division's sales of fluororesins, for which demand expanded in Japan and China.

Net Sales by Product Division

Air Conditioning

The Air Conditioning Division's total sales surged 17.3%, to ¥752,560 million.

Japan

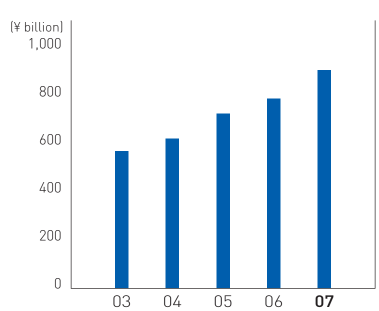
Domestic demand for residential air-conditioning systems was below the fiscal 2006 level, reflecting such nationwide weather situations as the delayed end of the spring-summer rainy season and the unusual coldness of the preceding winter. However, Daikin actively promoted such high-value-added products as URURU & SALALA air-conditioning systems—which feature sophisticated humidifying and dehumidifying capabilities, have already cleared the energy-saving standards Japan will introduce from 2010, and are considered to be the industry's No. 1 product in terms of energy-saving performance—and was able to increase its sales volume for such products. As a result, domestic net sales were sustained at approximately the same level as in the previous fiscal year.

In the commercial air-conditioning system market, while overall demand fell below the fiscal 2006 level, Daikin emphasized efforts to promote such highly differentiated products as the Ve-up Q multiple air-conditioning system for office buildings, which enables sales outlets and users to rapidly replace units using existing piping, and the Round Flow ZEAS system for shops and stores. These efforts and other marketing promotion activities centered on proposals presented to marketing agencies and users stimulated replacement demand and boosted overall sales volume and net sales to above the level in the previous fiscal year.

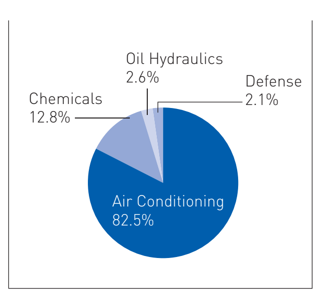
Europe

Daikin's air-conditioning operations in Europe were negatively affected by unseasonable weather through mid-June 2006, which restrained residential product sales. However, a quickly responsive strategic shift of marketing emphasis to commercial products at that time and another quick response by marketing and manufacturing systems to demand trends resulting from extremely hot weather from the latter half of July enabled the Company to record higher sales of both residential and commercial air-conditioning products centered on France and Italy. As a result, total net sales of air-conditioning products in Europe were up considerably. For several years, Daikin has strengthened its marketing network in Europe

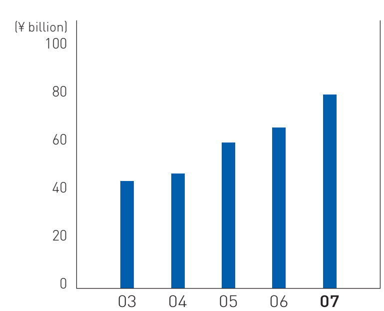
Net Sales



Sales Breakdown



Operating Income



Years Ended March 31,	**2007**	2006	2005	2004	2003
Gross profit (net sales less cost of sales) as a % of net sales	**34.3%**	34.1%	35.2%	34.1%	33.5%
Operating income as a % of net sales	**8.9**	8.5	8.4	7.7	7.8
Interest coverage (operating income plus interest and dividend income divided by interest expense) (times)	**13.8**	15.0	13.4	12.1	11.1
Net income as a % of net sales	**5.0**	5.1	5.3	4.6	3.8

through such measures as those to acquire marketing agencies, and it is believed that the Company's ability to achieve higher sales volume and net sales in fiscal 2007 reflected the benefits of such measures as well as such investments as those made to establish a manufacturing base in the Czech Republic.

China

Growth in the Chinese market was slowed by factors including measures taken to restrain real estate investment, which had been overheated. However, Daikin effectively elicited demand through measures to develop marketing agencies and also promoted greater sales in regional cities, enabling a considerable rise in its net sales.

Asia and Oceania

Daikin increased its sale volume of air-conditioning products in Australia, Thailand, and other countries in the Asia and Oceania region and recorded regional net sales considerably higher than in fiscal 2006.

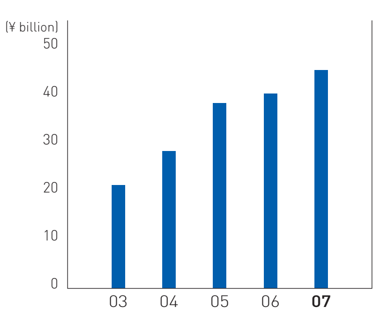
Chemicals

Fluorochemical sales were strong in Japan, reflecting a rise in demand for semiconductor-related products as well as a rise in corporate capital investments, and the division also benefited from demand growth in the Chinese market and higher sales in the U.S. and European markets. Thus, net sales of fluorochemicals increased from fiscal 2006. In the chemical products sector, sales of water and oil repellents declined, but higher sales of such high-performance materials as surface-enhancement products and pharmaceutical intermediates supported growth in overall sales. Sales in the fluorocarbon gases sector decreased, owing to a drop in sales to Asian markets. As a result, chemical business sales climbed 8.5% from the previous year, to ¥116,493 million.

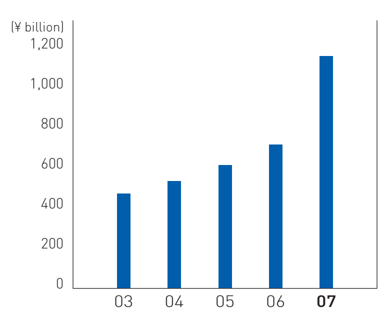
Others

Regarding oil hydraulics equipment for industrial machinery, amid robust demand for mainstay machine tool-related products, Daikin increased its market share through the promotion in Japan and other Asian countries of such highly differentiated products as inverter oil hydraulics units and the Oil Con Series of oil and water cooling systems with high-precision temperature control capabilities, and the Company's sales rose to above the fiscal 2006 level.

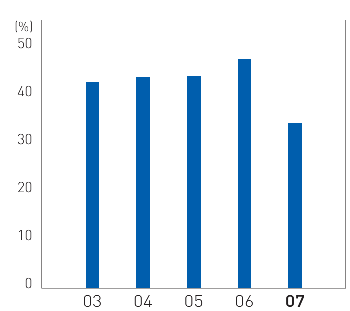
Net Income



Total Assets



Shareholders' Equity Ratio



Years Ended March 31,	2007	2006	2005	2004	2003
	Billions of yen				
Notes and accounts receivable, less allowance for doubtful receivables	**¥204.2**	¥144.9	¥133.7	¥116.0	¥103.1
Inventories	**214.5**	149.2	141.9	110.4	101.1
Interest-bearing debt (not including trade notes discounted)	**456.1**	173.0	166.4	149.0	142.3

The Company also increased its sales in the field of oil hydraulics equipment for construction machinery, supported by the continued strength of demand in the United States and China.

Defense business sales decreased, reflecting a decrease in orders received to provide Japan's Defense Agency with artillery shells and other products.

As a result, net sales in other operations declined 1.6%, to ¥43,075 million.

Costs, Expenses, and Earnings

The cost of sales amounted to ¥599,111 million, up ¥76,725 million. As the Company's efforts to reduce manufacturing costs offset the impact of higher procurement prices for copper, aluminum, and other raw materials, the cost of sales ratio decreased 0.2 percentage point from the previous year, to 65.7%.

Selling, general and administrative (SG&A) expenses increased ¥28,684 million from the previous year, to ¥232,078 million. As a share of net sales, however, SG&A expenses decreased to 25.4%, from 25.7% in fiscal 2006. The rise in SG&A expenses reflected various steps taken in response to growth in global sales volume—such as the boosting of advertising, sales promotion, and product shipment—and measures aimed at preparing for further growth in business scale—such as measures to strengthen sales engineering and R&D capabilities

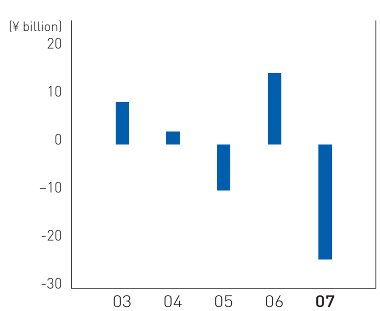
Operating income amounted to ¥80,939 million, up 20.7% from the previous fiscal year. This represented the 7th consecutive year of record-high levels of operating income and the 13th consecutive year of increase. The operating income ratio improved 0.4 percentage point, to 8.9%.

Other income (expenses)—net amounted to income of ¥2,374 million, up ¥1,911 million compared with income of ¥463 million in fiscal 2006, despite such factors as a rise in short-term borrowings and a related increase in interest expense.

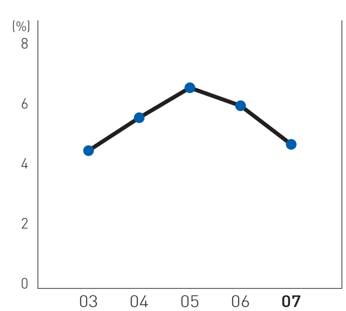
Extraordinary income (expenses)—net amounted to income of ¥4,842 million owing to a gain on foreign currency hedges associated with the acquisition of OYL shares, a gain on the transfer of oil hydraulic multi-tier parking equipment business, and a gain on the termination of a portion of the retirement payment system.

As a result, net income amounted to ¥45,619 million, up 12.1% from fiscal 2006.

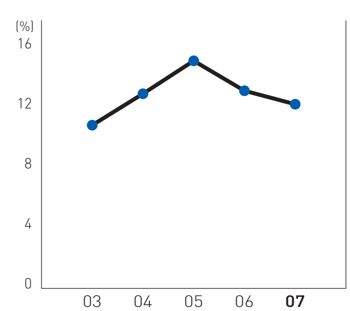
Free Cash Flow (FCF)



Return on Assets (ROA)



Return on Equity (ROE)



Financial Position

During fiscal 2007, Daikin acquired all the outstanding shares of OYL and transformed that company into a wholly owned subsidiary. As the de facto acquisition date was December 31, 2006, OYL was not included within the scope of consolidation until the end of the fiscal year. As a result of the inclusion, consolidated total assets amounted to ¥1,164,575 million, up ¥445,193 million from the previous fiscal year-end.

Current assets were increased by the consolidation of OYL as well as by growth in receivables and inventories that accompanied the expansion of operations centered on air-conditioning operations. As a result, current assets totaled ¥540,770 million, up ¥149,799 million.

The acquisition of OYL led to the generation of consolidated goodwill as well as a rise in fixed assets upon the consolidation of OYL. This and growth in facilities of overseas bases were primary factors boosting fixed assets to ¥623,805 million, up ¥295,394 million.

Total liabilities amounted to ¥751,454 million, up ¥386,802 million from the previous fiscal year-end.

Current liabilities grew ¥353,965 million, to ¥638,419 million, mainly owing to a rise in short-term borrowings that was mainly for the purpose of funding the acquisition of OYL shares.

For the above reasons, interest-bearing debt increased ¥283,078 million compared with the previous year-end, and the ratio of interest-bearing debt to total assets rose to 39.2%.

Regarding net assets, at the end of fiscal 2006, total shareholders' equity and minority interests amounted to ¥354,730 million. Reflecting a rise in retained earnings that resulted from growth in net income, net assets grew ¥58,391 million above that level, to ¥413,121 million.

The equity ratio fell to 35.5%, from 47.7% at the end of fiscal 2006.

Cash Flows

Net cash provided by operating activities increased ¥20,214 million from the fiscal 2006 level, to ¥83,725 million, reflecting rises in income before income taxes and minority interests and in depreciation and amortization.

Net cash used in investing activities grew ¥241,831 million, to ¥305,251 million, mainly owing to the acquisition of OYL shares.

Net cash provided by financing activities was ¥245,975 million, a ¥250,259 million change from ¥4,284 million of net cash used in financing activities in fiscal 2006, reflecting the growth in short-term borrowings.

As a result, cash and cash equivalents, end of year, totaled ¥82,659 million.

Dividends

Daikin is taking various measures to expand its operations and bolster its operating structure and thereby realize its top-priority objective of maximizing corporate value. For example, the Company is establishing virtual companies and introducing the use of such indicators as free cash flow (FCF), Daikin Value Added (DVA, an in-house-developed metric), return on assets (ROA), and return on equity (ROE) as management tools. Regarding returns to shareholders, the Company has a fundamental policy of maintaining the ratio of cash dividends to net assets (consolidated basis) at 2.0% or higher and seeking to set stable levels of dividends based on a comprehensive consideration of such factors as the Company's consolidated performance, financial position, and funding requirements. Dividend payments applicable to the fiscal year under review were ¥28.00 per share, up ¥6.00 per share from the previous fiscal year.

Consolidated Goodwill Associated with Acquisition of OYL

The acquisition of OYL led to the recording of ¥204.4 billion in consolidated goodwill. Plans call for this figure to be amortized according to the straight-line method over 20 years (at a rate of ¥10.2 billion per year).

This amortization expense will be accounted for within SG&A expenses.

Fund Procurement through Public Stock Offering

The May 31 meeting of the Board of Directors approved a proposal to issue new stock and sell that stock with an over-allotment option.

The public offering resulted in the issuance of 25.5 million new shares and a third-party allotment of 3.8 million shares, increasing the Company's total outstanding shares by 28.8 million, to 293,113,973.

The public offering generated ¥114.0 billion in funds (amount received), and plans call for using all of these funds to repay borrowings.

Consolidated Balance Sheets

Daikin Industries, Ltd. and Consolidated Subsidiaries
March 31, 2007 and 2006

	Millions of yen	
ASSETS	**2007**	2006
Current assets:		
Cash and cash equivalents	**¥ 82,659**	¥ 54,178
Short-term investments	**1,258**	1,284
Trade receivables (Notes 7 and 8):		
Notes	**12,988**	10,354
Accounts	**197,607**	137,326
Allowance for doubtful receivables	**(6,374)**	(2,822)
Inventories (Notes 3 and 8)	**214,534**	149,242
Deferred tax assets (Note 12)	**12,692**	14,845
Prepaid expenses and other current assets (Note 8)	**25,406**	26,564
Total current assets	**540,770**	390,971
Property, plant and equipment (Note 8):		
Land (Note 4)	**28,500**	24,264
Buildings and structures (Note 4)	**156,201**	137,467
Machinery and equipment	**334,734**	286,135
Furniture and fixtures	**98,632**	86,244
Construction in progress	**20,331**	9,239
Total	**638,398**	543,349
Accumulated depreciation	**400,079**	(346,864)
Net property, plant and equipment	**238,319**	196,485
Investments and other assets:		
Investment securities (Note 5)	**132,840**	103,998
Investments in and advances to unconsolidated subsidiaries and associated companies	**4,628**	3,733
Goodwill (Note 6)	**210,505**	6,707
Deferred tax assets (Note 12)	**8,732**	2,045
Other assets (Note 4)	**28,781**	15,443
Total investments and other assets	**385,486**	131,926
Total	**¥1,164,575**	¥719,382

See notes to consolidated financial statements.

LIABILITIES AND EQUITY	Millions of yen 2007	2006
Current liabilities:		
Short-term borrowings (Note 8)	**¥ 376,783**	¥113,687
Current portion of long-term debt (Note 8)	**10,755**	3,278
Trade payables (Note 7):		
Notes	**9,468**	8,494
Accounts	**112,359**	75,758
Construction payable	**10,231**	12,859
Income taxes payable	**13,581**	7,644
Deferred tax liabilities (Note 12)	**644**	32
Accrued expenses	**49,213**	29,785
Other current liabilities	**55,385**	32,917
Total current liabilities	**638,419**	284,454
Long-term liabilities:		
Long-term debt (Note 8)	**68,535**	56,030
Liabilities for retirement benefits (Note 9)	**5,159**	5,072
Deferred tax liabilities (Note 12)	**24,971**	18,531
Long-term accounts payable	**13,508**	565
Other long-term liabilities	**862**	
Total long-term liabilities	**113,035**	80,198
Minority interests		11,238
Commitments and contingent liabilities (Note 17)		
Equity (Notes 10, 11 and 18):		
Common stock—authorized, 500,000,000 shares; issued 263,813,973 shares in 2007 and 2006	**28,023**	28,023
Capital surplus	**25,968**	25,968
Stock acquisition rights	**219**	
Retained earnings	**289,106**	250,247
Net unrealized gain on available-for-sale securities	**33,780**	33,054
Deferred loss on derivatives under hedge accounting	**(26)**	
Foreign currency translation adjustments	**26,227**	7,750
Treasury stock, at cost: 797,424 shares in 2007 and 622,947 shares in 2006	**(2,367)**	(1,550)
Total	**400,930**	343,492
Minority interests	**12,191**	
Total equity	**413,121**	343,492
Total	**¥1,164,575**	¥719,382

Consolidated Statements of Income

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2007 and 2006

	Millions of yen	
	2007	2006
Net sales (Note 7)	**¥912,128**	¥792,857
Cost of sales (Note 7)	**599,111**	522,386
Gross profit	**313,017**	270,471
Selling, general and administrative expenses (Note 7)	**232,078**	203,394
Operating income	**80,939**	67,077
Other income (expenses):		
Interest and dividend income	**2,623**	2,051
Interest expense	**(6,065)**	(4,615)
Exchange gains	**691**	1,050
Gain on sales of land	**12**	
Loss on disposals of property, plant and equipment	**(870)**	(1,045)
Loss on impairment of long-lived assets (Note 4)		(796)
Gain on sales of investment securities	**347**	1,249
Gain on sales of shares of subsidiary	**16**	
Gain on the foreign exchange hedge transaction of acquiring subsidiary	**4,244**	
Write-down of investment securities	**(25)**	(45)
Equity in earnings of unconsolidated subsidiaries and associated companies	**589**	505
Gain on insurance for fire in Spain—net		1,448
Gain on transfer of oil hydraulic multi-tier parking equipment maintenance business	**700**	
Gain on partial termination of defined benefit pension plan	**681**	
Loss on withdrawal from oil hydraulic multi-tier parking equipment business		(1,952)
Loss on restructuring of subsidiary	**(263)**	
Other—net	**(306)**	2,613
Other income (expenses)—net	**2,374**	463
Income before income taxes and minority interests	**83,313**	67,540
Income taxes (Notes 2 and 12):		
Current	**28,984**	23,936
Deferred	**5,792**	274
Total	**34,776**	24,210
Minority interests	**(2,918)**	(2,621)
Net income	**¥ 45,619**	¥ 40,709
	Yen	
Amounts per common share (Notes 2 and 18):		
Basic net income	**¥173.42**	¥154.25
Diluted net income	**173.34**	154.21
Cash dividends applicable to the year	**28.00**	22.00

See notes to consolidated financial statements.

Consolidated Statements of Changes in Equity

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2007 and 2006

	Outstanding Number of Common Shares Issued	Millions of yen										
		Common Stock	Capital Surplus	Stock Acquisition Right	Retained Earnings	Unrealized Gain on Available-for-Sale Securities	Deferred Loss on Derivatives under Hedge Accounting	Foreign Currency Translation Adjustments	Treasury Stock	Total	Minority Interests	Total Equity
Balance, April 1, 2005	263,252,803	¥ 28,023	¥ 25,971		¥ 215,681	¥ 12,295		¥ (6,501)	¥ (1,347)	¥274,122		¥274,122
Cumulative effect of consolidating subsidiaries previously unconsolidated					23					23		23
Effect of change of the fiscal year-end of a certain consolidated subsidiary (Note 2)					(265)					(265)		(265)
Net income					40,709					40,709		40,709
Cash dividends, ¥22 per share					(5,791)					(5,791)		(5,791)
Bonuses to directors and corporate auditors					(110)					(110)		(110)
Repurchase of treasury stock	(155,367)								(435)	(435)		(435)
Disposal of treasury stock	93,590		(3)						232	229		229
Net unrealized gain on available-for-sale securities						20,759				20,759		20,759
Foreign currency translation adjustments								14,251		14,251		14,251
Balance, March 31, 2006	263,191,026	28,023	25,968		250,247	33,054		7,750	(1,550)	343,492		343,492
Reclassified balance as of March 31, 2006 (Note 2)											**¥11,238**	**11,238**
Effect of change of the fiscal year-end of a certain consolidated subsidiary (Note 2)					**(38)**					**(38)**		**(38)**
Net income					**45,619**					**45,619**		**45,619**
Cash dividends, ¥28 per share					**(6,577)**					**(6,577)**		**(6,577)**
Bonuses to directors and corporate auditors					**(110)**					**(110)**		**(110)**
Repurchase of treasury stock	**(299,167)**								**(1,163)**	**(1,163)**		**(1,163)**
Disposal of treasury stock	**124,690**				**(35)**				**346**	**311**		**311**
Net change in the year				**¥219**		**726**	**¥(26)**	**18,477**		**19,396**	**953**	**20,349**
Balance, March 31, 2007	**263,016,549**	**¥28,023**	**¥25,968**	**¥219**	**¥289,106**	**¥33,780**	**¥(26)**	**¥26,227**	**¥(2,367)**	**¥400,930**	**¥12,191**	**¥413,121**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2007 and 2006

	Millions of yen	
	2007	2006
Operating activities:		
Income before income taxes and minority interests	**¥ 83,313**	¥67,540
Adjustment for:		
Income taxes—paid	**(24,271)**	(25,281)
Proceeds from insurance for fire in Spain—net		3,379
Proceeds from transfer of oil hydraulic multi-tier parking equipment maintenance business	**700**	
Proceeds on the foreign exchange hedge transaction of acquiring subsidiary—net	**4,244**	
Depreciation and amortization	**34,561**	29,269
Gain on sales of investment securities	**(347)**	(1,249)
Gain on sales of shares of subsidiary	**(16)**	
Write-down of investment securities	**25**	45
Gain on sales of land	**(12)**	
Loss on disposals of property, plant and equipment	**870**	1,045
Loss on impairment of long-lived assets		796
Gain on insurance for fire in Spain—net		(1,448)
Gain on transfer of oil hydraulic multi-tier parking equipment maintenance business	**(700)**	
Loss on withdrawal from oil hydraulic multi-tier parking equipment business		1,952
Gain on the foreign exchange hedge transaction of acquiring subsidiary	**(4,244)**	
Equity in earnings of unconsolidated subsidiaries and associated companies	**(589)**	(505)
Changes in assets and liabilities, net of effects of the purchase of subsidiaries and a newly consolidated subsidiary:		
Trade notes and accounts receivable	**(9,077)**	(8,251)
Inventories	**(21,147)**	(5,084)
Other current assets	**5,745**	(5,608)
Prepaid pension cost	**(12,598)**	
Trade notes and accounts payable	**5,202**	4,945
Accrued expenses	**4,968**	(26)
Other current liabilities	**6,090**	1,643
Liabilities for retirement benefits	**(3,488)**	
Account payable for transaction to defined contribution pension plan	**13,458**	
Other—net	**1,038**	349
Total adjustments	**412**	(4,029)
Net cash provided by operating activities	**83,725**	63,511
Investing activities:		
Purchases of property, plant and equipment	**(42,573)**	(46,169)
Payment for acquisition of shares of newly consolidated subsidiaries, net of cash and cash equivalents acquired (Note 13)	**(235,686)**	
Increase in investments in unconsolidated subsidiaries and associated companies		(60)
Payment for purchase of minority interest		(115)
Payments to acquire investment securities	**(27,881)**	(18,090)
Proceeds from sales of investment securities	**385**	3,204
Other—net	**504**	(2,190)
Net cash used in investing activities	**(305,251)**	(63,420)
Financing activities:		
Net increase in short-term borrowings	**254,098**	15,760
Increase in long-term debt	**4,127**	1,903
Repayments of long-term debt	**(3,453)**	(14,419)
Payments of cash dividends	**(6,577)**	(5,791)
Other—net	**(2,220)**	(1,737)
Net cash provided by (used in) financing activities	**245,975**	(4,284)
Effect of exchange rate changes on cash and cash equivalents	**4,014**	3,226
Net increase (decrease) in cash and cash equivalents	**28,463**	(967)
Cash and cash equivalents of newly consolidated subsidiaries, beginning of year		347
Effect of change of the fiscal year-end of consolidated subsidiaries	**18**	(588)
Cash and cash equivalents, beginning of year	**54,178**	55,386
Cash and cash equivalents, end of year	**¥ 82,659**	¥54,178

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Daikin Industries, Ltd. and Consolidated Subsidiaries Years Ended March 31, 2007 and 2006

1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared from the consolidated financial statements issued for domestic reporting purposes in Japan, which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards. Daikin Industries, Ltd. (the "Company") and its consolidated domestic subsidiaries maintain their accounts and records in accordance with the provisions set forth in the Japanese Corporate Law and in conformity with accounting principles generally accepted in Japan, and its consolidated foreign subsidiaries in conformity with those of their respective countries of their domicile.

On December 27, 2005, the Accounting Standards Board of Japan (the "ASBJ") published a new accounting standard for the statement of changes in equity, which is effective for fiscal years ending on or after May 1, 2006. The statement of shareholders' equity, which was previously voluntarily prepared in line with the international accounting practices, is now required under generally accepted accounting principles in Japan ("Japanese GAAP") and has been renamed "the statement of changes in equity" in the current fiscal year.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the Company's consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan.

In addition, certain reclassifications have been made in the 2006 financial statements to conform to the classification used in 2007.

2. Summary of Significant Accounting Policies

Principles of Consolidation and Accounting for Investments in Unconsolidated Subsidiaries and Associated Companies

The accompanying consolidated financial statements include the accounts of the Company and its significant subsidiaries (together, the "Group").

Under the control or influence concept, those companies in which the Company, directly or indirectly, is able to exercise control are fully consolidated, and those companies over which the Group has the ability to exercise significant influence are accounted for by the equity method.

The Group applies the equity method of accounting for investments in unconsolidated subsidiaries and associated companies except for certain insignificant companies. Investments in such insignificant companies are stated at cost except that appropriate write-downs are recorded for investments for which the value has been permanently impaired. If these subsidiaries and associated companies had been consolidated and accounted for using the equity method, respectively, the effect on the accompanying consolidated financial statements would not have been material.

For the years ended March 31, 2007 and 2006, the Company consolidated the results of consolidated subsidiaries Daikin Airconditioning Portugal S.A. and Daikin Airconditioning UK Ltd. for the 15-month period ended March 31, 2007 and 2006, respectively, because such subsidiaries changed their fiscal year-end from December 31 to March 31. The Company included the subsidiaries' results for the 12-month period in the consolidated statements of income, and included their results for the three-month period in the consolidated statements of changes in equity as effect of change of the fiscal year-end of a certain consolidated subsidiary.

The excess of the cost of an acquisition over the fair value of the net assets of the acquired subsidiary at the date of acquisition (the "Consolidation goodwill") is to be amortized over a period of 5 to 20 years.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

Cash Equivalents

Cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value.

Cash equivalents include time deposits, marketable debt securities issued by the Japanese Government and private companies, all of which mature or become due within three months of the date of acquisition.

Marketable debt securities that mature or become due in more than three months but within a year of the date of acquisition are recorded as short-term investments.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is stated in amounts considered to be appropriate based on the companies' past credit loss experience and an evaluation of potential losses in the receivables outstanding.

Inventories

Inventories of the Company and its consolidated domestic subsidiaries are principally stated at cost, determined by the average method. Inventories of consolidated foreign subsidiaries are principally stated at the lower of cost, determined by the average method, or market.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Depreciation of property, plant and equipment of the Company and its consolidated domestic subsidiaries is computed by the declining-balance method while the straight-line method is applied to buildings acquired after April 1, 1998, at rates based on the estimated useful lives of the assets. Depreciation of property, plant and equipment of consolidated foreign subsidiaries is principally computed by the straight-line method at rates based on the estimated useful lives of the assets.

The range of useful lives is 15 to 50 years for buildings and structures, 5 to 15 years for machinery and equipment and 2 to 10 years for furniture and fixtures.

Long-Lived Assets

In August 2002, the Business Accounting Council (the "BAC") issued a Statement of Opinion, *Accounting for Impairment of Fixed Assets,* and in October 2003, ASBJ issued ASBJ Guidance No. 6, *Guidance for Accounting Standard for Impairment of Fixed Assets.* These new pronouncements were effective for fiscal years beginning on or after April 1, 2005 with early adoption permitted for fiscal years ending on or after March 31, 2004.

The Group adopted the new accounting standard for impairment of fixed assets as of April 1, 2005.

The Group reviews its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

The effect of adoption of the new accounting standard for impairment of fixed assets was to decrease income before income taxes and minority interests for the year ended March 31, 2006 by ¥796 million.

Leases

Under Japanese accounting standards for leases, finance leases that are deemed to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the financial statements.

Investment Securities

Under the Japanese accounting standard for financial instruments, all marketable securities held by the Group are classified as available-for-sale securities and are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of equity. The cost of securities sold is principally determined based on the moving-average method.

Non-marketable available-for-sale securities are stated at cost principally determined by the moving-average method.

For other than temporary declines in fair value, available-for-sale securities are reduced to net realizable value by charging such losses to income.

Employees' Retirement Benefits

The Company and its consolidated domestic subsidiaries have a non-contributory funded pension plan covering substantially all of its employees. Effective April 1, 2000, the Company and its consolidated domestic subsidiaries adopted a new accounting standard for employees' retirement benefits and accounted for the liability for retirement benefits based on projected benefit obligations and plan assets at the balance sheet date. The transitional obligation of ¥25,249 million as of April 1, 2000 is being amortized over 7 years and the annual amortization is presented as selling, general and administrative expenses in the consolidated statements of income.

Based on an agreement between labor and management in March 2006, the Company and certain consolidated subsidiaries implemented a defined benefit pension plan and a defined contribution pension plan effective June 1, 2006, by which time the former qualified defined benefit pension plan was terminated.

The Company and certain consolidated subsidiaries applied accounting treatments specified in the guidance issued by the ASBJ. The effect of this transfer was to increase income before income taxes and minority interests by ¥681 million and was recorded as a gain on partial termination of the defined benefit pension plan in the consolidated statements of income for the year ended March 31, 2007.

Stock Options

On December 27, 2005, the ASBJ issued ASBJ Statement No. 8, *Accounting Standard for Stock Options* and related guidance. The new standard and guidance are applicable to stock options newly granted on and after May 1, 2006.

This standard requires companies to recognize compensation expense for employee stock options based on the fair value at the date of grant and over the vesting period as consideration for receiving goods or services. The standard also requires companies to account for stock options granted to non-employees based on the fair value of either the stock option or the goods or services received. In the balance sheet, the stock option is presented as a stock acquisition right as a separate component of equity until exercised. The standard covers equity-settled, share-based payment transactions, but does not cover cash-settled, share-based payment transactions. In addition, the standard allows unlisted companies to measure options at their intrinsic value if they cannot reliably estimate fair value.

The Company applied the new accounting standard for stock options to those granted on and after May 1, 2006. The effect of adoption of this accounting standard for the year ended March 31, 2007 was to decrease income before income taxes and minority interests by ¥219 million.

Presentation of Equity

On December 9, 2005, the ASBJ published a new accounting standard for presentation of equity. Under this accounting standard, certain items which were previously presented as liabilities are now presented as components of equity. Such items include stock acquisition rights, minority interests and any deferred gain or loss on derivatives under hedge accounting. This standard is effective for fiscal years ending on or after May 1, 2006. The consolidated balance sheet as of March 31, 2007 is presented in line with this new accounting standard.

Foreign Currency Transactions

All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the exchange rates at the balance sheet date. The foreign exchange gains and losses from translation are recognized in the consolidated statements of income to the extent that they are not hedged by forward exchange contracts.

Foreign Currency Financial Statements

The balance sheet accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the current exchange rates as of the balance sheet date except for equity, which is translated at historical rates. Revenue and expense accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the average exchange rates. Differences arising from such translations were shown as "Foreign currency translation adjustments" in a separate component of equity.

Bonuses to Directors and Corporate Auditors

Prior to the fiscal year ended March 31, 2005, bonuses to directors and corporate auditors were accounted for as a reduction of retained earnings in the fiscal year following approval at the general shareholders' meeting. The ASBJ issued ASBJ Practical Issues Task Force (the "PITF") No. 13, *Accounting Treatment for Bonuses to Directors and Corporate Auditors*, which encouraged companies to record bonuses to directors and corporate auditors on the accrual basis with a related charge to income but still permitted the direct reduction of such bonuses from retained earnings after approval of the appropriation of retained earnings.

The ASBJ replaced the above accounting pronouncement by issuing a new accounting standard for bonuses to directors and corporate auditors on November 29, 2005. Under the new accounting standard, bonuses to directors and corporate auditors must be expensed and are no longer allowed to be directly charged to retained earnings. This accounting standard is effective for fiscal years ending on or after May 1, 2006. The companies must accrue bonuses to directors and corporate auditors at the year-end to which such bonuses are attributable.

The Company and its consolidated domestic subsidiaries adopted the new accounting standard for bonuses to directors and corporate auditors in the year ended March 31, 2007. The effect of adoption of this accounting standard was to decrease income before income taxes and minority interests for the year ended March 31, 2007 by ¥151 million.

Income Taxes

The provision for current income taxes is computed based on the income before income taxes and minority interests included in the consolidated statements of income. Deferred income taxes are recorded to reflect the impact of temporary differences between assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes. These deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

Derivative Financial Instruments

The Group uses foreign exchange forward contracts, currency swaps and currency options to hedge foreign exchange risk associated with certain assets and liabilities denominated in foreign currencies, mainly interest rate swaps and interest rate options to manage its exposures to fluctuations in interest rates, and commodity future contracts to hedge the risk of fluctuation of commodity prices for materials. The Group does not enter into derivatives for trading or speculative purposes.

Derivative financial instruments and foreign currency transactions are classified and accounted for as follows: a) all derivatives are recognized as either assets or liabilities and measured at fair value, and gains or losses on derivative transactions are recognized in the consolidated statements of income and b) for derivatives used for hedging purposes, if such derivatives qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, gains or losses are deferred until maturity of the hedged transactions.

The interest rate swaps that qualify for hedge accounting and meet specific matching criteria are not remeasured at market value but the differential paid or received under the swap agreements is recognized and included in interest expense or income.

Appropriations of Retained Earnings

Appropriations of retained earnings at each year-end are reflected in the financial statements for the following year upon shareholders' approval.

Amounts per Common Share

Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period, retroactively adjusted for stock splits.

Diluted net income per share of common stock assumes full exercise of the outstanding stock options which have dilutive effect.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years, including dividends to be paid after the end of the year.

Business Combination and Business Separation

In October 2003, the BAC issued a Statement of Opinion, *Accounting for Business Combinations,* and on December 27, 2005, the ASBJ issued ASBJ Statement No. 7, *Accounting Standard for Business Separations* and ASBJ Guidance No. 10, *Guidance for Accounting Standard for Business Combinations and Business Separations*. These new accounting pronouncements were effective for fiscal years beginning on or after April 1, 2006.

The accounting standard for business combinations allows companies to apply the pooling of interests method of accounting only when certain specific criteria are met such that the business combination is essentially regarded as a uniting-of-interests.

For business combinations that do not meet the uniting-of-interests criteria, the business combination is considered to be an acquisition and the purchase method of accounting is required. This standard also prescribes the accounting for combinations of entities under common control and for joint ventures.

Under the accounting standard for business separations, in a business separation where the interests of the investor no longer continue and the investment is settled, the difference between the fair value of the consideration received for the transferred business and the book value of net assets transferred to the separated business is recognized as a gain or loss on business separation in the statement of income. In a business separation where the interests of the investor continue and the investment is not settled, no such gain or loss on business separation is recognized.

New Accounting Pronouncements

Measurement of Inventories

Under Japanese GAAP, inventories are currently measured either by the cost method, or at the lower of cost or market. On July 5, 2006, the ASBJ issued ASBJ Statement No. 9, *Accounting Standard for Measurement of Inventories*, which is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted. This standard requires that inventories held for sale in the ordinary course of business be measured at the lower of cost or net selling value, which is defined as the selling price less additional estimated manufacturing costs and estimated direct selling expenses. The replacement cost may be used in place of the net selling value, if appropriate. The standard also requires that inventories held for trading purposes be measured at the market price.

Lease Accounting

On March 30, 2007, the ASBJ issued ASBJ Statement No. 13, *Accounting Standard for Lease Transactions*, which revised the existing accounting standard for lease transactions issued on June 17, 1993.

Under the existing accounting standard, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized; however, other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the note to the lessee's financial statements.

The revised accounting standard requires that all finance lease transactions should be capitalized. The revised accounting standard for lease transactions is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted for fiscal years beginning on or after April 1, 2007.

Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements

Under Japanese GAAP, a company currently can use the financial statements of foreign subsidiaries which are prepared in accordance with generally accepted accounting principles in their respective jurisdictions for its consolidation process unless they are clearly unreasonable. On May 17, 2006, the ASBJ issued ASBJ PITF No. 18, *Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements*. The new task force prescribes: 1) the accounting policies and procedures applied to a parent company and its subsidiaries for similar transactions and events under similar circumstances should in principle be unified for the preparation of the consolidated financial statements, 2) financial statements prepared by foreign subsidiaries in accordance with either International Financial Reporting Standards or the generally accepted accounting principles in the United States tentatively may be used for the consolidation process, 3) however, the following items should be adjusted in the consolidation process so that net income is accounted for in accordance with Japanese GAAP unless they are not material:

(1) Amortization of goodwill
(2) Actuarial gains and losses of defined benefit plans recognized outside profit or loss
(3) Capitalization of intangible assets arising from development phases
(4) Fair value measurement of investment properties, and the revaluation model for property, plant and equipment, and intangible assets
(5) Retrospective application when accounting policies are changed
(6) Accounting for net income attributable to a minority interest

The new task force is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted.

3. Inventories

Inventories at March 31, 2007 and 2006 consisted of the following:

	Millions of yen	
	2007	2006
Finished products and merchandise	**¥122,776**	¥ 85,103
Semi-finished products and work-in-process	**51,830**	43,180
Raw materials and supplies	**39,928**	20,959
Total	**¥214,534**	¥149,242

4. Long-Lived Assets

The Group reviewed its long-lived assets for impairment for the year ended March 31, 2006 and, as a result, recognized an impairment loss of ¥796 million as other expense for certain land, buildings and leaseholds, which were deemed to be idle assets with no future plan for utilization and of which the carrying amount exceeded the fair value. The carrying amount of the relevant assets was written down to the recoverable amount. The recoverable amount of these assets was measured by the net selling price at disposition, which was primarily determined by independent real estate appraisals of land and buildings. No impairment loss was recognized for the year ended March 31, 2007.

5. Investment Securities

The acquisition costs and aggregate fair values of marketable available-for-sale securities included in investment securities at March 31, 2007 and 2006 were as follows:

	Millions of yen			
	2007			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as available-for-sale:				
Equity securities	**¥71,942**	**¥56,704**	**¥(193)**	**¥128,453**
Other	**503**	**362**		**865**
Total	**¥72,445**	**¥57,066**	**¥(193)**	**¥129,318**

	Millions of yen			
	2006			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as available-for-sale:				
Equity securities	¥44,909	¥55,219	¥(21)	¥100,107
Other	504	444		948
Total	¥45,413	¥55,663	¥(21)	¥101,055

Available-for-sale securities whose fair value is not readily determinable as of March 31, 2007 and 2006 were as follows:

	Millions of yen	
	Carrying Amount	
	2007	2006
Available-for-sale:		
Equity securities	**¥2,171**	¥1,910
Other	**1,351**	1,033
Total	**¥3,522**	¥2,943

Proceeds from sales of available-for-sale securities for the years ended March 31, 2007 and 2006 were ¥385 million and ¥3,204 million, respectively. Gross realized gains on these sales principally computed on the moving average cost basis were ¥347 million and ¥1,249 million for the years ended March 31, 2007 and 2006, respectively.

6. Goodwill

Goodwill at March 31, 2007 and 2006 consisted of the following:

	Millions of yen	
	2007	2006
Consolidation goodwill	**¥209,396**	¥5,427
Others	**1,109**	1,280
Total	**¥210,505**	¥6,707

7. Related Party Transactions

Receivables and payables, with respect to transactions with unconsolidated subsidiaries and associated companies, at March 31, 2007 and 2006 were as follows:

	Millions of yen	
	2007	2006
Trade notes and accounts receivable	**¥921**	¥2,172
Trade notes and accounts payable	**701**	695

Sales to and purchases from unconsolidated subsidiaries and associated companies for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen	
	2007	2006
Sales	**¥18,984**	¥16,340
Purchases	**7,546**	8,102

Material transactions and balances with related individuals for the years ended March 31, 2007 and 2006 were as follows:

			Millions of yen			
			Transactions		Resulting Account Balances	
Name	Description of Post	Ownership of the Company (%)	Description of Transaction	**2007**	Account	**2007**
Noriyuki Inoue	Chairman of the Board and CEO/Director General of Daikin Foundation for Contemporary Arts	0.02	Donation to Daikin Foundation for Contemporary Arts	**¥ 6**		
	Director General of Kansai Philharmonic Orchestra		Donation and support money to Kansai Philharmonic Orchestra	**48**		
Chiyono Terada	Outside Director/CEO and President of Art Cooperation	0.00	Commission of move business and delivery business	**53**	Other current liabilities	**¥3**

			Millions of yen			
			Transactions		Resulting Account Balances	
Name	Description of Post	Ownership of the Company (%)	Description of Transaction	2006	Account	2006
Noriyuki Inoue	Chairman of the Board and CEO/Director General of Daikin Foundation for Contemporary Arts	0.02	Donation to Daikin Foundation for Contemporary Arts	¥7		

8. Short-Term Borrowings and Long-Term Debt

Short-term borrowings of the Group at March 31, 2007 and 2006 consisted of the following:

	Millions of yen	
	2007	2006
Bank overdrafts and notes to banks	**¥287,783**	¥ 53,044
Commercial paper	**89,000**	60,643
Total	**¥376,783**	¥113,687

Unused short-term bank credit lines were ¥25,000 million at March 31, 2007. Weighted average interest rates of bank overdrafts and notes to banks at March 31, 2007 and 2006 were 1.28% and 2.73%, respectively.

Weighted average interest rates of commercial paper at March 31, 2007 and 2006 were 0.60% and 0.18%, respectively.

Long-term debt at March 31, 2007 and 2006 consisted of the following:

	Millions of yen	
	2007	2006
0.82% unsecured bonds, due 2009	**¥20,000**	¥20,000
Collateralized loans from government sponsored banks, with interest 1.75%, due through 2012	**1,200**	1,200
Unsecured loans from government sponsored banks, with interest 1.40% (2007), and interest 1.40% (2006), due through 2012	**2,500**	3,000
Collateralized loans from banks and others, payable in foreign currencies, with interest ranging from 4.00% to 6.00% (2007), due through 2012	**358**	
Collateralized loans from banks with:		
Floating interest ranging from 1.02% to 1.21% (2007), and from 0.44% to 0.59% (2006), due through 2010	**8,250**	8,250
Unsecured loans from banks and others, payable in foreign currencies, with interest ranging from 1.59% to 7.0% (2007), and from 1.59% to 5.42% (2006), due through 2009	**34,065**	13,909
Unsecured loans from banks with interest ranging from 0.96% to 6.10% (2007), and from 0.45% to 6.10% (2006), due through 2027	**12,917**	12,949
Total	**79,290**	59,308
Less current portion	**(10,755)**	(3,278)
Long-term debt, less current portion	**¥68,535**	¥56,030

Annual maturities of long-term debt outstanding at March 31, 2007 were as follows:

Years ending March 31,	Millions of yen
2008	¥10,755
2009	9,910
2010	12,155
2011	14,272
2012 and thereafter	32,198
Total	¥79,290

At March 31, 2007, property, plant and equipment, trade accounts receivables, inventories and prepaid expense and other current assets with a book value of ¥49,326 million, ¥10,063 million, ¥6,060 million and ¥2,206 million, respectively, were pledged as collateral for short-term borrowings and long-term debt, and short-term investments with a book value of ¥1,212 million were pledged as collateral for a supplier's borrowings of ¥1,093 million.

Certain loan agreements provide that the lender may require the Group to submit proposals for paying dividends, issuing additional long-term debt and certain other matters for prior approval. As is customary in Japan, security must be given if requested by a lending bank. Banks have the right to offset cash deposited with them against any debt or obligation that becomes due, or, in case of default and certain other specified events, against all other debt payable to them. To date, none of the lenders has ever exercised this right with respect to debt of the Group.

9. Severance Indemnities and Pension Plans

Under the Group's pension plans, employees terminating their employment are, in most circumstances, entitled to pension payments based on their average pay during their employment, length of service and certain other factors.

Based on an agreement between labor and management in March 2006, the Company and certain consolidated subsidiaries implemented a defined benefit pension plan and a defined contribution pension plan effective June 1, 2006, by which time the former qualified defined benefit pension plan was terminated.

The Company and certain consolidated subsidiaries applied accounting treatments specified in the guidance issued by the ASBJ. The effect of this transfer was to increase income before income taxes and minority interests by ¥681 million and was recorded as a gain on partial termination of the defined benefit pension plan in the consolidated statements of income for the year ended March 31, 2007.

The liabilities for employees' retirement benefits at March 31, 2007 and 2006 consisted of the following:

	Millions of yen	
	2007	2006
Projected benefit obligation	**¥74,633**	¥69,681
Fair value of plan assets	**(89,300)**	(67,852)
Unrecognized prior service cost	**250**	400
Unrecognized actuarial loss	**6,819**	6,450
Unrecognized transitional obligation		(3,607)
Net (asset) liability	**(7,598)**	5,072
Prepaid pension cost	**(12,757)**	
Liabilities for retirement benefits	**¥ 5,159**	¥ 5,072

The effect of the transition to the defined contribution pension plan for the year ended March 31, 2007 was as follows:

	Millions of yen
Decrease in projected benefit obligation	¥18,701
Unrecognized prior service cost	118
Unrecognized actuarial loss	(395)
Unrecognized transitional obligation	(837)
Decrease in liability for retirement benefits and increase in prepaid pension cost	¥17,587

The plan assets of ¥16,906 million will be transferred over a period of five years. At March 31, 2007, total plan assets not yet transferred in the amount of ¥13,458 million were presented as other current liabilities and long-term accounts payable.

The components of net periodic benefit costs for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen	
	2007	2006
Service cost	**¥2,703**	¥3,498
Interest cost	**1,347**	1,706
Expected return on plan assets	**(1,696)**	(1,257)
Amortization of prior service cost	**(33)**	(13)
Amortization of transitional obligation	**2,770**	3,607
Recognized actuarial (gain) loss	**(81)**	1,171
Net periodic benefit costs	**5,010**	8,712
Gain on transfer to a defined contribution pension plan	**(681)**	
Contribution to defined contribution pension plan and other	**1,124**	
Total	**¥5,453**	¥8,712

Assumptions used for the years ended March 31, 2007 and 2006 were set forth as follows:

	2007	2006
Discount rate	**Mainly 2.5%**	2.5%
Expected rate of return on plan assets	**Mainly 2.5%**	2.5%
Amortization period of prior service cost	**10 years**	10 years
Recognition period of actuarial gain/loss	**Mainly 10 years**	10 years
Amortization period of transitional obligation	**7 years**	7 years

10. Equity

On and after May 1, 2006, Japanese companies are subject to a new corporate law of Japan (the "Corporate Law"), which reformed and replaced the Commercial Code of Japan (the "Code") with various revisions that are, for the most part, applicable to events or transactions which occur on or after May 1, 2006 and for the fiscal years ending on or after May 1, 2006. The significant changes in the Corporate Law that affect financial and accounting matters are summarized below:

(1) Dividends

Under the Corporate Law, companies can pay dividends at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders' meeting. For companies that meet certain criteria such as: (1) having the Board of Directors, (2) having independent auditors, (3) having the Board of Corporate Auditors, and (4) the term of service of the directors is prescribed as one year rather than two years of normal term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends in kind) if the Company has prescribed so in its articles of incorporation.

The Corporate Law permits companies to distribute dividends-in-kind (non-cash assets) to shareholders subject to a certain limitation and additional requirements.

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the Company so stipulate. The Corporate Law provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

(2) Increases/Decreases and Transfer of Common Stock, Reserve and Surplus

The Corporate Law requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus) depending on the equity account charged upon the payment of such dividends until the total of the aggregate amount of the legal reserve and additional paid-in capital equals 25% of the common stock. Under the Corporate Law, the total amount of additional paid-in capital and legal reserve may be reversed without limitation. The Corporate Law also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts under certain conditions upon resolution of the shareholders.

(3) Treasury Stock and Treasury Stock Acquisition Rights

The Corporate Law also provides for companies to purchase treasury stock and dispose of such treasury stock by resolution of the Board of Directors. The amount of treasury stock purchased cannot exceed the amount available for distribution to the shareholders which is determined by specific formula.

Under the Corporate Law, stock acquisition rights, which were previously presented as a liability, are now presented as a separate component of equity.

The Corporate Law also provides that companies can purchase both treasury stock acquisition rights and treasury stock. Such treasury stock acquisition rights are presented as a separate component of equity or deducted directly from stock acquisition rights.

11. Stock Option

The stock option outstanding for the year ended March 31, 2007 was as follows:

Stock Option	Persons Granted	Number of Options Granted	Date of Grant	Exercise Price	Exercise Period
2000 Stock Option	19 directors 14 employees	93,000 shares	2000.7.25	¥2,471	From July 1, 2002 to June 30, 2006
2001 Stock Option	18 directors 12 employees	92,000 shares	2001.7.30	2,541	From July 1, 2003 to June 30, 2007
2002 Stock Option	20 directors 19 employees	118,000 shares	2002.7.26	2,330	From July 1, 2004 to June 30, 2008
2003 Stock Option	20 directors 19 employees	118,000 shares	2003.7.30	2,405	From July 1, 2005 to June 30, 2009
2004 Stock Option	9 directors 40 employees	144,000 shares	2004.7.27	2,957	From July 1, 2006 to June 30, 2010
2005 Stock Option	9 directors 44 employees	153,000 shares	2005.7.29	2,852	From July 1, 2007 to June 30, 2011
2006 Stock Option	9 directors 44 employees	298,000 shares	2006.7.18	3,790	From July 19, 2008 to July 18, 2012

The stock option activity was as follows:

	2000 Stock Option	2001 Stock Option	2002 Stock Option	2003 Stock Option	2004 Stock Option	2005 Stock Option	2006 Stock Option
				(Shares)			
For the year ended March 31, 2007							
Vested							
March 31, 2006—Outstanding	26,100	47,900	50,000	98,000	144,000	153,000	
Granted							298,000
Exercised	20,900	20,600	29,000	40,000	14,000		
Canceled	5,200			2,000	2,000	2,000	
March 31, 2007—Outstanding		27,300	21,000	56,000	128,000	151,000	298,000
Exercise price	¥2,471	¥2,451	¥2,330	¥2,405	¥2,957	¥2,852	¥3,790
Average stock price at exercise	¥3,655	¥3,690	¥3,892	¥3,780	¥3,811		
Fair value price at grant date							¥ 736

The assumptions used to measure fair value of 2006 Stock Option

Estimate method:	Black-Scholes option pricing model
Volatility of stock price:	30%
Estimated remaining outstanding period:	4 years
Estimated dividend:	¥22 per share
Interest rate with risk free:	1.1%

12. Income Taxes

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 40.6% for the years ended March 31, 2007 and 2006.

The tax effects of significant temporary differences and loss carryforwards which resulted in deferred tax assets and liabilities at March 31, 2007 and 2006 were as follows:

	Millions of yen	
	2007	2006
Deferred tax assets:		
Inventories	**¥ 8,592**	¥ 7,716
Liabilities for retirement benefits	**787**	1,983
Foreign tax credit	**1,634**	1,626
Tax loss carryforwards of consolidated subsidiaries	**1,176**	391
Accrued bonus	**3,478**	2,929
Warranty reserve	**4,967**	2,932
Software and other assets	**7,620**	4,161
Business tax payable	**1,011**	769
Property, plant and equipment	**675**	469
Investment securities	**195**	190
Long-term account payable	**4,302**	229
Other	**9,085**	3,315
Less valuation allowance	**(1,541)**	
Total deferred tax assets	**¥41,981**	¥26,710
Deferred tax liabilities:		
Deferred gains on sales of property	**¥ 2,168**	¥ 2,168
Unrealized gain on available-for-sale securities	**23,104**	22,598
Prepaid pension cost	**5,102**	
Undistributed earnings of consolidated subsidiaries	**10,916**	
Other	**4,882**	3,617
Total deferred tax liabilities	**¥46,172**	¥28,383
Net deferred tax liabilities	**¥ (4,191)**	¥ (1,673)

A reconciliation between the normal effective statutory tax rates and the actual effective tax rates reflected in the accompanying consolidated statements of income for the year ended March 31, 2006 was as follows:

Normal effective statutory income tax rate	40.6%
Permanent non-deductible expenses	3.4
Difference in foreign subsidiaries' tax rates	(6.1)
Tax credit for research and development cost	(2.8)
Losses of consolidated subsidiaries	1.0
Other—net	(0.3)
Actual effective income tax rate	35.8%

A reconciliation of difference between the normal effective statutory tax rates and the actual effective tax rates is not disclosed since the difference is less than 5% of the normal effective statutory income tax rate for the year ended March 31, 2007.

13. Supplemental Cash Flow Information

The Company acquired O.Y.L. Industries Bhd and 92 companies of the subsidiaries of O.Y.L. Industries Bhd for the year ended March 31, 2007.

A reconciliation between assets and liabilities of the subsidiaries at the time of consolidation, cash paid for the capital and payment for acquisition of shares of newly consolidated subsidiaries, net of cash and cash equivalents acquired were as follows:

	Millions of yen
Assets	¥127,712
Goodwill	204,413
Liabilities	(84,339)
Minority interests	(1,724)
Cash paid for the capital	246,062
Cash and cash equivalents of consolidated subsidiaries	(10,376)
Payment for acquisition of shares of newly consolidated subsidiaries, net of cash and cash equivalents acquired	¥235,686

14. Research and Development Costs

Research and development costs were ¥27,204 million and ¥26,648 million for the years ended March 31, 2007 and 2006, respectively.

15. Leases

The Group leases certain computer equipment and other assets.

Lease payments under finance leases were ¥2,333 million and ¥2,283 million for the years ended March 31, 2007 and 2006, respectively.

Pro forma information of leased property under finance leases that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the years ended March 31, 2007 and 2006 was as follows:

	Millions of yen		
For the year ended March 31, 2007	Furniture and Fixtures	Others	Total
Acquisition cost	**¥5,920**	**¥1,897**	**¥7,817**
Accumulated depreciation	**2,862**	**855**	**3,717**
Net leased property	**¥3,058**	**¥1,042**	**¥4,100**

	Millions of yen		
For the year ended March 31, 2006	Furniture and Fixtures	Others	Total
Acquisition cost	¥6,282	¥2,413	¥8,695
Accumulated depreciation	2,798	981	3,779
Net leased property	¥3,484	¥1,432	¥4,916

Obligations under finance leases:

	Millions of yen	
	2007	2006
Due within one year	**¥1,843**	¥2,061
Due after one year	**2,257**	2,855
Total	**¥4,100**	¥4,916

The amount of acquisition cost and obligations under finance leases includes the imputed interest expense portion.

Depreciation expense under finance leases:

	Millions of yen	
	2007	2006
Depreciation expense	**¥2,333**	¥2,283

Depreciation expense, which is not reflected in the accompanying consolidated statements of income, was computed by the straight-line method over the respective lease periods.

The minimum rental commitments under noncancellable operating leases at March 31, 2007 were as follows:

	Millions of yen
Due within one year	¥12
Due after one year	21
Total	¥33

16. Derivatives

The Group enters into mainly various interest rate swap agreements and interest rate options covering certain portions of long-term debt as a means of managing interest rate exposure. The impact on interest expense from these agreements is recognized over the lives of the respective agreements, which are the same as the terms of the related loans.

The Group also enters into foreign exchange forward contracts, currency swaps and currency options to hedge foreign exchange risk associated with certain assets and liabilities denominated in foreign currencies.

In addition, the Group enters into commodity future contracts to hedge the risk of fluctuation of commodity prices for materials.

All derivative transactions are entered into to hedge interest, foreign currency and commodity price exposures incorporated within the Group's business. Accordingly, market risk in these derivatives is basically offset by opposite movements in the value of hedged assets or liabilities. The Group does not enter into derivatives for trading or speculative purposes.

Because the counterparties to these derivatives are limited to major international financial institutions, the Group does not anticipate any losses arising from credit risk.

Derivative transactions entered into by the Group have been made in accordance with internal policies which regulate the authorization and credit limit amount.

Fair Value of Derivative Financial Instruments

The fair values of the Group's derivative financial instruments at March 31, 2007 and 2006 were as follows:

	Millions of yen					
	2007			2006		
	Contract Amount	Fair Value	Unrealized Gain (Loss)	Contract Amount	Fair Value	Unrealized Gain (Loss)
Forward exchange contracts:						
Selling: GBP	**¥ 5,095**	**¥ 5,114**	**¥ (19)**	¥ 3,797	¥ 3,795	¥ 2
EUR	**9,080**	**9,126**	**(46)**	2,856	2,863	(7)
US$	**1,451**	**1,429**	**22**	1,880	1,860	20
ZAR	**1,184**	**1,190**	**(6)**	1,844	1,846	(2)
CZK	**1,505**	**1,502**	**3**	1,830	1,829	1
PLN	**326**	**326**		60	60	
MYR	**1,190**	**1,216**	**(26)**			
AUD	**2,194**	**2,229**	**(35)**			
HKD	**348**	**347**	**1**			
SGD	**70**	**69**	**1**			
Currency swap contracts:						
Receive JPY/Pay HK$	**495**	**(87)**	**(87)**	647	106	106
Total	**¥22,938**	**¥22,461**	**¥(192)**	¥12,914	¥12,359	¥120

	Millions of yen					
	2007			2006		
	Contract Amount	Fair Value	Unrealized Gain (Loss)	Contract Amount	Fair Value	Unrealized Gain (Loss)
Interest rate swap contracts:						
Pay fixed/receive floating				¥7,854	¥205	¥205
Interest rate option contracts:						
Buying				1,542		
Total				¥9,396	¥205	¥205
Commodity futures contracts:						
Metal						
Buying	**¥918**	**¥813**	**¥(105)**			

Information related to derivative contracts that qualify for hedge accounting and forward contracts that are assigned to associated assets and liabilities and recorded on the balance sheets at March 31, 2007 and 2006 are excluded from the disclosure of market value information.

The contract or notional amounts of the derivatives which are shown in the above table do not represent the amounts exchanged by the parties and do not measure the Group's exposure to credit or market risk.

17. Commitments and Contingent Liabilities

Commitments for capital expenditures outstanding at March 31, 2007 totaled approximately ¥7,359 million.

Guarantees of bank loans and items of a similar nature at March 31, 2007 were ¥892 million.

18. Net Income Per Share

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the year ended March 31, 2007 and 2006 were as follows:

	Millions of yen	Thousands of shares	Yen
For the year ended March 31, 2007	Net Income	Weighted Average Shares	EPS
Basic EPS			
Net income available to common shareholders	**¥45,619**	**263,051**	**¥173.42**
Effect of dilutive securities			
Stock options		**122**	
Diluted EPS			
Net income for computation	**¥45,619**	**263,173**	**¥173.34**

	Millions of yen	Thousands of shares	Yen
For the year ended March 31, 2006	Net Income	Weighted Average Shares	EPS
Basic EPS			
Net income available to common shareholders	¥40,599	263,198	¥154.25
Effect of dilutive securities			
Stock options		71	
Diluted EPS			
Net income for computation	¥40,599	263,269	¥154.21

19. Segment Information

Information about operations in different industry segments, foreign operations and sales to foreign customers of the Group for the years ended March 31, 2007 and 2006 was as follows:

(1) Industry Segments

a. Sales and Operating Income

	Millions of yen				
For the year ended March 31, 2007	Air Conditioning	Chemicals	Others	Eliminations and Corporate	Consolidated
Sales to customers	**¥752,560**	**¥116,493**	**¥43,075**		**¥912,128**
Intersegment sales	**615**	**2,516**	**146**	**¥(3,277)**	
Total sales	**753,175**	**119,009**	**43,221**	**(3,277)**	**912,128**
Operating expenses	**685,633**	**106,941**	**41,887**	**(3,272)**	**831,189**
Operating income	**¥ 67,542**	**¥ 12,068**	**¥ 1,334**	**¥ (5)**	**¥ 80,939**

b. Assets, Depreciation and Capital Expenditures

	Millions of yen				
For the year ended March 31, 2007	Air Conditioning	Chemicals	Others	Eliminations and Corporate	Consolidated
Assets	**¥843,867**	**¥146,789**	**¥30,235**	**¥143,684**	**¥1,164,575**
Depreciation	**20,399**	**11,214**	**1,243**		**32,856**
Capital expenditures	**22,169**	**17,631**	**1,335**		**41,135**

a. Sales and Operating Income

For the year ended March 31, 2006	Air Conditioning (Millions of yen)	Chemicals	Others	Eliminations and Corporate	Consolidated
Sales to customers	¥641,657	¥107,411	¥43,789		¥792,857
Intersegment sales	488	3,376	19	¥(3,883)	
Total sales	642,145	110,787	43,808	(3,883)	792,857
Operating expenses	585,035	100,034	44,582	(3,871)	725,780
Operating income (loss)	¥ 57,110	¥ 10,753	¥ (774)	¥ (12)	¥ 67,077

b. Assets, Depreciation and Capital Expenditures

For the year ended March 31, 2006	Air Conditioning (Millions of yen)	Chemicals	Others	Eliminations and Corporate	Consolidated
Assets	¥440,199	¥129,919	¥29,258	¥120,006	¥719,382
Depreciation	16,842	10,273	1,246		28,361
Capital expenditures	33,737	14,402	1,551		49,690

Corporate assets consist principally of the Company's cash, time deposits, short-term investments and investment securities.

The effect of the adoption of the new accounting standard for stock options in Note 2 was to decrease operating income of air conditioning, chemicals and others for the year ended March 31, 2007 by ¥168 million, ¥36 million and ¥14 million, respectively, from such segments in the prior year.

The effect of the adoption of the new accounting treatment for bonuses to directors and corporate auditors in Note 2 was to decrease operating income of air conditioning, chemicals and others for the year ended March 31, 2007 by ¥113 million, ¥25 million and ¥11 million, respectively, from such segments in the prior year.

The effect of the adoption of the new accounting standard for impairment of fixed assets in Note 2 was to decrease corporate assets at March 31, 2007 by ¥796 million.

Notes: Air Conditioning consists of Air Conditioning and Refrigeration Equipment, Electronics, Vacuums and Cryogenics and Medical Equipment.
Chemicals consists of Fluorochemicals.
Others consists of Oil Hydraulics and Defense.

(2) Geographical Segments

The geographical segments of the Group for the years ended March 31, 2007 and 2006 were summarized below:

For the year ended March 31, 2007	Japan (Millions of yen)	Asia and Oceania	Europe	Americas	Other	Eliminations and Corporate	Consolidated
Sales to outside customers	**¥481,745**	**¥154,556**	**¥235,329**	**¥ 36,994**	**¥3,504**		**¥ 912,128**
Interarea transfers	**117,949**	**72,861**	**4,815**	**4,468**		**¥(200,093)**	
Total sales	**599,694**	**227,417**	**240,144**	**41,462**	**3,504**	**(200,093)**	**912,128**
Operating expenses	**564,209**	**206,771**	**213,195**	**42,983**	**3,331**	**(199,300)**	**831,189**
Operating income (loss)	**¥ 35,485**	**¥ 20,646**	**¥ 26,949**	**¥ (1,521)**	**¥ 173**	**¥ (793)**	**¥ 80,939**
Assets	**¥487,765**	**¥371,238**	**¥200,571**	**¥145,564**	**¥5,642**	**¥ (46,205)**	**¥1,164,575**

For the year ended March 31, 2006	Japan (Millions of yen)	Asia and Oceania	Europe	Americas	Other	Eliminations and Corporate	Consolidated
Sales to outside customers	¥465,540	¥116,277	¥174,811	¥33,443	¥2,786		¥792,857
Interarea transfers	96,162	67,279	3,270	3,572		¥(170,283)	
Total sales	561,702	183,556	178,081	37,015	2,786	(170,283)	792,857
Operating expenses	531,342	163,345	165,636	36,704	2,640	(173,887)	725,780
Operating income	¥ 30,360	¥ 20,211	¥ 12,445	¥ 311	¥ 146	¥ 3,604	¥ 67,077
Assets	¥416,261	¥159,943	¥114,812	¥38,703	¥2,491	¥ (12,828)	¥719,382

The above amounts are summarized by geographic area based on the countries where subsidiaries are located.

The effect of the adoption of the new accounting standard for stock options in Note 2 was to decrease operating income of Japan for the year ended March 31, 2007 by ¥219 million.

The effect of the adoption of the new accounting treatment for bonuses to directors and corporate auditors in Note 2 was to decrease operating income of Japan for the year ended March 31, 2007 by ¥151 million.

The effect of the adoption of the new accounting standard for impairment of fixed assets in Note 2 was to decrease assets of Japan at March 31, 2007 by ¥796 million.

(3) Sales to Foreign Customers

Sales to foreign customers for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen	
	2007	2006
Asia and Oceania	**¥180,968**	¥143,310
Europe	**234,988**	178,822
Americas	**43,239**	36,403
Other	**10,280**	8,966
Total sales to foreign customers	**¥469,475**	¥367,501

20. Subsequent Events

(1) New Share Issuance

On May 31, 2007, the Company's Board of Directors authorized the issuance of new shares in the form of a public offering, and the Company issued and publicly offered the 25,500 thousand shares at ¥99,231 million with a payment due date of June 22, 2007. On May 31, 2007, the Board also authorized another issuance of 3,800 thousand shares at ¥14,787 million by allocation to a third party, if necessary, because a secondary offering of the shares by Nomura Securities Co., Ltd. will be implemented through the use of over-allotments. The amount of funds to be raised by this public offering of new shares and a third-party capital increase is to be a maximum of ¥113,318 million and the Company expects to use these funds for repayment of borrowings for acquisition of O.Y.L. Industries Bhd.

(2) Resolutions Approved by the Company's Shareholders at the General Shareholders' Meeting Held on June 28, 2007

a. Appropriations of Retained Earnings

The shareholders approved payment of a year-end cash dividend of ¥14 per share to holders of record at March 31, 2007, totaling ¥3,682 million.

b. Purchase of Treasury Stock

The Company is authorized to repurchase up to 400 thousand shares of the Company's common stock (aggregate amount of ¥2,200 million) as treasury stock until the next general shareholders' meeting.

(3) Stock Option Plan

At the meeting of the Company's Board of Directors held on June 28, 2007, the Company determined the following stock option plan for the Company's directors and key employees:

The plan provides for granting options to directors and key employees to purchase up to 292 thousand shares of the Company's common stock in the period from July 18, 2009 to July 17, 2013. The options will be granted at an exercise price of 105% of the average fair market value of the Company for the last month of the date of option granted.

The Company plans to issue acquired treasury stock upon exercise of the stock options.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of Daikin Industries, Ltd.:

We have audited the accompanying consolidated balance sheets of Daikin Industries, Ltd. (the "Company") and consolidated subsidiaries (the "Group") as of March 31, 2007 and 2006, and the related consolidated statements of income, changes in equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Daikin Industries, Ltd. and consolidated subsidiaries as of March 31, 2007 and 2006, 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.

As discussed in Note 20 to the consolidated financial statements, on May 31, 2007, the Company's Board of Directors authorized the issuance of new shares in the form of public offering and allocation to a third party, the Company issued and publicly offered the new shares with a payment due date of June 22, 2007.

Deloitte Touche Tohmatsu

June 28, 2007

Member of
Deloitte Touche Tohmatsu

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Printed on 100% recycled paper with vegetable ink by waterless printing
Printed in Japan

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CC-A2A (07-09-008) IB