# Annual Report 2009

Fiscal Year Ended March 31, 2009

DAIKIN INDUSTRIES, LTD.

# Profile



Founded in 1924, Daikin Industries, Ltd., has grown to become a leading manufacturer of air-conditioning systems and fluorochemical products. Today, as the world has become a single global market characterized by megacompetition, we are continuing to address new challenges as we move ahead toward our goal of attaining the global No. 1 position as a comprehensive air-conditioning and refrigeration manufacturer.

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.

To maximize our corporate value as a “global and excellent company,” we finalized our numerical performance targets for the FUSION 10 strategic management plan (ending fiscal 2011). This plan gives top priority to proactively contributing to the resolution of global environmental problems while concurrently expanding the scale of business operations, and we are currently moving ahead with diverse measures designed to attain this objective.

## Contents



## 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.

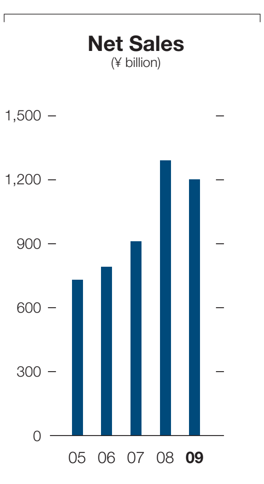
# Financial Highlights

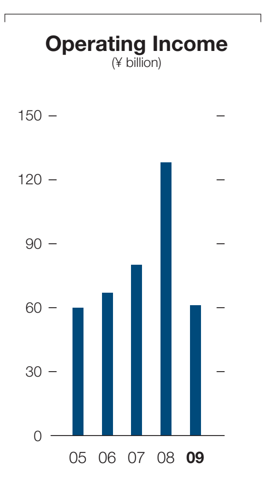
Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31

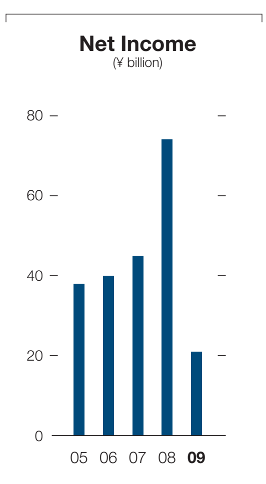
| | Millions of yen | | |
|---|---|---|---|
| | **2009** | 2008 | 2007 |
| **For the Year:** | | | |
| Net sales | **¥1,202,420** | ¥1,291,081 | ¥ 911,749 |
| Operating income | **61,394** | 128,098 | 80,754 |
| Net income | **21,755** | 74,822 | 45,420 |
| ROE (%) | **4.3** | 15.9 | 12.3 |
| **At Year-End:** | | | |
| Total assets | **1,117,418** | 1,210,094 | 1,161,364 |
| Total equity | **484,486** | 559,987 | 409,952 |

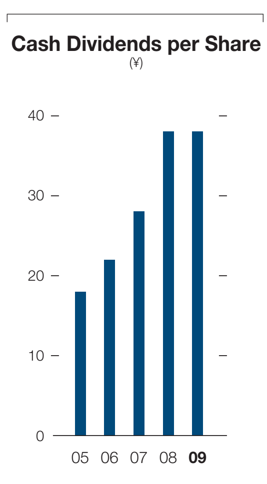
| | Yen | | |
|---|---|---|---|
| | **2009** | 2008 | 2007 |
| **Per Share Data:** | | | |
| Basic net income* | **¥ 74.51** | ¥ 262.24 | ¥ 172.66 |
| Cash dividends applicable to the year | **38.00** | 38.00 | 28.00 |
| Total equity | **1,615.98** | 1,867.79 | 1,511.47 |
| **Stock Information (March 31):** | | | |
| Stock price | **2,680** | 4,290 | 4,100 |
| Market capitalization (Millions of yen) | **785,545** | 1,257,458 | 1,081,637 |

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



## Generating Profit amid an Unprecedented Recession

The financial crisis became increasingly serious in fiscal 2009, ended on March 31, 2009, particularly in the latter half of the year, causing a rapid and severe deterioration of conditions in the global economy. Against this backdrop, the Daikin Group recorded declines in both revenues and profits. Reflecting the considerable negative impact of weakening demand and yen appreciation, our consolidated net sales amounted to ¥1,202,420 million, a decrease of 6.9% from the previous fiscal year. Operating income was down 52.1%, to ¥61,394 million. These drops and a rise in the effective tax rate caused our net income to fall 70.9%, to ¥21,755 million. The rise in the tax rate stemmed largely from the parent company's non-consolidated net loss for the fiscal year, which made it impossible for us to make use of tax deductions and other preferential tax treatment provisions with respect to royalties from overseas subsidiaries, R&D expenditures, and certain other items.

The decrease in demand caused by the recession and progressive yen appreciation had a strong impact on export-oriented industries that had been supporting Japan's economy, causing net losses on the parts of many Tokyo Stock Exchange First Section companies centered on those in the electrical products and industrial machinery fields.

Having established solid presences in Europe, China, and other growing markets around the world, the Daikin Group increased its overseas sales ratio to 64% in fiscal 2008. The considerable size of our overseas operations magnified the impact on our performance from the sharp drop in overseas demand and greater-than-anticipated degree of yen appreciation.

Amid these conditions, the Daikin Group emphasized the expansion of such new businesses as heat-pump room- and water-heating system operations in Europe while also working to thoroughly reduce costs and increase efficiency in manufacturing and marketing operations as well as all other kinds of Group operations. Despite our harsh performance situation in fiscal 2009, however, I am proud to note that the Group was able to quickly respond to the rapid and sharp deterioration of economic conditions throughout the world by modifying its business strategies and that the Group's concerted efforts to implement those strategies enabled it to generate a profit.

## Maintaining a Firm Commitment to "Environmental Fusion"

The Daikin Group is currently working toward the goals of FUSION 10, a strategic management plan covering the five-year period through fiscal 2011. In May 2008, we instituted a medium-term action plan for the last three years of FUSION 10 based on efforts to reexamine all our strategies while emphasizing our "environmental fusion" goal of concurrently sustaining business growth and contributing to the solution of global environmental issues.

Because rapid shifts in the global economy and the deterioration of our operating environment have greatly altered the assumptions we made at the time we drafted FUSION 10, we have reluctantly recognized that we must push back the target dates for attaining the plan's numerical goals. On the other hand, we are not making any changes to our firm commitment to our long-term "environmental fusion" goal, and we are making steady progress in implementing measures designed to facilitate a performance surge when economic conditions improve.

Accelerating the global development of our heat-pump room- and water-heating business is a key strategic objective. Accordingly, in Europe, we rapidly expanded our marketing network through measures including those to acquire a Germany-based company and also introduced a succession of new products. In addition, we launched our heat-pump operations in China and the United States a year ahead of the original schedule.

In line with our goal of promoting broad-spread use of energy-efficient inverter air conditioners worldwide, we are cooperating with China-based Gree Electric Appliances, Inc., to develop inverter room air conditioners that offer both high efficiency and low cost. In the United States, we began operating a state-of-the-art air-conditioning development and testing facility, and we are leveraging our energy conservation- and inverter-related capabilities with respect to large-scale commercial air-conditioning systems as a means of expanding our presence in the applied solutions (commercial) field, which the Daikin Group has not yet sufficiently developed. Through concentrated investments of management resources in strategic initiatives related to the strategic theme of energy conservation, we are striving to bring those initiatives to fruition more quickly than originally planned.

## "Creative Destruction and Innovation" to Promote a Surge of Daikin Group Development

The current recession is quite different from previous recessions, and we are highly conscious that it will be impossible to overcome the associated challenges if we depend on conventional concepts alone. With the outlook highly uncertain, we must quickly gain a grasp of situations that require immediate attention, accurately make the right judgments on how to address those situations, and then implement our strategic measures with unprecedented speed. I believe that our ability to perform these processes repeatedly will be vital to our success in this difficult environment.

At the beginning of 2009, I announced that the Daikin Group's central strategic theme would be "creative destruction and innovation." Accordingly, the Group's officers and employees are implementing their jobs while giving due attention to the following three goals.

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1. **Maintain a thorough emphasis on generating short-term earnings while leveraging the Group's overall strengths to address new challenges.**
2. **Accelerate efforts to produce results from growth strategies offering abundant opportunities (such as strategies for strengthening operations related to environment-friendly products, business in NIC markets, and maintenance and other services that now offer opportunities due to the recession).**
3. **Make the Daikin Group more agile and flexible so it can adapt rapidly to changes in market environments.**

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While striving to achieve these goals, the Daikin Group will unstintingly draw on the strengths of its distinctive corporate culture, which gives it outstanding capabilities for executing strategic measures, conscientiously thorough attention to details, a dynamic eagerness for new challenges, and an elemental resilience and robustness. In these ways, we aim to be a step ahead of other companies in quickly moving forward with measures to launch a new surge of business development when economic conditions begin improving.

As Daikin implements these strategies, I hope for the continued support and encouragement of shareholders.

June 26, 2009

Noriyuki Inoue

Noriyuki Inoue
Chairman of the Board and CEO

**Yukiyoshi Okano**
President and COO,
Member of the Board

## Q: How do you view Daikin's performance in the fiscal year that ended on March 31, 2009?

**Okano:** The global economic recession made fiscal 2009 a very difficult period. The financial crisis and its impact on the real economy caused recessions in the United States, Europe, Japan, and other industrialized countries. Even the economic growth in China and other emerging countries slowed as external demand weakened.

We did everything possible in order to overcome these challenges. Cost-reduction campaigns targeted both operating expenses and fixed costs. At the same time, we took steps aimed at increasing sales, such as the full-scale launch of heating system sales in Europe. Unfortunately, the benefits of these measures were unable to offset rapid deterioration in our operating environment in the fiscal year's second half. We had to cope with a sharp economic downturn, a stronger yen, more costly raw materials, and a lower capacity utilization rate at our factories. The combination of these negative factors resulted in decreases in consolidated sales and earnings from the previous fiscal year.

On the positive side, we succeeded in posting operating income, ordinary income, and net income for the fiscal year. I believe this is proof of the effectiveness of the actions we took in response to the economic recession. Many Japanese manufacturers of electrical and industrial machinery that are listed on the First Section of the Tokyo Stock Exchange reported losses for the past fiscal year.

Even amid the adversity of the past fiscal year, Daikin had a number of significant achievements. In Europe, the sales volume of heat-pump heating systems more than tripled. In Japan, the sales volume of room air conditioners that conserve energy while improving comfort increased. Leading this growth was our high-performance URURU & SALALA (R-series) air-conditioning systems that conform to 2010 energy conservation standards. We also recorded a year-on-year increase in the sales volume of our variable refrigerant volume (VRV) multiple air-conditioning systems for office buildings. One reason was the popularity of our Ve-up Q multiple air-conditioning system for office buildings, which uses existing piping so that an air-conditioning system can be replaced faster. The Hotto Eco Building Multi (Hotto Eko Biru Maru), a multiple air-conditioning system, also contributed to VRV sales growth.

## Q: What are Daikin's strategies for overcoming the challenges created by the worldwide recession?

**Okano:** The global economy contracted in 2009 for the first time in the postwar era. Some people think the economic decline may be near the end, but I think that our business climate will remain difficult for some time. There are still many sources of concern about the economic outlook. In the United States, for example, automakers are restructuring operations and households are struggling with the aftermath of excessive borrowing. In fact, I think there is still a significant risk of an even deeper economic downturn.

Our highest priority in fiscal 2010 is generating short-term profits. After a lengthy series of discussions about how to accomplish this goal, we came up with a list of 49 themes. We have named individuals in charge of each theme and established numerical goals and deadlines for achieving the required improvements. Many initiatives are now under way in order to reach our objectives.

Holding sales steady even as demand falls is one of our most important goals. The only way to do this is by heightening our position in our industry in order to raise our market share. We will develop distinctive products even faster. For our current products, we are enlarging sales networks. Furthermore, our sales, development, production, logistics, and service operations are closely cooperating to put our customers first in every way. Our aim is to transform higher customer satisfaction directly into sales growth.

We foresee solid demand for environmentally responsible products even during this recession. To target this demand, we are working hard to develop more energy-efficient air-conditioning products and increase sales of these products.

The entire Daikin Group is moving faster to cut all expenses. We have a more flexible procurement system for materials and parts to reflect changes in foreign exchange rates. We are making the Group's administrative departments more efficient. We are consolidating tasks outsourced to other companies and starting to perform many of these tasks ourselves. For our workforce, we are using a strategic deployment system for higher productivity. As we cut costs, we must concurrently lower inventories from the standpoint of increasing cash flows.

New investments will be tightly focused on strategic R&D programs and capital expenditures. All other investments will be suspended or canceled. But we must avoid the tendency to adopt an excessively negative stance in response to the global recession. At some point, the economy will start recovering. The Daikin Group must channel a significant amount of resources to building a foundation for growing more and faster than our competitors do once market conditions improve.

Global economic weakness may produce a further decline in demand that exceeds our expectations. We must build a framework that can remain profitable even if this happens. This is why we have established a contingency plan that includes ¥15 billion in cost reductions. We are prepared to activate this plan at any time if warranted by market conditions.

### Q: You explained that short-term earnings are your top priority. But what are your strategies for achieving growth from a longer-term perspective?

**Okano:** As we concentrate on short-term earnings, we are focusing on carefully selected themes that can contribute to long-term growth. Our aim is to produce benefits as quickly as possible.

In fiscal 2010, we are concentrating on three themes that represent excellent opportunities for long-term growth.

The first theme is the environment. Countries worldwide are stepping up measures to combat global warming. This will probably result in the imposition of even tighter restrictions. In the United States, the Obama administration is increasing emphasis on environmental policies. Global environmental problems represent an opportunity for the Daikin Group to gain worldwide recognition for its outstanding environmental technologies and products. Most significant is our expertise in heat-pump technology and inverter technology for air-conditioning. Both are gaining acceptance worldwide as an effective means of fighting climate change. Taking this expertise to a higher level is vital to our ability to become more competitive. Furthermore, we need to build a global infrastructure for marketing and other activities for creating demand for products using these technologies and increasing sales.

Of course, our environmental commitment extends beyond air-conditioning to include our chemicals business and other operations.

The second theme is emerging markets. Even as the global economy contracts, emerging markets continue to post economic growth, although at a slower pace. Much of this expansion is taking place in the BRIC countries. Population and many other factors indicate that emerging markets have outstanding long-term growth prospects.

To grow along with these markets, we are building and upgrading sales networks faster while quickly developing products that reflect the needs of customers in these regions. Expanding operations in India and Brazil is our first goal. Our plans also include establishing a presence in the Middle East and Russia.

The third theme is maintenance and repair services for air-conditioning systems. This business benefits from the recession as owners of these systems extend replacement cycles. The Daikin Group has many advantages. Most important is the very large installed base of our air-conditioning equipment. Our AIRNET online monitoring service for the diagnosis of air-conditioning problems using the Internet and our global sales and service network are two more valuable advantages. We will take full advantage of these strengths along with our skill in creating proposals that precisely target each customer’s needs. Using these resources will allow us to play an active role in increasing demand for maintenance and repair services and capturing orders.

### Q: Please outline major acquisitions and alliances during the past fiscal year. In addition, please tell us about progress in capturing synergies from the acquisition of O.Y.L. Industries Bhd (OYL) in 2006.

**Okano:** In October 2008, we acquired Rotex Heating Systems GmbH of Germany. The Daikin Group is well-known in Europe as a supplier of heat-pump heating systems. Rotex has a powerful sales network in Germany, Italy, France, and other countries for residential heating systems along with extensive know-how in this field. Rotex manufactures and sells highly efficient condensing boilers, floor-heating systems, solar water heaters, and other products. With this acquisition, we enlarged our lineup of environmentally friendly heaters and hot water heaters. Our sales network is much larger, too. We plan to use these resources to grow even faster in the residential heating market in Europe.

In China, we used our agreement with Gree Electric Appliances, Inc., of Zhuhai to outsource the production of 500,000 small inverter air conditioners in 2009 for sale in Japan.

In February 2009, Daikin and Gree Electric Appliances agreed to establish two joint ventures. One company (Zhuhai Gree Daikin Device Co., Ltd.) will produce such key components as compressors and electrical parts that are developed for inverter air conditioners. This will be vital to making these air conditioners more popular worldwide. We are supplying technologies so that production can start soon. Components made by this joint venture will be used at Daikin Group factories around the world.

The second joint venture (Zhuhai Gree Daikin Precision Mold Co., Ltd.) will manufacture molds. Gree Electric Appliances has a high level of internal mold design and fabrication capabilities. Combining that company's expertise with our own knowledge in this field will allow making molds faster while improving quality and lowering costs.

We plan to cooperate with this partner in other ways, too. Daikin and Gree Electric Appliances are considering the joint development of lower-priced inverter air conditioners. The joint procurement of raw materials and parts is another potential area of collaboration.

Turning to OYL, I can report that synergies from this acquisition are already contributing to our earnings. OYL has a very competitive cost structure. This allows us to quickly target demand in emerging economies and expand sales in markets for lower-priced air conditioners. Following the acquisition, McQuay International, OYL's U.S. subsidiary, established the Daikin McQuay Applied Development Center. We upgraded this center in May 2009 with the installation of a sophisticated development and testing facility that can replicate a broad range of weather conditions. Integrating McQuay's skills in commercial (applied) air-conditioning technologies with our energy-conservation technologies creates a powerful platform for developing products with a low environmental profile. I want to distribute these products worldwide to make the Daikin Group very competitive in the commercial air-conditioning market.

One more highlight of fiscal 2009 is growth in sales of both VRV and commercial air-conditioning systems in the United States. I am especially proud of the selection of Daikin Group member McQuay International to supply the HVAC systems for the Freedom Tower in New York City, which will be completed in 2011 at the site of the World Trade Center. Higher U.S. sales demonstrate the recognition that our energy-conservation technologies have earned. I look forward to building on these accomplishments to continue growing in the United States.

## Q: Would you tell us about the problem involving inappropriate accounting procedures and how Daikin has responded to this issue?

**Okano:** In March 2009, an internal investigation revealed that the After Sales Service Division of Daikin and subsidiary Daikin Facilities Co., Ltd. (DFC), had been using inappropriate accounting procedures starting with the fiscal year that ended in March 31, 2000, and ending with the third quarter of the fiscal year that ended March 31, 2008. This had a cumulative effect on sales of about ¥4,015 million. I deeply regret the confusion this incident caused for shareholders and other stakeholders.

On April 10, I established a committee to investigate this incident. The Investigation Committee was chaired by an attorney from outside the Daikin Group and included a certified public accountant and other members, including me. The committee confirmed the facts involving the incident by conducting interviews and checking accounting records and other documents. Through these activities, we determined the amount of money involved, personal accountability, and the reason that this practice went undiscovered for so many years. Committee members also discussed preventive measures. The investigation report was submitted to the Board of Directors on April 30, and a press release concerning this incident was issued.

Our investigation revealed that the problem originated in 1999 when the director in charge of after-sales service placed excessive pressure on subordinates to reach performance targets. To reach these targets, the After Sales Service Division and DFC recorded some projects that were uncompleted at the end of the fiscal year as net sales. In other cases, employees recorded as work in process (inventories) at the end of the fiscal year work for which all or most steps were to take place in the following fiscal year. Other improper measures were used to lower the cost of sales. As a result, financial data for a particular fiscal year included sales and gross profit that belonged in the following fiscal year.

The director in charge of after-sales service as well as several other managers supervised by this director were found to have engaged in inappropriate accounting procedures. However, there was no involvement by any other directors or units of the Daikin Group.

The Investigation Committee identified the causes of the problem and the reasons that no one discovered the problem for 10 years. This information was then used to determine preventive measures designed to be certain a similar incident never happens again. We are currently putting these measures into place.

There are four measures in the After Sales Service Division: a double check for all business operations; a stricter procedure for checking financial data; a reexamination of budget preparation and management processes; and more sophisticated controls for IT systems. Preventive measures for the entire Group cover 11 themes. Major initiatives include more-thorough checking by using cooperation between corporate departments and business units; upgrading the financial reporting process; reinforcing monitoring systems; and expanding internal controls, compliance training, and guidance programs.

Due to this incident, we have revised our financial statements for each fiscal year in the five-year period ending March 31, 2009, along with all interim and quarterly statements during this period. Revised financial information was announced in a press release dated May 8, 2009.

Individuals who engaged in this inappropriate accounting were severely punished in accordance with our internal regulations.

I regard this incident as an issue of the utmost seriousness. The entire Daikin management team is dedicated to restoring the public's trust in the Daikin Group by preventing this type of incident from happening again.

## Q. What is your outlook for Daikin's performance in the fiscal year ending in March 2010?

**Okano:** I do not expect to see a global economic recovery in the near future even though many countries have enacted economic stimulus programs. As I explained earlier, I think our operating environment will remain challenging because of the drop in all categories of demand. To succeed, we will use "Creative Challenge and Change" as the central theme for the Daikin Group this year. That means we must abandon our past behavior and mind-set.

Everyone must accept the challenge of transforming Daikin into an organization with the speed and agility to adapt to rapid changes in our markets.

Our chemicals business recorded a loss in fiscal 2009. Achieving a recovery will be difficult because the performance of this business is closely linked to the U.S. economy. We will continue to concentrate on structural reforms. Goals include cutting annual costs by ¥5 billion, eliminating ¥9 billion of fixed expenses, and improving productivity through moves that include shifting workers to other business units. New investments for chemicals have been dramatically reduced. In addition, we are strengthening product development as well as our manufacturing and sales capabilities.

Although we are taking the actions I just outlined to increase our earnings, we forecast an 11% decrease in consolidated net sales, to ¥1,070 billion, a 35% decrease in operating income, to ¥40 billion, a 35% decrease in ordinary income, to ¥34 billion, and a 45% decrease in net income, to ¥12 billion.

## Q. What is your position regarding the distribution of earnings to shareholders?

**Okano:** I believe that increasing our corporate value through growth in sales and earnings is the best way to meet the expectations of shareholders and other stakeholders. This is why we manage our operations with the goal of increasing market capitalization.

Daikin's fundamental policy is to provide returns to shareholders through a combination of dividend payments and capital gains that are produced by growth in market capitalization.

Our current target for dividend payments is to maintain the ratio of cash dividends to net assets (consolidated basis) at 2% or higher. The policy is to pay a stable dividend that takes into consideration our consolidated performance, financial condition, need for funds, and other factors. The dividend per share applicable to fiscal 2009 was unchanged at ¥38, the sum of interim and year-end distributions of ¥19.

In closing, I ask for the continued support and understanding of shareholders as we take the actions I have just outlined.

June 26, 2009

Yukiyoshi Okano

Yukiyoshi Okano
President and COO,
Member of the Board

# By Leveraging Its Superior Technological Power, the Daikin Group Is Providing Comfortable Air while Concurrently Reducing the Burden on the Global Environment

Because air conditioners use more energy than most other consumer products, the air conditioner industry has been attracting considerable attention regarding its contribution to global warming; in fact, it is the consumer product manufacturing industry with the second largest contribution, after that of the automobile industry. While reducing air conditioners' contribution to global warming is a global task, Daikin has diverse energy-conserving technologies—such as heat-pump technologies, inverter technologies, and refrigerant technologies—that are reducing air conditioners' environmental impact and helping preserve the global environment while also giving powerful impetus to the Company's growth.

## Heat Pumps That Reduce $CO_2$ Emissions and Offer Outstanding Energy Efficiency

Noteworthy examples of Daikin's energy-conserving technologies involve heat pumps and technologies for "mobilizing heat."

Because heat-pump systems for heating and hot water supply do not burn fuel, they do not directly generate $CO_2$. Although they require electric power to drive their compressors and other components, they consume extremely little energy, because they simply pump up heat from the air and use it to heat rooms. For example, if an electric space heater uses one unit of electric power to produce one unit of heat energy, a heat pump can leverage the one unit of electric power to provide three to six units of heat energy.

The International Energy Agency (IEA) has reported that the spread of heat pumps could reduce global $CO_2$ emissions by about 8%—almost twice Japan's current $CO_2$ emissions. In terms of automobiles, it corresponds to the annual $CO_2$ emissions of 250 million or more automobiles.

## Large Rise in Sales of Altherma Heat-Pump Systems Tailored to European Needs

About 60% to 80% of the energy consumed by an average European household is used for room- and water-heating purposes.

In view of this, in 2006, Daikin launched its Altherma heat-pump systems, which were specially designed to meet household room- and water-heating requirements in the markets of France, Germany, and Sweden. Besides being able to maintain ample room- and water-heating power even when the outside temperature is below 0°C, these systems can be operated as air conditioners during the summer—which is impossible for fuel-burning heating systems—and they also feature top levels of energy conservation performance. Altherma products have earned a ubiquitously high appraisal since their launch, and fiscal 2009 sales of the products surged to three times the fiscal 2008 level.

Reflecting its position on the leading edge of environmental protection policies, the EU has recently recognized that heat pumps are "renewable energy sources" (RESs) worthy of promotion along with such other RESs as solar, wind, and geothermal energy.

Daikin is continuing to improve its Altherma products. In 2008, the Company began marketing a solar panel kit that can provide from 30% to 70% of the electric power required by Altherma systems. In 2009, we launched such new products as a monobloc (unitary-type) low-temperature warm water tank and a hot water tank.

Aiming to quickly develop and promote the widespread use of new kinds of heat-pump room- and water-heating equipment that harmonizes with European lifestyles and cultures, Daikin has established its European Environment Research Center in Belgium.

## Building on Strong Performance in Japan to Expand Heat-Pump Sales Worldwide

Daikin estimates that annual sales of fuel-burning room- and water-heating systems in Japan, North America, and China are approximately ¥3 trillion, and the Company is working to transform the fuel-burning system markets of those regions into heat-pump system markets.

In Japan, Daikin has been marketing EcoCute natural refrigerant heat-pump water heaters since 2001. In 2008, the Company completed the development of systems with greater room-heating power—such as Hotto Eco Building Multi systems, which are VRV systems for large-scale buildings, and Danzen Heat systems, which are specialized for heating rooms in commercial facilities—and worked to promote the widespread use of these and other heat-pump systems in regions of Japan characterized by relatively cold winter weather. In 2009, we have launched the large-capacity MEGA-Q system, which is designed for medium-to-large-scale facilities, such as hotels and hospitals, and can supply up to 120 tons of hot water daily. Facilities that replace their fuel-burning systems with MEGA-Q systems can expect to roughly halve their annual $CO_2$ emissions.

To promote heat-pump systems in North America, China, and other markets where such systems are still rare, Daikin is developing products suited for the climates and consumer tastes of each market and building marketing routes. Implementation of the Company's plan for developing those markets was begun in May 2009, one year ahead of the original schedule.

## Inverter Technologies Enable Large Reductions in Power Consumption

Another kind of Daikin Group technology making a large contribution toward preventing global warming is inverter technology for continuously changing the AC current frequency of electric power supplied to the AC motor that powers an air conditioner compressor and thereby continuously changing the speed of that motor's operation.

Air conditioners without inverters attain a temperature setting and then stop, periodically starting up when the temperature rises. Repeated starts and stops make the room temperature unstable and also lead to excessive electric power consumption. Replacing a noninverter air conditioner with an inverter model can reduce power consumption by about 30%.

In Japan, the market share of inverter air conditioners has reached almost 100%. This situation, together with benefits from progress in DC motor technology, has boosted the energy efficiency of air conditioners in Japan to roughly three times the level of 20 years ago. However, the market share of inverter air conditioners has reached only 20% in Europe and 7% in China, while such air conditioners are almost completely absent from the North American and South American markets.

## Making Inverter Air Conditioners the Global Standard

In response to these situations, Daikin is developing inverter air conditioners that offer high efficiency and reasonable prices. In March 2009, Daikin created two joint ventures with China-based Gree Electric Appliances to establish systems for manufacturing principal components and molds and dies in China. By combining Daikin's inverter technology with Gree's expertise in procurement and manufacturing, the partners aim to manufacture high-quality inverter air conditioners at a relatively low price. It appears certain that such products will become increasingly popular in China as well as such other important markets as India and Brazil.

In North America, the most popular kind of air-conditioning and heating systems are ducted systems, in which a large heat-source unit sends cold or warm air to multiple locations via ducts. While ducted systems facilitate centralized administration, they reduce their efficiency by sending air to locations that may not be using the air. The VRV systems Daikin has developed use inverters and individual cooling units in individual spaces, and they are attracting considerable attention due to their energy conservation merits. We are promoting the broader-spread use of these systems.

Moreover, in May 2009, Daikin established a leading-edge testing facility within the Daikin McQuay Applied Development Center in the U.S. state of Minnesota. The new facility will accelerate the development of energy-saving large-scale commercial (applied) air-conditioning equipment for the U.S. market, including inverter models, and improve the Group's competitiveness in the global market for applied air-conditioning equipment.

## Commercializing Low-Environmental-Impact Refrigerants

While air-conditioning equipment has conventionally used hydrochlorofluorocarbon (HCFC) refrigerants, the industrialized countries have decided to completely eliminate the use of such refrigerants by 2020. The Daikin Group is transitioning to hydrofluorocarbon (HFC) refrigerants that do not harm the ozone layer, and all the products it markets in Japan and the EU already employ such refrigerants. In China, the Group has been quicker than other companies to create HFC refrigerant versions of VRV systems and market household air conditioner products that employ HFC refrigerants.

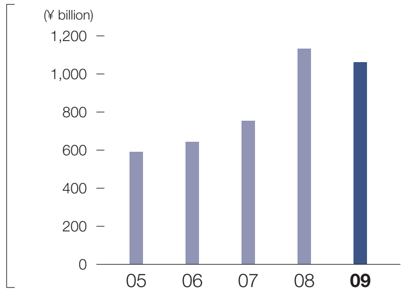
While HFC refrigerants' coefficient of ozone layer damage is zero, the release of these refrigerants into the atmosphere contributes to global warming. In view of this, Daikin has proceeded with R&D programs to create refrigerants with much less greenhouse effect than HFC refrigerants. One example is $CO_2$. At an exhibition held in Germany in October 2008, Daikin announced the world's first VRV air-conditioning system to employ $CO_2$ refrigerant. This system has also been exhibited at events in Spain and France, and it has earned a high appraisal at all three display venues.

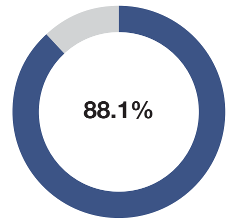
Daikin is working to discover other refrigerants with low coefficients of ozone layer damage and develop equipment that employs such new refrigerants. Since fiscal 2009, the Company has been participating in a refrigerants development project of the New Energy and Industrial Technology Development Organization (NEDO), an independent corporation owned by the Japanese government.

Net Sales

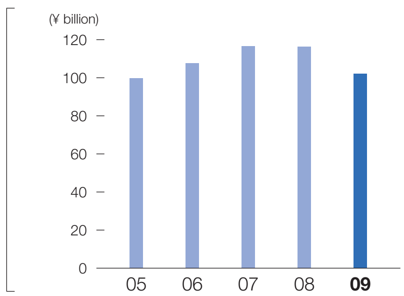
Percentage of Net Sales

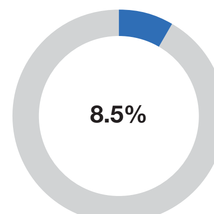
## Air-Conditioning



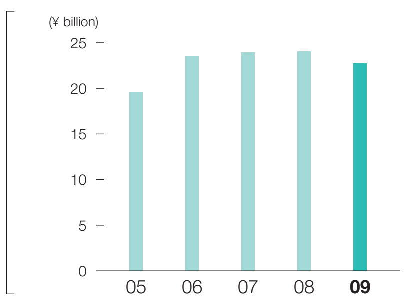



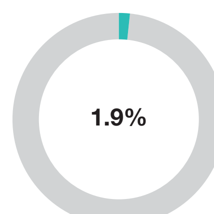

## Chemicals



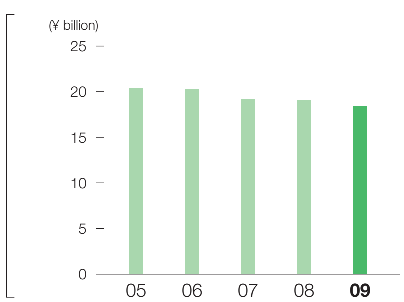



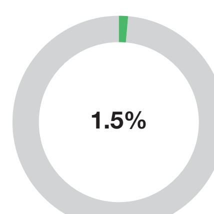

## Oil Hydraulics




## Defense

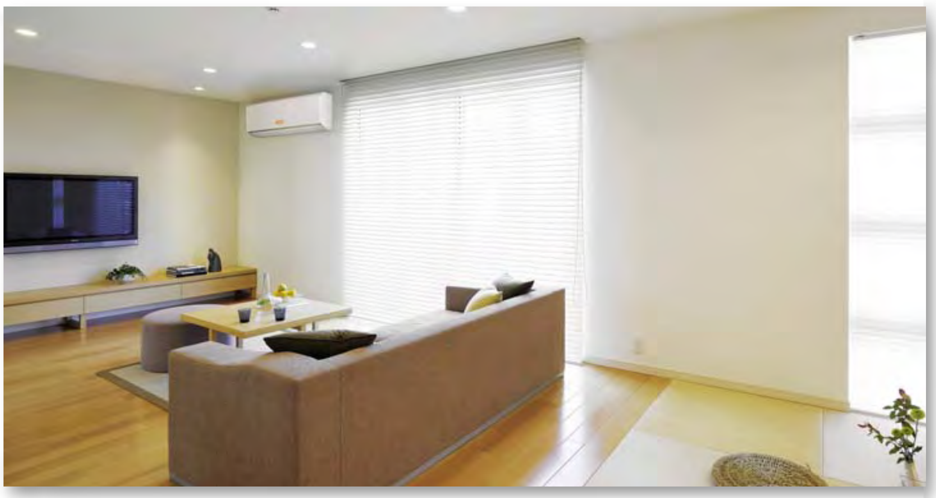


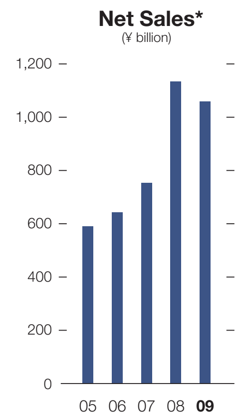



| Major Products & Services | | Description |
|---|---|---|
| • Room air-conditioning systems<br>• Heat-pump hot-water-supply and room-heating systems<br>• Packaged air-conditioning systems<br>• Multiple air-conditioning systems for office buildings<br>• Air-conditioning systems for facilities and plants<br>• Medium- and low-temperature air-conditioning systems | • Absorption refrigerators<br>• Humidity-adjusting external air-processing units<br>• Air purifiers<br>• Water chillers<br>• Air-handling units<br>• Marine-type container refrigeration | 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<br>• Fluoroplastics<br>• Fluoro coatings<br>• Fluoroelastomers<br>• Fluorinated oils<br>• Oil- and water-repellent products<br>• Mold release agents<br>• Pharmaceuticals and intermediates<br>• Semiconductor-etching products<br>• 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. |
| • Oil hydraulic units<br>• Oil hydraulic pumps<br>• Oil hydraulic valves<br>• Cooling equipment and systems<br>• Hydrostatic transmissions<br>• Centralized lubrication units and systems | | Daikin's unique hydraulic technologies offer outstanding energy conservation performance and are contributing to the development of industry by unleashing the potential of power control. |
| • Warheads<br>• Home-use oxygen therapy equipment<br>• Aircraft parts | | Daikin's superior machining and quality control technologies are used in the production of defense-related products and other industries where high levels of precision and performance are critical. |

# Air-Conditioning

## The Japanese Market






* Net sales include domestic air conditioner sales and overseas air conditioner sales.

### Operating Environment and Performance in Fiscal 2009

Japanese demand for residential air-conditioning systems in the first half of fiscal 2009 was above the level in the same period of fiscal 2008, but a drop in demand during the latter half kept demand for fiscal 2009 as a whole approximately unchanged from the fiscal 2008 level.

The Daikin Group launched the high-value-added URURU & SALALA (R-series) room air-conditioning systems, which feature an extremely quiet automatic filter-cleaning function and other special functions and clear the Japanese energy-saving standards to be applied from 2010. These systems offer such additional features as an improved version of Daikin's unique humidifying function, which does not require a water supply; more-advanced energy-saving operating functions; and a panel display to provide information on electric power changes, outside temperature, and energy conservation data.

Throughout fiscal 2009, Daikin's marketing promotion activities emphasized its products' energy conservation performance as well as the comfortable living environments they provide, and the Company was able to realize a year-on-year increase in its residential air-conditioning system sales volume. By effectively leveraging its comprehensive range of marketing, service, and product planning strengths and other capabilities, the Daikin Group maintained a residential air-conditioning system market share of approximately 18%, roughly the same level as in the previous fiscal year.

Regarding the commercial air-conditioning system market, demand during the first half of fiscal 2009 was roughly the same as in the first half of fiscal 2008. However, because the deterioration of economic conditions during the latter half of fiscal 2009 led to capital investment restraint and sluggishness in new construction starts, demand during fiscal 2009 as a whole was down from the previous fiscal year.

Daikin was able to increase its sales of such environment-friendly products as the Hotto Eco Building Multi, a highly efficient multiple air-conditioning system that meets the needs for energy-conserving operation and pleasant heating functions even in particularly cold regions. In December 2008, we launched our MEGA-Q large-scale commercial-use heat-pump systems, which can supply up to 120 tons of hot water daily and reduce $CO_2$ emissions to far below those of comparable fuel-burning systems. MEGA-Q systems also offer backup operating functions for use during breakdowns or inspections and are more compact than previous systems.

Daikin's share of Japan's commercial air-conditioning system market declined slightly but remained over 40%.

Daikin's domestic sales of air-conditioning systems amounted to ¥370.7 billion, approximately unchanged from the previous fiscal year.

## Thorough Measures to Increase Market Share and Generate Profit

The Group is seeking to increase its market share through a marketing promotion campaign tightly focused on environment-friendly and energy-conserving products.

Daikin's strategies for generating profits include new measures to reduce costs by consigning certain manufacturing processes to China-based Gree Electric Appliances. Another strategy is to generate profits by placing greater emphasis on the marketing of such high-value-added products as those in the DESICA commercial-use humidity adjustment air conditioner line, which can humidify and dehumidify without being connected to water pipes, and the Clear Force household humidifier/dehumidifier/air purifier line.

## Leveraging Strengths in the Commercial Air-Conditioning Field despite the Recession

The Daikin Group has a huge stock of equipment installed at customers' facilities and is now leveraging this stock to expand its service and maintenance business. In addition, having long provided 24-hour remote monitoring services, Daikin launched the Air Net II Service System in June 2008. This new service meets the needs of small and medium-sized building owners who want to reduce the energy consumption of their air-conditioning systems to comply with energy-conservation regulations. Besides providing warnings and notifications about air-conditioning equipment malfunctions, along with proposals on appropriate maintenance measures, the system offers such features as those enabling remote control of optimal energy-conserving equipment operation. Another service, provided mainly to owners and managers of multiple stores or offices, is the DAIKIN Direct service, which allows remote, unified monitoring and administration of air-conditioning units in multiple store or office locations via the Internet, as a means of promoting energy conservation.

Daikin plans to supplement its lineup of such systems as the Hotto Eco Building Multi and MEGA-Q large-scale commercial-use heat-pump systems with the fiscal 2010 launch of Danzen Heat—the world's first heat-pump-type heater designed specifically for use in stores and other commercial facilities. Plans call for Daikin to complete the establishment of full-scale heating product operations through the launch of this and other highly differentiated products.

# Air-Conditioning

## The Global Market

### Operating Environment and Performance in Fiscal 2009

During fiscal 2009, Daikin's global air-conditioning operations faced drops in demand in principal Western European markets that led to year-on-year declines in the Group's sales volume and net sales. However, Daikin worked to increase its Western European market share; expand sales in central Europe, Eastern Europe, Russia, the Middle East, and other new markets; and augment operations in such new product fields as heat-pump heating systems and large-scale commercial (applied) air-conditioning systems.

Daikin was able to more than triple its sales volume of heat-pump-type room- and water-heating systems in Europe and strengthen its foundation for future business growth through such measures as the October 2008 acquisition of a Germany-based manufacturer of heating equipment, Rotex Heating Systems, which considerably expanded the Group's marketing network.

In China, Daikin increased its unit sales volume and net sales of residential and commercial air-conditioning systems to levels higher than those in fiscal 2008. This reflects the Group's expansion of its marketing network into outlying regions as well as the Group's strength in multiple air-conditioning systems and efforts to expand the scope of its meticulous marketing campaigns for such systems for applications ranging from office buildings to residences.

In the United States, Daikin was able to record residential air-conditioning system unit sales volume almost equal to the fiscal 2008 level and commercial air-conditioning system unit sales volume exceeding the fiscal 2008 level. In addition, McQuay International obtained an order for applied air-conditioning systems for the Freedom Tower, which is to be built on the former site of the World Trade Center in New York City. This order reflects the fact that the Daikin Group's outstanding energy conservation technologies have earned recognition in the United States, and the Group's participation in this symbolic project is expected to facilitate a further increase in Daikin's name recognition as well as the expansion of the Daikin Group's business in the United States.

In Southeast Asia and Oceania, the unit sales volume in Australia was depressed to below the fiscal 2008 level owing to an economic recession, but the unit sales volume was up in Thailand and Malaysia. Moreover, Daikin Airconditioning Korea Co., Ltd., was established in July 2008 to augment marketing capabilities in South Korea.

Daikin Group efforts to strengthen and develop its marketing companies in NICs supported a year-on-year rise in sales in central Europe, Eastern Europe, the Middle East, and India.

As a result, consolidated net sales in the overseas air-conditioning business segment amounted to ¥688.7 billion, 9% below the level in fiscal 2008.

### Chinese Business Development Helping Daikin Become the Global No. 1 Air-Conditioning Company

The Group is proactively working to address Chinese demand by creating specialized teams to focus on needs for building-use multiple air-conditioning systems and large-scale commercial (applied) air-conditioning systems associated with public-sector investments.

The sharpest rates of market growth in China are progressively shifting from large coastal cities to inland

regions, and Daikin's efforts to expand its marketing coverage to China in its entirety are an additional factor propelling the expansion of the Group's business in China.

Moreover, because it is assumed that China will strengthen its energy-conservation regulations, Daikin is expanding the application of its outstanding inverter technologies. Regarding room air conditioners, Daikin and Gree Electric Appliances established two joint ventures to provide energy-conserving technologies at competitive prices. By supplying inverter air conditioners to a broader range of customers, Daikin is aiming to expand the overall market for such products and pioneer the global air conditioner industry's response to environmental issues.

Another part of Daikin's strategy for becoming the global No. 1 air-conditioning company is the development of the heating business in China. Daikin has accelerated by one year its plans for the introduction in China of the heating products that are enabling successful business development in Europe. Plans call for beginning the local manufacture of such products in August 2009.

## Aiming for Surges in European Heating Business and U.S. Applied Business

While harsh conditions in the European and U.S. markets are expected to persist during fiscal 2010, Daikin is aiming to quickly double its heating business sales volume and net sales compared with the fiscal 2009 level.

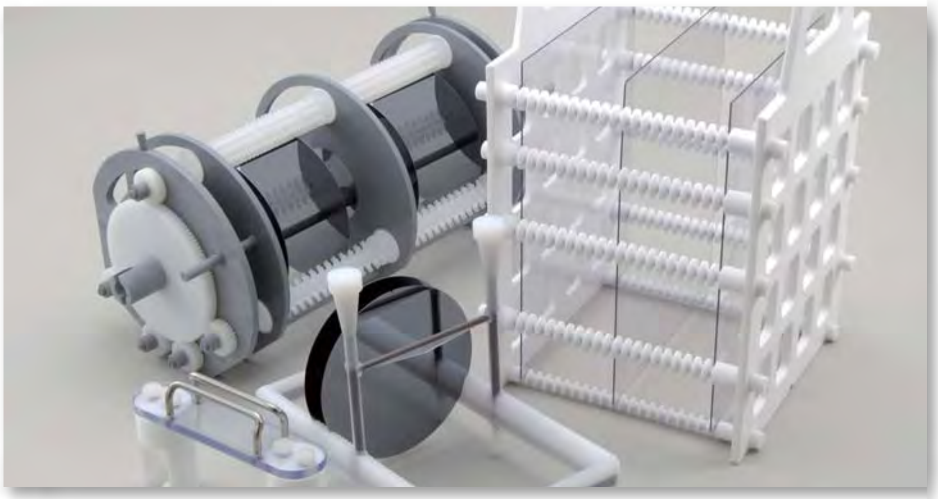
The EU's recent recognition that heat pumps are RESs and other factors are focusing increased European attention on the energy efficiency of heat pumps, and the transition from fuel-burning heating equipment to heat pumps is expected to accelerate. In view of this, Daikin has strengthened its lineup of heat-pump room- and water-heating system products with such new products as an easy-to-install low-temperature monobloc water tank launched in March 2009 and a high-temperature monobloc water tank launched in July 2009. Moreover, Daikin is strengthening its European room-heating business by establishing specialized room-heating product marketing agencies in Germany, the United Kingdom, Belgium, and other countries.

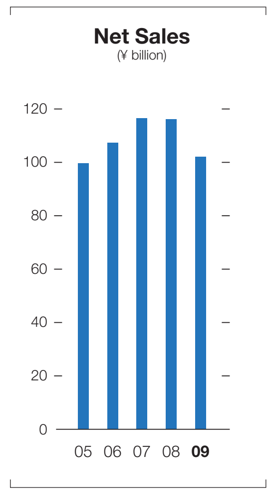
Just as in China, Daikin is accelerating its plans to begin marketing heat-pump room-heating equipment in the United States ahead of the schedule in its original plan.

On the other hand, U.S. demand for applied air-conditioning systems is expected to drop by a large margin during fiscal 2010. In response, Daikin is working to achieve cost cuts through the reduction of fixed costs and internalization of additional business processes. At the same time, Daikin intends to strategically employ the applied air-conditioning systems business base it has strengthened through synergies with McQuay International. This base now features a powerful service system, expanded marketing channels, and other features that Daikin aims to leverage as it emphasizes the objective of increasing market share and boosting the profitability of its applied air-conditioning systems business.

The Daikin McQuay Applied Development Center, which is responsible for developing highly environment-friendly applied air-conditioning products, has recently been equipped with a leading-edge testing facility that can replicate diverse climate conditions found in various parts of the world, and this facility is expected to enable the center to create numerous outstanding products. As the U.S. government transforms its policies regarding global warming, the Daikin Group is preparing for a surge of business development.

# Chemicals






## Operating Environment and Performance in Fiscal 2009

In fiscal 2009, Daikin's chemicals business was greatly affected by the worldwide economic recession.

Regarding the fluorochemicals sector, Daikin's sales to China and Europe for applications related to the U.S. LAN cable market during the first half of fiscal 2009 increased to above the level in the first half of fiscal 2008. During the latter half of fiscal 2009, however, demand for semiconductor and automobile applications plunged, depressing Daikin's sales to below the level in the same period of the previous fiscal year.

In the chemical products sector, Daikin recorded a robust performance with respect to sales of water and oil repellents to China and other Asian markets and sales of liquid crystal related fine chemical products. On the other hand, demand for water and oil repellents and semiconductor-etching products decreased in Japan, the United States, and Europe, depressing the Group's sales in this sector to below the fiscal 2008 level.

In the fluorocarbon gases sector, the steady strength of sales in Asia helped sales rise to above the fiscal 2008 level.

Total consolidated sales in Daikin's chemicals business declined 12% from the previous year, to ¥101.9 billion, reflecting a sharp drop in demand as well as such factors as inventory adjustments and other business reform measures implemented to improve the soundness of chemicals operations.

While the chemicals business is a major pillar of the Daikin Group's profitability, it unfortunately recorded an operating loss for fiscal 2009. Plans call for eliminating losses during fiscal 2010 and subsequently making determined efforts to restore profitability. The Group will do its utmost to resolutely implement drastic business reforms as well as develop new applications and take other measures in line with strategies drafted for each individual product.

## Overcoming Challenges through Focused Expansion Initiatives and Structural Reforms

The principal products of Daikin's chemicals business are highly dependent on demand related to automobiles, semiconductors, and housing construction. From a geographical perspective, the United States accounts for a large share of demand for the products. In view of these points, it is assumed that the operating environment will continue to be harsh until the U.S. economy musters a full-scale recovery and the automobile, semiconductor, and housing construction industries regain their dynamism. To help compensate for this, the Group intends to develop additional automotive and semiconductor applications for such principal products as fluoropolymer resins, fluoroelastomers, and water and oil repellents. From a geographical perspective, plans call for achieving a large-scale increase in sales in China, which is projected to sustain its economic growth.

In addition, Daikin is organizing teams of R&D, manufacturing, and marketing staff to investigate business development in fields with relatively great profit and growth potential. These teams have the task of clarifying strategic emphases and promoting sales related to those emphases. For example, we have organized teams focused on solar cell films in the energy field, heat-insulation coatings in the environmental field, and additives in the solutions field.

Moreover, Daikin is accelerating the pace of its fundamental reforms to improve the structural soundness of its chemicals businesses as well as the pace of its efforts to develop new product applications related to the environmental protection field.

Regarding the structural reforms, the Group has resolutely moved ahead with measures to cut costs through lowering inventory levels and large-scale reduction of fixed costs. With an eye to stepping up the development of new applications, we are promoting the building of close direct relationships between our R&D staff and customers and expect to transform our organization into one that engages in product development operations that respond to diverse needs. By giving units comprehensive responsibility for all processes from R&D through marketing, we anticipate that our organization will generate one new material after another in response to society's changing needs.

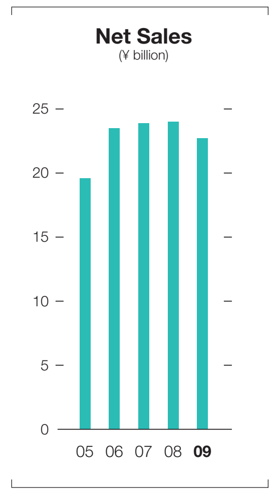
Daikin is continuing to promote composite product development in fluorochemicals and other materials sectors, which are aiming to expand the scope of their operations. We have already successfully commercialized Unidyne™ TG-5521, a fluorochemicals/silicone composite fabric treatment developed in collaboration with U.S.-based Dow Corning Corporation, and developed a water-based fluorinated urethane coating material with superior anti-stain properties and weather resistance in cooperation with Germany-based LANXESS Deutschland GmbH.

## Developing New Applications Centered on Environment-Friendly Applications

Regarding the development of new applications in the environmental protection field, Daikin is establishing businesses related to heat-insulating coatings and new materials for next-generation lithium batteries. The Group is also moving ahead with application development projects related to such leading-edge functional materials as those involving liquid crystals, optically functional materials, semiconductors, information processing and communications, energy, and pharmaceutical intermediates, and this work is expected to elicit new demand.

Particularly in the United States, the increasing rigor of environmental regulations is expected to expand the scope of ethylene tetrafluoroethylene (ETFE, a fluoropolymer resin) use in fuel lines and other applications, and Daikin initiated the marketing of DAI-EL™ FluoroTPV, a newly developed fluorochemical material that features the flexibility to withstand bending and twisting as well as a low level of permeability to hydrocarbons contained in automobile fuel. Use of this material is expected to rise in response to California's Partial-Credit Zero Emission Vehicle (PZEV) regulation, which offers benefits for ultralow-pollution vehicles with low levels of hydrocarbon evaporation.

# Oil Hydraulics




## Operating Environment and Performance in Fiscal 2009

In fiscal 2009, Daikin worked to shift from the marketing of individual products—particularly highly energy efficient hybrid oil hydraulic equipment that integrates motor, inverter, and hydraulic control technologies—toward a new business model that comprehensively meets customer needs by offering proposals and designs for systems centered on hybrid oil hydraulic equipment and then marketing those system packages. In May 2008, we established Osaka-based Daikin Hydraulic Engineering Co., Ltd., to incorporate the various business units required to realize the new business model.

However, sales of industrial machinery related oil hydraulic equipment decreased during fiscal 2009 to below the fiscal 2008 level, mainly reflecting the large production cuts implemented by the machine tool manufacturers that are Daikin's principal customers in this business field. Because an extremely large proportion of certain oil-cooling systems, for which Daikin has a high market share, are installed in conjunction with high-precision processing equipment, sales of such oil-cooling system products were negatively impacted when production cuts for high-precision processing equipment expanded from the start of the latter half of fiscal 2009. Regarding export sales, Daikin was able to achieve a year-on-year increase during the first half of fiscal 2009 by means of sales promotion campaigns for highly differentiated inverter drive hydraulic units (super units) in the molding equipment markets of Taiwan and South Korea, but export sales for the fiscal year as a whole were down due to the impact of the global weakening of market conditions.

Sales of oil hydraulic equipment for construction machinery and motor vehicles were higher than in fiscal 2008, reflecting the benefits of sales promotion campaigns for hydrostatic transmission pumps in the United States, Europe, and other markets throughout the world.

## Marketing Hybrid Oil Hydraulic Package Products Worldwide, Beginning with the United States

In fiscal 2010, the Daikin Group has made environmental countermeasures a medium-to-long-term business theme, and this theme applies to the Group's oil hydraulics operations, which are developing a broad range of industrial applications for its products.

Since 2001, Daikin has emphasized measures to commercialize business in hybrid oil hydraulic package



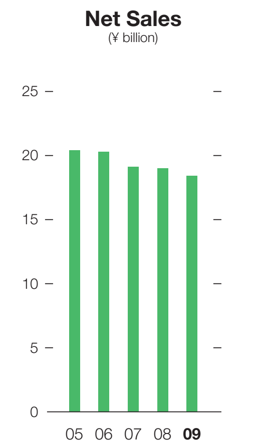
products that integrate hydraulic technologies with motor inverter technologies developed in connection with the air-conditioning business. Because hybrid oil hydraulic package products offer outstanding energy conservation performance and enable the creation of oil hydraulic equipment that contributes to the preservation of the global environment, latent demand for such products is continuing to grow in line with the steady expansion of markets for environment-friendly products that offer considerable benefits regarding the reduction of $CO_2$ emissions.

As Japanese markets are becoming increasingly mature, the Daikin Group has also made the acceleration of global business development a medium-to-long-term business theme. One particularly promising market is the North American after-service market for industrial machinery, including hydraulic equipment, and this field is expected to offer opportunities to create new demand for the Daikin Group's hybrid oil hydraulic equipment. In February 2008, as part of the Group's global strategy for hydraulic operations, Daikin acquired All World Machinery Supply Inc. (AWM), a distributor of hydraulic equipment headquartered in Harvard, Illinois. In addition to having powerful marketing routes in the North American hydraulic equipment market, AWM has developed a strong maintenance repair operation (MRO) customer solution provision business.

Going forward, plans call for steadily developing environmental business, mainly in end-user markets, based on a business differentiation strategy centered on the integration of hybrid oil hydraulic equipment and the MRO business.

Rather than being restricted to operations in Japan and the United States, the Daikin Group intends to continue strengthening its business foundation through measures to promote hybrid oil hydraulic equipment in machine tool and molding equipment markets throughout the world, with particular emphasis on market creation efforts in China and Europe.

# Defense




## Operating Environment and Performance in Fiscal 2009

Daikin's defense business sector includes defense business as well as civil sector business. In fiscal 2009, the Company recorded robust deliveries of ammunition and guided missiles to Japan's Ministry of Defense despite a downtrend in the ministry's budget for those items.

The share of civil sector business in the Group's defense business sector has been rising, and Daikin has continued to make efforts to reinforce this trend.

In home-use oxygen therapy equipment, the Company worked to help improve the quality of life of people with chronic respiratory insufficiency by continuing to develop new oxygen concentration units featuring a comprehensive range of improvements regarding size, weight, functionality, and ease of use.

With respect to commissioned manufacturing business, Daikin is making use of such resources as the precision processing technologies it has developed in the course of its defense business to perform high-quality work. During fiscal 2009, efforts were made related to the processing of molds and dies for next-generation compressors and other strategic objectives.

Defense business departments have been handling the production of EcoCute hot water storage tank units—one of the environment-friendly products on which the Daikin Group places strategic emphasis—on behalf of other Daikin Group departments since fiscal 2007, and the manufacturing volume of these tanks was greatly increased during fiscal 2009.

## Strengthening Civil Sector Business and Exploring New Business Opportunities

In fiscal 2010, plans call for dependably meeting defense business demand while striving to further expand civil sector business operations.

In the field of home-use oxygen therapy equipment, Daikin has large competitive advantages regarding the price and functionality of its respiration synchronizing units, which supply oxygen in accordance with users' respiratory rhythms, and it is emphasizing measures to promote greater sales of these products. With respect to oxygen concentration units, which take in air and raise the concentration of oxygen in that air, the Company has begun marketing new products, aiming to generate high profits by providing products that offer user merits and outstanding, unique characteristics.

In the business of manufacturing EcoCute hot water storage tank units, Daikin is emphasizing the persistent pursuit of still-more-sophisticated welding technologies as a means of differentiating its capabilities from those of competing companies.

In recent years, the Company's defense business departments have worked to develop promising new civil sector businesses, and it is now considering entering the automotive collision-response safety product field, where it can differentiate its capabilities based on explosive device technologies related to ammunition and fuses. Going forward, the departments will continue proactively seeking and rigorously selecting prospective new businesses that offer opportunities to leverage diverse accumulated technologies.

## Management and Corporate Information Section



## Fundamental Corporate Governance Concept

The Daikin Group's corporate governance, in accord with the Group Management Philosophy, is designed to help accelerate decision making and operational execution work in response to changes in management tasks and the surrounding environment while concurrently promoting consistently high levels of management transparency and soundness, thereby seeking to increase the Group's corporate value.

To realize these objectives—rather than adopt a U.S.-style "committees system" that completely separates decision making from operational execution—the Group has adopted an "integrated management" system that calls for directors to bear responsibility for management responsibilities as well as for operational execution responsibilities. In view of the special characteristics of the Group's business, it was judged that the "integrated management" system is a more effective means of accelerating decision making and operational execution. In addition, the Group has created diverse systems to ensure the soundness and transparency of management.

Going forward, the Group will be striving to ensure the increasing sophistication of speedy management, the strengthening of consolidated management, and still-higher levels of soundness and transparency. In addition, to realize an increase in corporate value, the Group will continually consider and reevaluate its concepts regarding the most appropriate forms of corporate governance as it pursues a diverse range of Group-level initiatives aimed at ensuring best practices throughout the Group.

## Systems for Optimizing Management and Execution

Daikin entrusts the CEO with the responsibility for making management decisions, including those involving the overall management of the Group, while it assigns the COO the responsibility for executing operations. This system is used to give due attention to both decision making and operational execution processes while seeking to accelerate both kinds of processes with respect to the increasing breadth and depth of management tasks, including Group management tasks.

To facilitate speedy decision making based on substantive discussions, the Board of Directors has been designed to include a small number of members. As of June 2009, the Board of Directors included 10 members.

Since 2004, Daikin has employed an Executive Officer System to accelerate the speed of execution based on autonomous judgments and decisions in units handling each region, division, and function. In parallel to the Executive Officer System, the Board of Directors is responsible for making speedy strategic decisions and performing sound supervision for the entire Group.

The top deliberative unit in the Group's management system is the Group Steering Meeting, which quickly and in a timely manner determines the Group's strategic direction regarding important management policies and strategies as well as quickly resolving problems.

In addition, the Group Management Meeting aims to unify the Group's decisions by thoroughly sharing important management policies and the basic strategies of the Group and supporting and expediting the Group companies' problem-solving efforts. To further increase the Group's overall corporate value and ensure the Group lives up to its responsibilities to society, the Group Management Meeting provides direction and instruction regarding cooperation among Group companies as well as undertaking coordination measures to promote good communications among those companies. In these ways, the meeting aims to ensure that the Group is characterized by a unified understanding and integrated corporate operations.

## Systems for Increasing Transparency and Soundness

Daikin employs a Board of Corporate Auditors and seeks to nominate two or more outside members—with no relationship of interest with the Company—to both its Board of Directors and its Board of Corporate Auditors. As of June 2009, Daikin's 10 directors included two outside directors, and the Company's four corporate auditors included two outside corporate auditors.

The outside directors are assigned assistants in the Management Planning Office who strive to provide the outside directors with early notice of Board of Directors meetings. In addition, in the case that an outside director is not able to attend a Board of Directors meeting, the assistants provide the outside director with related materials, and the general manager of the Management Planning Office subsequently provides the outside director with an explanation of the proceedings of the meeting, thereby ensuring that the outside directors can effectively contribute to Daikin's corporate governance system.

The outside corporate auditors attend meetings of the Board of Directors as well as sessions of the Executive Officers' Meeting, the Companywide Technology Meeting, and other important meetings and receive reports. In addition, they are able to express diverse opinions.

To ensure effective audit functions, the Board of Corporate Auditors receives reports on important issues impacting management and performance when necessary and also investigates relevant units, confirms approval documents, and regularly exchanges opinions with representative directors, executive officers, and the independent auditors.

To strengthen Groupwide auditing and supervision functions for all Group companies, including overseas subsidiaries, principal Group companies appoint Group auditors. The corporate auditors and Group auditors regularly hold Group Auditors' meetings and otherwise work to increase the smoothness of information flows. In addition, the corporate auditors have established an Auditing Department separate from the Internal Auditing Department, with staff who assist in auditing activities. The staff of the Auditing Department report directly to the corporate auditors and perform their duties in accordance with the corporate auditors' instructions, and such decisions relating to the staff as personnel reassignments and evaluations are made with due deference to the opinions of the Board of Corporate Auditors.

To ensure the transparency of management with respect to corporate officer appointment and compensation, Daikin has established its Personnel and Compensation Advisory Committee, which is chaired by an outside director and conducts deliberations regarding such issues as corporate officer selection standards, corporate officer candidates, and corporate officer remuneration.

## Systems for Supporting the Strengthening of Governance

To further strengthen its corporate governance, Daikin has established committees and systems that support corporate governance processes.

For example, the Corporate Advisors Committee offers advice from an independent perspective regarding diverse kinds of management issues. It meets approximately twice each year.

To strengthen internal controls related to financial reporting, the Company has established the Internal Control Construction Committee, which is chaired by Daikin's president.

The Disclosure Committee confirms the completeness and appropriateness of annual securities reports (*Yuka Shoken Hokokusho*) and diverse other information disclosure media and seeks to upgrade accountability.

Serving as a management regulatory body designed to raise corporate value, the Independent Committee is comprised of highly independent outside directors and advisors. In the event that a party purchases or seeks to purchase a large amount of Daikin shares, the Board of Directors will, based on the Daikin Shareholder Relationship Policy, convene a meeting of the Independent Committee, which has the roles of obtaining information from the stock purchaser, considering whether the purchase would be beneficial to corporate value and shareholders, providing shareholders with information and its fair opinion on this issue, and, thereby, creating an environment that facilitates the making of an appropriate decision. Rather than aiming to help prevent a takeover of Daikin through the issuance of share warrants, allocation of shares, or any other means, the Independent Committee and Daikin Shareholder Relationship Policy are designed to increase the transparency and objectivity of Daikin's processes for dealing with takeover bids.

Daikin's Corporate Ethics & Risk Management Committee constantly works to maintain a grasp of internal and external changes in the corporate ethics and risk situations of each Group company as well as to identify problems regarding which the Group should strengthen its performance and to promote the resolution of those problems.

The CSR Committee was established to determine the direction of the Group's CSR activities as a whole, monitor and supervise the execution of those activities, and take measures to respect and protect the interests of diverse stakeholders other than stockholders.

## Systems Related to Respect for Shareholders

To contribute to shareholder benefits, Daikin has introduced a system that enables shareholders to exercise their voting rights via personal computer or mobile phone. In addition, the Company sends out invitations to its general shareholders' meetings three weeks in advance, or one week before the legally required date.

To upgrade its communications with shareholders and a wide range of other investors, Daikin is proactively implementing IR campaigns. The Company has assigned responsibility for handling IR activities to internal units and staff, and it regularly holds explanation briefings for analysts, institutional investors, and overseas investors. In addition, IR materials are posted on the Company's website.

Regarding other stakeholders, Daikin acts in line with its management philosophy as it works to give due respect for various standpoints and set policies regarding the provision of information. The Daikin Group is energetically engaged in environmental protection programs and other CSR activities, and the nature and results of these activities are publically disclosed in the Group's *CSR Report* as well as being posted on the website.

## Directors, Auditors, and Executive Officers (As of June 26, 2009)

| Position(s) | Name | Responsibilities & Principal Jobs |
|---|---|---|
| Chairman of the Board and CEO | **Noriyuki Inoue** | |
| President and COO | **Yukiyoshi Okano** | Chairman of the CSR Committee, the Corporate Ethics Committee, and the Development Committee for Operational Adequacy Promotion System |
| Outside Director | **Chiyono Terada** | President and CEO of Art Corporation |
| Outside Director | **Kosuke Ikebuchi** | Senior Advisor to the Board and Senior Technical Executive of Toyota Motor Corporation |
| Senior Executive Officer | **Katsuhiko Takagi** | Chairman of the Board and CEO of O.Y.L. Industries Bhd and Chairman of McQuay International, Inc. |
| Director and Senior Executive Officer | **Guntaroh Kawamura** | Responsible for Chemicals Business and General Manager of Yodogawa Plant |
| Director and Senior Executive Officer | **Hiroshi Tanaka** | Responsible for Japan Air-Conditioning Business and Commercial and Industrial Refrigeration Business, General Manager of Air-Conditioning Sales Division, Chairman of the Board (nonmanaging) of Daikin Applied Systems Co., Ltd., and Chairman of the Board (nonmanaging) of Daikin Air Technology Co., Ltd. |
| Director and Senior Executive Officer | **Masanori Togawa** | Responsible for Corporate Communications, Human Resources, General Affairs, and Facilities Operations and General Manager of the Secretariat Office and the Human Resources Division |
| Director and Senior Executive Officer | **Shigeki Hagiwara** | Responsible for Service Operations, General Manager of Air-Conditioning Manufacturing Division, and Chairman of the PD Affiliation Alliance Promotion Committee |
| Director and Senior Executive Officer | **Takeshi Ebisu** | General Manager of the Corporate Planning Department and Member of Technology and Innovation Center Development Department |
| Director and Senior Executive Officer | **Takeshi Matsuzaki** | Responsible for Air-Conditioning/Low-Temperature Technology Management and Global Procurement Business, Deputy General Manager of Air-Conditioning Manufacturing Division, General Manager of Global Procurement Division, and Member of Technology and Innovation Center Development Department |
| Corporate Auditor | **Shinichi Fujita** | |
| Corporate Auditor | **Yutaka Kato** | |
| Outside Corporate Auditor | **Yoshiyuki Kaneda** | Former officer of Sony Corporation |
| Outside Corporate Auditor | **Hitoshi Murakami** | Senior Advisor to Sumitomo Trust & Banking Co., Ltd. |
| Senior Executive Officer | **Osamu Okumura** | Responsible for Electronic System, Corporate Ethics, Legal Affairs, Compliance, and Logistics Operations |
| Senior Executive Officer | **Ken Tayano** | Responsible for China Region Business, President of the Board of Daikin (China) Investment Co., Ltd., and Member of Air-Conditioning Global Committee |
| Senior Executive Officer | **Junichi Sato** | Responsible for Global Air-Conditioning Business (excluding Japan) and Global Sales Strategies for Commercial and Industrial Refrigeration (excluding Japan), General Manager of Global Strategy Division, Member of Global Air-Conditioning Committee, and F.J. Project Leader |
| Senior Executive Officer | **Kunikazu Torikoshi** | Responsible for Technology Fusion Strategies and Technology Alliance and Coordination Business, General Manager of the Technology Innovation Development Department, and General Manager of Sakai Plant |
| Senior Executive Officer | **Yukio Hayashi** | Responsible for Liaison Business and Refrigeration Sales Operations and General Manager of Tokyo Branch |
| Senior Executive Officer | **Kiyohiko Ihara** | Responsible for Chemicals Research/Technology/Environment/Safety and Chemicals Patents, General Manager of Chemical Research & Development Center, Member of Technology and Innovation Center Development Department, and F.J. Project Leader |
| Senior Executive Officer | **Yoshibumi Katayama** | Responsible for Air-Conditioning Applied Business, Member of the Board and Vice President of O.Y.L. Industries Bhd, COO of McQuay International, and AP Project Leader |
| Senior Executive Officer | **Kosei Uematsu** | General Manager of New York Branch, President and Member of the Board of Daikin Holdings (USA), Inc., President and Member of the Board of Daikin U.S. Corporation, and Member of Global Air-Conditioning Committee |
| Senior Executive Officer | **Seiji Ideno** | Responsible for Oil Hydraulics Division |
| Senior Executive Officer | **Hiroo Yoshioka** | Responsible for strengthening Air-Conditioning Overseas Base, Air-Conditioning Manufacturing Technology, and Chemicals Manufacturing Technology, Deputy General Manager of Air-Conditioning Manufacturing Division, and Member of Global Air-Conditioning Committee |
| Senior Executive Officer | **Yasushi Yamada** | Responsible for Safety |
| Executive Officer | **Susumu Okano** | General Manager of Corporate Communication Department and Leader of the Corporate Communication Department's Management IR Group |
| Executive Officer | **Shinya Okada** | Responsible for PL/Quality, Air-Conditioning/Refrigeration QA, CSR/Global Environment, Defense Systems, and Training Business, Deputy General Manager of Air-Conditioning Manufacturing Division, General Manager of Shiga Plant, C.D. Project Leader, N.F. Project Leader, and Member of Technology and Innovation Center Development Department |
| Executive Officer | **Satoru Akama** | Responsible for Air-Conditioning Sales Division |
| Executive Officer | **Masanori Fujikawa** | Responsible for Business Flow Innovation Business, Deputy General Manager of Global Procurement Division, and General Manager of Business Flow Innovation Business |
| Executive Officer | **Koichi Takahashi** | Responsible for Accounting, Finance, and Budget Operations and General Manager of the Finance and Accounting Division |
| Executive Officer | **Katsuyuki Sawai** | General Manager of the Refrigeration Division, Deputy General Manager of Air-Conditioning Manufacturing Division, and T.J. Project Leader |
| Executive Officer | **Masatsugu Minaka** | Responsible for Global Strategy Division's Operations regarding Air-Conditioning Operations in the Europe/Middle East/Africa Region, General Manager of the Düsseldorf Office, President of Daikin Europe N.V., and Member of Air-Conditioning Global Committee |
| Executive Officer | **Toshitaka Tsubouchi** | Director of Daikin Europe N.V. |

## Additional Measures to Promote Thorough Compliance

In March 2009, the Daikin Group discovered that inappropriate accounting processes were being used by certain departments of the parent company and its subsidiaries. Subsequently, measures were rapidly taken to determine the causes of this situation, and other measures were taken to prevent the recurrence of such a situation. Going forward, however, the Daikin Group intends to have all its officers and employees participate in educational courses focused on accounting and internal controls, and the Group will take diverse additional measures to promote thorough compliance performance and prevent the incidence of violations of any relevant laws or regulations.

The Daikin Group's measures for promoting and checking to confirm rigorous compliance performance are as follows.

**Group Compliance Policy**

The Group Compliance Policy articulates the fundamental concepts that each Group company and its officers and employees must comply with in the course of the Daikin Group's global development of corporate activities. As hearings were held at overseas Group companies during fiscal 2009, the Group has been able to draft a unified global compliance policy. Previously, main Group companies* have shared information with the parent company in Japan. Going forward, plans call for giving due consideration to differences between the laws, regulations, and customs of various countries and regions while promoting still-higher levels of compliance and corporate ethics at overseas Group companies.

The Group Compliance Policy covers various situations that occur on a day-to-day basis with respect to the following 15 themes.

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1. Provision of Safe and High-Quality Products, 2. Free Competition and Fair Transactions, 3. Compliance with International Trade-Related Laws and Regulations, 4. Respect for and Maintenance of Intellectual Property, 5. Appropriate Administration and Use of Information, 6. Prohibition of Insider Trading, 7. Timely and Appropriate Disclosure of Corporate Information, 8. Preservation of the Global Environment, 9. Ensuring Safe Operations, 10. Respect for Human Rights and Diversity at Workplaces and Compliance with Labor-Related Laws and Regulations, 11. Protection of Corporate Assets, 12. Appropriate Accounting Methods, 13. Moderation in Entertainment and Gifts, 14. Resolute Resistance to Antisocial Behavior, 15. Compliance with Diverse Industry-Centered Laws.

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** These companies include Daikin Europe N.V.; Daikin America, Inc.; Daikin AC (Americas), Inc.; Daikin Airconditioning (Singapore) Pte Ltd.; Daikin Industries (Thailand) Ltd.; Daikin Australia Pty., Ltd.; Daikin Air-Conditioning (Shanghai) Co., Ltd.; Daikin (China) Investment Co., Ltd.; Daikin Fluorochemicals (China) Co., Ltd.; AAF-McQuay International Inc.; and O.Y.L. Manufacturing Company Sdn. Bhd.*

**Corporate Ethics & Risk Management Committee**

Chaired by the Company's president, this committee is the Company's supreme organizational unit with respect to the maintenance of rigorous corporate ethics—including compliance-related ethics—and risk management. It plays a leading role in solving problems and improving and strengthening systems throughout the Group.

**Law, Compliance & Intellectual Property Center**

In cooperation with the Corporate Ethics & Risk Management Committee, the Law, Compliance & Intellectual Property Center is responsible for activities that promote thorough compliance and other objectives. The center performs legal audits based on the results of self-assessment activities by employees at Group companies.

**Internal Audit Department**

The Internal Audit Department conducts checkups (internal audits) with various themes as means of confirming the compliance situations of each of the parent company's departments as well as of Group companies.

**Compliance/Risk Management Leaders (CRL)**

Each division and main Group company appoints "compliance and risk management leaders (CRL)." Besides working to share information through monthly CRL meetings, a concise intranet compendium of legal and regulatory information, and other means, CRLs strive to gain a good understanding of problems and promote the implementation of effective countermeasures. The CRLs play a central role in "daily triple check" compliance self-assessment activities by each employee, and they also gather the latest legal and regulatory information, adjust internal regulations to harmonize with changes in the external legal and regulatory environment, and conduct monthly checks to confirm the nature of compliance performance within the Group.

**Corporate Ethics Handbooks and Compliance Cards**
All employees are provided with copies of the *Handbook for Corporate Ethics*, which includes legal compliance guidelines. To promote rigorous compliance with those guidelines, each employee undertakes self-assessment activities as well as "daily triple checks." In fiscal 2009, the Daikin Group revised the handbook it prepared before becoming a participant in the United Nations' Global Compact program* by adding materials related to the elimination of forced labor and child labor. As another means of increasing each employee's consciousness of ethics issues, the Group has issued compliance cards designed to be carried by employees at all times.

** Launched in July 2000, the United Nations Global Compact is a strategic policy initiative in which diverse companies and other organizations are participating. By improving the responsible corporate citizenship and collective activities of participating companies, the Compact aims to align business activities throughout the world with 10 universally accepted principles and catalyze actions in support of broader UN goals. The 10 universally accepted principles relate to human rights, labor, environment, and anticorruption objectives.*

## Living Up to Society's Expectations and Trust

Rather than focusing on clear-cut laws and regulations alone, the Daikin Group Philosophy recognizes the need to constantly remember the need to "thoroughly respect those things that should be respected in light of what is required to sustain sound corporate activities while living up to society's expectations and trust amid changing societal conditions."

The Law, Compliance & Intellectual Property Center has established a Corporate Ethics Consultation service that enables employees to consult or offer opinions via telephone calls or facsimile transmissions. When ethics problems are reported, the center investigates and cooperates with relevant Group units to establish systems for quick and appropriate response measures. In the case that countermeasures require the collaboration of multiple Group units, emphasis is placed on concurrently implementing thorough countermeasures in each relevant unit. Attention has been given to making the Corporate Ethics Consultation service easy to utilize through measures including those to strictly preserve the confidentiality of those using the service.

Japan's Financial Instruments and Exchange Law (also referred to as the Japanese version of the U.S. Sarbanes-Oxley Act, or J-SOX) took effect during fiscal 2009. To respond to J-SOX, Daikin began revising and upgrading its internal control systems related to financial reporting in August 2005. Subsequently, the Company introduced systems designed to ensure the appropriateness of all operational processes throughout the Daikin Group that could affect financial reporting.

Daikin is continually evaluating these systems to ensure they are properly functioning so that the Company is able to effectively and appropriately provide the internal control reports required by J-SOX. We are preparing to make corrections to the systems if needed to ensure our sustained compliance with J-SOX and related regulations.

In addition to its internal control systems, the Daikin Group has established global accounting regulations and is working to ensure that each Group company is well aware of these regulations as well as to make further improvements with respect to the effectiveness and appropriateness with which the regulations are followed.

Through its response to J-SOX, Daikin is naturally taking measures to attain such internal control objectives as those associated with ensuring the dependability of financial reports and increasing the effectiveness and efficiency of related operations. In addition, the Company is doing its utmost to work through its actions to earn still greater trust and confidence on the parts of shareholders and diverse other stakeholders.

While living up to its responsibilities to its stakeholders, the Daikin Group is endeavoring to help society realize sustainable growth. The Group's fundamental corporate social responsibility (CSR) policies are as follows.

1. By ensuring the thorough application of its Group Philosophy, the Daikin Group will execute its social responsibilities worldwide with respect to all stakeholders, thereby increasing its corporate value and contributing to society's sustainable development.
2. Based upon the solid foundation of rigorous legal compliance and corporate ethics, the Daikin Group will undertake CSR initiatives with emphasis on contributing to society. These initiatives will include those to create and offer new value by anticipating the future needs of customers; to take measures throughout business operations that sustain and improve the environment and to promote new product development and technological innovation that facilitates society's environmental friendliness; to build friendly yet competitive relations with all suppliers and other business partners; and to cultivate workplaces that foster pride and enthusiasm in each employee. Furthermore, acting as a good corporate citizen, the Daikin Group will demonstrate its usefulness and high level of sensitivity to each community in which it operates by undertaking activities that contribute to society.
3. Rather than simply undertaking business activities that reflect consideration of CSR, the Daikin Group will proactively incorporate CSR initiatives in all its business activities and integrate and unify such initiatives with business activities to realize truly sustained CSR programs and promote improved business performance.
4. The Daikin Group will pursue CSR in a distinctive Daikin manner that leverages Daikin's strengths regarding its traditional corporate culture—which emphasizes freedom and boldness, thorough customer-oriented management, warm hospitality, and other virtues—as well as its world-leading technologies and other special Daikin resources.
5. The Daikin Group will undertake CSR while engaging in widespread two-way communications within society, living up to its responsibility to explain its actions, and maintaining a high level of transparency.

Based on these policies and due consideration of its own special characteristics, the Daikin Group is currently implementing CSR programs while placing particularly strong emphasis on four CSR themes—"the natural environment," "quality and customer satisfaction," "human resources," and "contributions to society."

## Environment

The Daikin Group recognizes that promoting a balanced combination of environmental preservation and economic growth is the key to the sustainability of its operations. As the world's only company that engages in the development and production of both air-conditioning equipment and fluorocarbon refrigerants, Daikin is striving to leverage the energy saving technologies incorporated in its offerings to help customers reduce their $CO_2$ emissions. The Group has also progressively lowered the level of $CO_2$ emissions associated with its own manufacturing processes, aiming to cut emissions to half the fiscal 2006 level (to 1.4 million tons or less) by fiscal 2011. By making the kind of contributions that are optimal for each country and region of the world, the Daikin Group is endeavoring to promote the global spread of a "green-hearted" spirit that cherishes the Earth and emphasizes environmental friendliness as well as the inheritance of that "green-hearted" spirit by future generations.

## Product Quality/Customer Satisfaction

Besides doing its utmost to ensure the safety and increasingly high quality of its products in line with customers' expectations, Daikin is intent on promoting ever-higher levels of customer satisfaction by realizing an unparalleled level of service quality with respect to speed, dependability, and cordial solicitude. In both air-conditioning equipment and chemicals operations, Daikin has obtained a growing number of international ISO 9001 certifications of its quality management systems. Currently, all corporate bases in Japan have these certifications, while 10 overseas air-conditioning bases and seven overseas chemical bases have ISO 9001 certifications. Daikin's service departments are now working to obtain their own ISO 9001 certifications.

## Human Resources

In line with its corporate philosophy, the Daikin Group is promoting "people-oriented" management. Recognizing that a company's people are its most fundamental source of competitive strength, Daikin has established personnel and remuneration systems that provide congenial conditions for the self-development efforts of dynamically ambitious employees. The Company emphasizes the principles of "equal opportunity" and "fairness" as it seeks to ensure that personnel are appropriately rewarded for their contributions. Moreover, the Company welcomes and respects diverse employees, regardless of their age, gender, nationality, race, or special needs, and it seeks to enable all its employees to maintain a good work-life balance. Also emphasizing measures to ensure its employees' health and safety, Daikin works to provide work environments that are beneficial for workers' mental and physical health as well as augmenting worker satisfaction.

## Contribution to Society

As it has expanded its presence throughout the world, the Daikin Group has sought to establish strong roots in many regional and local societies and undertake CSR activities that make tangible contributions to those societies. Much of these contributions stem from Group employee participation in such programs as those involving arts and culture, education, and environmental preservation.

**For the Benefit of the World,**
**For the Benefit of Society**

The following sections describe recent events that concretely illustrate the state of the Daikin Group's CSR activities.

## Start of "Re: Air Conditioner Project"

In fiscal 2009, Daikin began the "Re: Air Conditioner Project" cooperative-type environmental preservation project in collaboration with room air conditioner users. The most distinctive aspect of the project is that, rather than centering on corporate environment protection efforts alone, it calls for the Company and users to think and take action together. When users select the "Comfort Eco Mode" setting on their air conditioner remote control—which automatically controls temperature, humidity, and air flows in a way that promotes the concurrent attainment of energy savings and comfort—they accumulate the Daikin Group's unique eco points, and a tree displayed on the remote control screen will grow. When the tree has grown to maturity, the user can contact Daikin, which makes a contribution to a forest preservation program on the user's behalf.

In November 2008, Daikin cooperated with an international nonprofit organization, Conservation International, to participate in a tree-planting ceremony at the Gunung Gede-Pangrango National Park in Indonesia to mark the start of a new conservation program. Different from conventional tree-planting programs, this program is designed to help enable the local community to obtain alternative income sources—such as fruit tree cultivation and eco-tourism—in place of logging and, thereby promote ecodiversity preservation while providing educational opportunities related to forest restoration and development. This project is expected to generate a particularly high level of benefits because it is being planned and executed based on the results of scientific surveys.

Daikin is providing detailed information on the significance and progress of the project via its "Re: Air Conditioner Project" website.

## Recognition as an "Eco First Enterprise"

Through the implementation of its "Environmental Fusion" plan—a component of the FUSION 10 strategic management plan covering the last three years of that plan's term—the Daikin Group is currently placing strong emphasis on proactive measures to both preserve the environment and expand business operations. In November 2008, Daikin became the first member of the air-conditioning industry to be designated an "Eco First Enterprise" by Japan's Ministry of the Environment.

Established in April 2008 to promote autonomous environmental preservation activities by leading companies in each industry, the "Eco First Enterprise" system calls for leading companies to make promises to the Environment Minister regarding their plans to implement global warming countermeasures that help attain Kyoto Accord targets and other environmental activities. Companies who announce these "Eco First Promises" and have them approved by the Environment Ministry are authorized to use the "Eco First Mark" environmental label.

The main points of the "Eco First Promises" announced by the Daikin Group are that Daikin will:

1. Promote a reduction in the emission of greenhouse gases associated with business activities,
2. Develop and promote the diffusion of products that contribute to the prevention of global warming,
3. Minimize refrigerant leakage—from the time of manufacture to the time of disposal—by promoting the recovery and destruction of refrigerant, and
4. Rigorously manage chemical substances and reduce emissions of such substances.

Going forward, the Daikin Group will leverage such environment-friendly technologies as those related to inverters and heat pumps as it endeavors to promote global warming prevention and corporate growth concurrently.

## "*Sho-Ene Toban*" Wins Environment Minister's Award at the Eco-Products Awards 2008

As air-conditioning can account for up to about 40% of an office building's total energy consumption, it is clear that conserving the energy consumed by air conditioners is an important task. In light of this, the Daikin Group is proposing environmental impact reduction methods related to all processes, from the design and manufacture of new air conditioners through the provision of preventive maintenance and management services for installed air conditioners.

In November 2008, one of these initiatives—the "*Sho-Ene Toban*" (Conserve Energy On-Duty) remotely controlled energy conservation service—became the first remotely controlled energy conservation technology for air conditioners to be awarded the Eco-Service Division Environment Minister's Award of the Eco-Products Awards, which are supported by the Ministry of the Environment; the Ministry of Economy, Trade and Industry; and the Ministry of Agriculture, Forestry and Fisheries as well as other sponsors.

Established in 2004, the Eco-Products Awards are designed to broadly spread information related to outstanding environment-friendly products and services (referred to collectively as eco-products) among consumers and to support the environmental protection efforts of companies with advanced approaches to environment friendliness and other entities. In these ways, the awards are meant to promote the widespread use of eco-products in Japan.

The award-winning "*Sho-Ene Toban*" uses local weather forecasts and building air conditioner operation data to remotely input optimal energy-saving operational modes into building air conditioner systems and otherwise control the systems from a remote location. It is capable of reducing $CO_2$ emissions from building air conditioner systems by up to 20%.* It has attracted numerous customers since its November 2006 launch, and, as of the end of August 2008, it was estimated to be enabling the annual reduction of the equivalent of approximately 440 tons** of $CO_2$ emissions. This high level of energy conservation performance is the factor that won "*Sho-Ene Toban*" the Environment Minister's Award.

**This figure is based on calculations for a 2,000m$^2$-class office building in Japan's 60Hz electric power region.*

***This figure is calculated based on the aggregated energy conservation goals of individual customers.*

## Expanded Hiring of the Physically Challenged

The Daikin Group is expanding its hiring of physically challenged people. In June 2009, Daikin Sunrise Settsu Co., Ltd., began full-scale operation of a new facility that has approximately three times more floor space than its previous facility. Based in Settsu, Osaka, Daikin Sunrise Settsu is a private/public-sector company in which Daikin has invested with the objective of creating a facility that employs numerous severely challenged people. Its main businesses include the subcontracted manufacture and computer-aided design (CAD) of components for air conditioner and oil hydraulic products, and it currently employs 74 people, of whom 68 are physically challenged. Having become profitable during its second year of operation, it was able to increase its ordinary income to ¥160 billion in fiscal 2009.

The new facility was constructed in line with plans to improve employees' skills and make the most of employees' accumulated experience and know-how to progressively expand the scope and increase the sophistication of Daikin Sunrise Settsu's operations.

Because the company's factory operations are handled entirely by physically challenged people, the new building offers tools and equipment that are easy to operate while in a wheelchair, a support school and other training facilities, and a wide range of other conveniences that have attracted nationwide attention. Based on the Daikin Group's goal of helping the physically challenged realize personal growth through involvement with manufacturing activities that enable them to play roles that contribute to society, Daikin plans to further increase the workforce of Daikin Sunrise Settsu to 100 people during fiscal 2012.

Building on the experience gained via Daikin Sunrise Settsu, Daikin has also promoted the proactive hiring of physically challenged people by Daikin Air-Conditioning (Shanghai) Co., Ltd., and this initiative has won that company the designation by the Shanghai government as an "occupational training base for physically challenged people."

For more-detailed information about our CSR activities, please visit our website. You may also download our *CSR Report* from the website.

**http://www.daikin.com/csr/index.html**

# Five-Year Summary

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years ended March 31



| | Millions of yen | | | | |
|---|---|---|---|---|---|
| | **2009** | 2008 | 2007 | 2006 | 2005 |
| Net sales: | **¥1,202,420** | ¥1,291,081 | ¥911,749 | ¥792,837 | ¥729,414 |
| Air conditioning | **1,059,435** | 1,131,932 | 752,181 | 641,637 | 589,808 |
| Chemicals | **101,910** | 116,096 | 116,493 | 107,412 | 99,612 |
| Others | **41,075** | 43,053 | 43,075 | 43,789 | 39,994 |
| Operating income | **61,394** | 128,098 | 80,754 | 66,547 | 60,206 |
| Income before income taxes and minority interests | **45,974** | 118,136 | 83,128 | 67,010 | 63,111 |
| Net income | **21,755** | 74,822 | 45,420 | 40,146 | 38,083 |
| Per share of common stock (in yen): | | | | | |
| Basic net income* | **¥74.51** | ¥262.24 | ¥172.66 | ¥152.11 | ¥144.24 |
| Diluted net income | **74.50** | 262.04 | 172.58 | 152.07 | 144.21 |
| Cash dividends applicable to the year | **38.00** | 38.00 | 28.00 | 22.00 | 18.00 |
| Total assets | **¥1,117,418** | ¥1,210,094 | ¥1,161,364 | ¥716,440 | ¥615,596 |
| Total equity | **484,486** | 559,987 | 409,952 | 340,523 | 271,716 |
| Net property, plant and equipment | **243,083** | 243,142 | 238,319 | 196,485 | 170,209 |
| Number of employees | **39,896** | 36,300 | 33,480 | 21,747 | 19,062 |

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

**Restatement of a Portion of the Company's Securities Report (*Yuka Shoken Hokokusho*)**

Upon the discovery of inappropriate accounting methods in the Company's After Sales Service Division involving the front-loading of sales and construction work-in-progress, the Daikin Group conducted an in-depth investigation of these accounting methods. On May 8, 2009, based on those findings, the Company announced corrected financial statements for the fiscal years ended March 31, 2004, 2005, 2006, 2007, and 2008 and submitted restated securities reports to the Kanto Local Finance Bureau. We again extend our sincere apologies to shareholders for this incident.

In accordance with the restatement of the securities reports, the Company made the following corrections to the financial figures in this annual report:

**Effect of Corrections**

| | | Millions of yen | | | | |
|---|---|---|---|---|---|---|
| | | Net sales | Operating income | Net income | Total assets | Total equity |
| Year ended March 31, 2004 | Before corrections | 625,718 | 47,988 | 28,611 | 536,379 | 235,771 |
| Consolidated financial statements | After corrections | 625,080 | 46,920 | 26,869 | 534,726 | 234,029 |
| Year ended March 31, 2005 | Before corrections | 728,880 | 60,897 | 38,747 | 617,874 | 274,122 |
| Consolidated financial statements | After corrections | 729,414 | 60,206 | 38,083 | 615,596 | 271,716 |
| Year ended March 31, 2006 | Before corrections | 792,857 | 67,077 | 40,709 | 719,382 | 343,492 |
| Consolidated financial statements | After corrections | 792,837 | 66,547 | 40,146 | 716,440 | 340,523 |
| Year ended March 31, 2007 | Before corrections | 912,128 | 80,939 | 45,619 | 1,164,575 | 413,121 |
| Consolidated financial statements | After corrections | 911,749 | 80,754 | 45,420 | 1,161,364 | 409,952 |
| Year ended March 31, 2008 | Before corrections | 1,290,893 | 128,497 | 75,224 | 1,213,649 | 563,557 |
| Consolidated financial statements | After corrections | 1,291,081 | 128,098 | 74,822 | 1,210,094 | 559,987 |

## Overview of Net Sales

The crisis in the global economy, especially in the latter half of fiscal 2009, grew suddenly more serious. Daikin and its consolidated subsidiaries (Daikin, the Group) experienced a sharp decline in demand in their air-conditioning business, both in Japan and overseas, as well as in their chemicals business, particularly from the automobile and semiconductor industries.

On the other hand, since Daikin attained the targets for fiscal 2010 set in its Fusion 10 strategic management plan one year ahead of schedule, it formulated a plan for the latter three years of Fusion 10 and, under its motto of "Dynamism and Challenge," began to work toward the new targets in fiscal 2009.

As a result, however, of the decline in demand in the latter half of the fiscal year and the impact of foreign currency factors accompanying the appreciation of the yen, Daikin reported a decline in consolidated net sales of 6.9%, to ¥1,202,420 million. Despite initiatives to reduce manufacturing costs and cut other expenses and fixed costs, consolidated operating income declined a substantial 52.1%, to ¥61,394 million, and consolidated net income decreased 70.9%, to ¥21,755 million. These declines in profitability were due to increases in the prices of raw materials, the decrease in net sales, reduced utilization rates of plant and equipment, and other factors.

### Impact of Changes in Currency Exchange Rates

Compared to the previous fiscal year, the yen appreciated against the U.S. dollar and the euro. As a result of these movements in foreign currency exchange rates, Daikin sales were estimated to be ¥97.0 billion lower and operating income ¥27.0 billion lower than they would have been without movements in exchange rates.

The impact of changes in foreign exchange rates was estimated based on a comparison of the yen value of non-yen transactions by each overseas subsidiary and other Group companies when converted at the exchange rates shown below.

| | Fiscal 2008 | Fiscal 2009 |
|---|---|---|
| Yen-U.S. dollar rate | ¥114 | ¥101 |
| Yen-euro rate | ¥162 | ¥143 |

## Net Sales by Product Segment

### Air-Conditioning

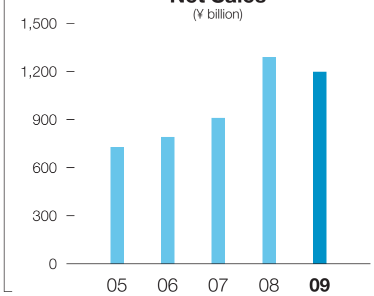
*Japan*

Demand in Japan for residential air-conditioning systems rose above the same period of the previous year during the first half of the fiscal year, sustained by favorable weather conditions during the high-demand period in July. In the second half, however, demand fell below the level of the previous year, and, for the fiscal year as a whole, demand was at about the same level as in the previous year.

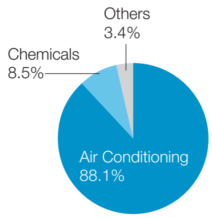
Daikin actively promoted the URURU & SALALA room air-conditioning systems, which feature an extremely quiet automatic filter-cleaning function and conform to the Japanese energy-saving standards that will be applied from 2010. As a consequence of these marketing efforts, units sold rose above the level of the previous fiscal year.

Industry demand for package air-conditioning systems in the first half of the fiscal year was at about the same level as during the same period of the previous fiscal year. However, beginning in the second half, capital investment was restrained because of the downturn in the economy and stagnation in construction starts. As a result, demand for the fiscal year was below the level of the previous fiscal year. Daikin's performance was influenced by the decrease in industry demand, and sales in both unit and value terms declined. Even in the midst of these conditions, however, Daikin focused on conducting proposal-type sales promotion campaigns directed at marketing agencies and users that focused on such products as the Ve-up Q multiple air-conditioning systems for office buildings, which enable the rapid replacement of units using existing piping, and the Hotto Eco Building Multi multiple air-conditioning systems for use in cold regions. As a consequence, Daikin was able to increase sales in unit and value terms of multiple air-conditioner systems for building use over the previous fiscal year.

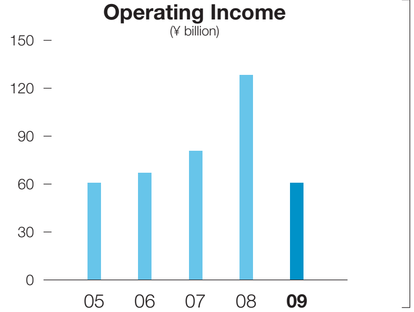
**Net Sales**
(¥ billion)




**Sales Breakdown**




**Operating Income**
(¥ billion)



**Unit Sales of Air-Conditioning Systems in the Japanese Air-Conditioning Industry (Fiscal 2009)**
(1,000 units)

| | First half | Year on year | Second half | Year on year | Full year | Year on year |
|---|---|---|---|---|---|---|
| Residential use | 5,333 | 6% | 2,260 | (9%) | 7,593 | 1% |
| Commercial use | 416 | 0% | 311 | (8%) | 727 | (4%) |

*Overseas*

Because of the appreciation of the yen and decline in value of the euro, U.S. dollar, and other foreign currencies, sales of the overseas air-conditioning business rose over the previous year during the first half of the fiscal year, but declined year on year for the full fiscal year.

In Europe, unit sales of both residential and commercial air conditioners were below the previous year because of unfavorable weather conditions, the economic downturn, and the credit contraction accompanying the financial crisis. Demand in the major countries of Western Europe was down steeply from the previous year. Under these circumstances, Daikin worked to increase its market share even in the midst of declining demand, expand sales in regions where growth is expected in the medium-to-long term, including central Europe, Eastern Europe, Russia, the Middle East, and elsewhere, and expand its business domains to include heating systems and large-scale commercial (applied) air-conditioning equipment.

In the heating systems business, Daikin acquired the heating equipment business of Rotex Heating Systems GmbH in Germany in October 2008 and took other initiatives to enlarge its business base in this field. Unit sales of the heat-pump-type hot water heating systems for residential use that Daikin developed for the European market showed a major increase of threefold over the previous fiscal year.

In China, although the economy moved into a downturn following the Beijing Olympics, and conditions in the real estate market deteriorated, unit sales of air-conditioning systems for residential and commercial use both rose over the previous year, and total sales also rose above the prior year. The Daikin Group is working to expand its sales channels from major cities to regional areas and broadening marketing activities to sell multiple air conditioners, which are one of Daikin's strongest core products, through approaches carefully tailored to the needs of commercial and residential users.

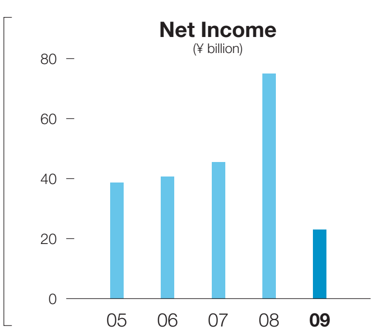
The Daikin Group places emphasis on environmental initiatives and, in February 2009, concluded a cooperative agreement with Chinese air-conditioning system manufacturer Gree Electric Appliances, Inc., of Zhuhai. Under this agreement, Daikin will combine its energy-conservation technology with the low-cost production capabilities of Gree to expand sales of inverter-type air-conditioning systems for the mass market.

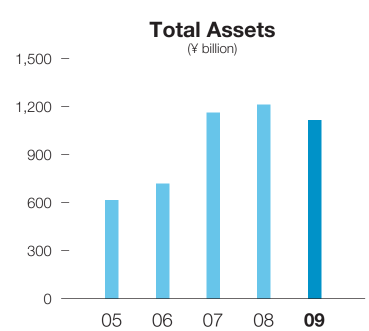
In the inverter-type air-conditioning systems field, Daikin has formulated a strategy to market its inverter-type systems around the world. The usage ratio of inverter-type units has reached 100% in Japan, but is only about 7% in China and virtually zero in North America.

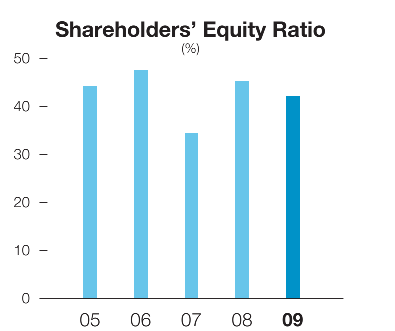
In Southeast Asia and Oceania, unit sales in Australia were below the level of the previous fiscal year because of the economic downturn, but unit sales in Thailand and Malaysia rose above the prior year.

Among emerging markets, rates of expansion slackened in the latter half of the fiscal year, reflecting the effects of the global economic downturn, but Daikin worked to strengthen and further develop the capabilities of its sales companies. As a consequence, sales in central Europe, Eastern Europe, the Middle East, and India expanded above the previous year, and Daikin was able to report further progress in developing its position in the emerging economies.

In the Americas, despite the weakness in residential and commercial construction fields, Daikin's unit sales of



systems for residential use were at about the same level as during the previous year, and sales of systems for commercial use exceeded the previous year's level. Daikin Group member McQuay International obtained an order to supply air-conditioning equipment for the Freedom Tower, which will be built on the site of the former New York World Trade Center and is expected to become a new symbol of New York City. Daikin's air-conditioning technology has been recognized and accepted in the United States. This order is expected to lead to increased awareness of Daikin and expansion in future business.

In the low-temperature/freezing equipment business, sales were substantially below the level of the previous year, reflecting the worldwide drop in demand for ocean-going transportation in the second half of the fiscal year.

As a result of these various factors, the net sales of Daikin's air-conditioning business in Japan and overseas amounted to ¥1,059,435 million, 6.4% lower than the prior fiscal year. Operating income was ¥71,649 million, 42.3% below the previous year.

**Chemicals**

In the fluorochemicals sector, during the first half of the fiscal year, sales of products for use in LAN cables and sales in China and Europe rose and were above the level of the previous year, but, beginning in the second half, demand, principally from the semiconductor and automobile industries, dropped sharply, and, as a result of inventory adjustments, sales were below the previous year.

In the chemical products sector, sales of fine chemical products for use in LCDs and water and oil repellents to the Chinese and other Asian markets remained firm. However, demand for water and oil repellents dropped in Japan, the United States, and Europe, while demand for etching chemicals for the semiconductor industry also decreased. As a result, sales of chemicals fell below the previous year.

Sales of fluorocarbon gases rose above the prior year, supported by strong sales in the rest of Asia.

As a consequence of these factors, chemical business sales declined 12.2%, to ¥101,910 million. Profitability was adversely influenced by the declines in sales and production, changes in the product mix, and other factors. In addition, as a result of the impact of the appreciation of the yen, increases in raw material prices, and other developments, this business reported an operating loss of ¥9,509 million.

**Others**

In the industrial machinery related oil hydraulic equipment business, leading manufacturers in the machine tool field, which are key customers for this business, cut their production levels drastically. Especially in the latter half of the fiscal year, sales of this business fell below the previous year. Exports were above the level of the previous fiscal year during the first half because of an expansion in sales of inverter oil hydraulic units (super units) to molding machinery manufacturers in Taiwan and South Korea. However, for the year as a whole, sales were below the previous year, reflecting the effects of global market stagnation.

Sales of oil hydraulic equipment for construction equipment and vehicles were above the previous year because of the positive effects of an expansion in sales of medium-load closed circuit pumps (HSTs) in global markets, including the United States and Europe in particular.

In the defense business, deliveries of munitions to Japan's Ministry of Defense remained firm.

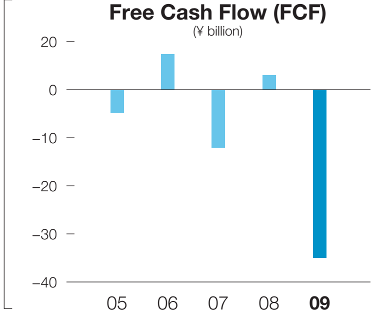
As a result of these factors, net sales in this segment declined 4.6%, to ¥41,075 million, and, reflecting the worsening profit situation of the oil hydraulics business, the segment reported an operating loss of ¥818 million.

## Costs, Expenses, and Earnings

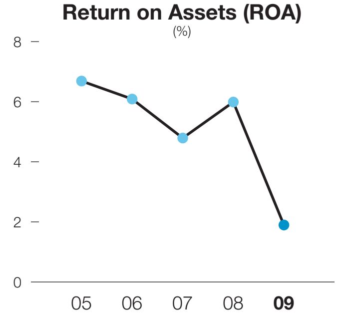
Reflecting the impact during the latter half of the year of a decrease in demand associated with rapid economic deceleration as well as of foreign currency translation factors associated with the progressive appreciation of the yen, consolidated net sales in the fiscal year under review amounted to ¥1,202,420 million, down 6.9% from the level in the previous fiscal year.

Although Daikin had reported 8 consecutive fiscal years of record-high operating income and 14 consecutive years of increase in this indicator, in fiscal 2009, operating

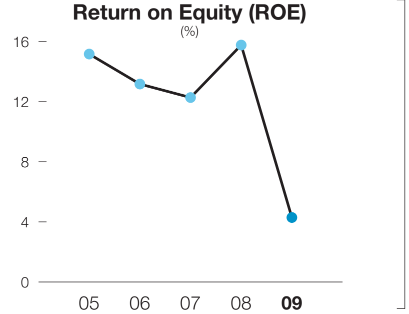
**Free Cash Flow (FCF)**




**Return on Assets (ROA)**




**Return on Equity (ROE)**



income declined 52.1%, to ¥61,394 million. The operating income ratio declined 4.8 percentage points, to 5.1%. Despite the reduction of cost of sales and SG&A expenses, the decline in operating income reflected the impact of such factors as the drop in net sales, surging raw materials prices, and a fall in the capacity utilization rate.

The cost of sales amounted to ¥838,760 million, ¥10,772 million lower than in the previous fiscal year, reflecting the impact of such factors as changes in foreign currency exchange rates and a fall in the capacity utilization rate. The cost of sales ratio deteriorated to 69.8%, compared with 65.8% in the previous fiscal year, owing to the decline in sales and a rise in manufacturing fixed costs. Selling, general and administrative expenses decreased ¥11,185 million, to ¥302,266 million, due to progress made in cutting costs and reducing expenses and fixed expenses.

Other income (expenses)—net amounted to expenses of ¥15,420 million, reflecting an increase of ¥5,112 million in foreign exchange losses and other factors.

As a result, net income amounted to ¥21,755 million, 70.9% lower than in the previous fiscal year.

## Outlook for Fiscal 2010

As a result of the economic downturn on a global scale and the deterioration in the real economy, the outlook is for negative growth in fiscal 2010, the first year of negative growth in the world economy in the postwar period. To deal with these conditions, governments around the world have formulated and are implementing economic policies, but recovery will take time. In view of the weakness in total demand, extremely challenging economic conditions are assumed to continue for the time being.

Daikin has selected the phrase “Now is the time for full focus on the three Cs—Creative Challenge & Change” for its New Year’s slogan. Daikin will take up the challenge of changing and creating a corporate structure that is flexible and nimble as well as able to survive and win in the rapidly changing environment.

In particular, Daikin has positioned thoroughgoing emphasis on securing short-term profits as its maximum priority goal. Daikin will implement every measure possible to attain this goal and, at the same time, for themes aiming at medium-to-long term growth and development, will put emphasis on exercising selectivity and concentration in the allocation of resources as it works to accelerate the creation of results in these areas.

Specific initiatives will include the following:

- Daikin will demonstrate its comprehensive strengths, including sales, service, product development, production, and supply chain management to increase its market share in existing products
- Even under recessionary conditions, Daikin will expand sales of environment-related products for which demand is strong (such as inverter air-conditioning systems, heater and hot water supply, and large-scale commercial (applied) air-conditioning applications).
- Substantially stronger promotion of total cost reduction initiatives
- Major reductions in fixed costs (restrain capital investments, focus R&D themes more sharply, undertake reassignment of personnel, and conduct Companywide reductions in expenses)
- Drastic reductions in capital investments (stop all investments other than those related to major themes)

At the same time, Daikin will look to the period of recovery following the current recession and aim to leap ahead of other companies by emphasizing the following themes drawing on the full energies and resources of the Daikin Group.

- Substantially increase the pace of development of environment-related products, such as next-generation cooling and air-conditioning equipment
- Structure sales networks in emerging countries (especially India and Brazil)
- Structure new business models that are environmentally focused and can offer products that meet customer needs in the residential, shop and office, building, factory, and other areas as well as comprehensive systems and solutions

Daikin’s outlook on a consolidated basis for fiscal 2010 is for an 11.0% decrease in net sales, to ¥1,070.0 billion, a 34.8% decline in operating income, to ¥40.0 billion, and a 44.8% decline in net income, to ¥12.0 billion.

Foreign currency exchange rates assumed for fiscal 2010 are ¥120 to one euro and ¥90 to one U.S. dollar.

### Assets

At the end of fiscal 2009, consolidated total assets amounted to ¥1,117,418 million, ¥92,676 million lower than at the previous fiscal year-end. Current assets declined ¥78,801 million, to ¥531,834 million, as a consequence of lower trade receivables and other factors.

Fixed assets were down ¥13,875 million from the previous fiscal year-end, to ¥585,584 million, despite increases in capital investment in overseas production bases in the air-conditioning business segment, because of declines in the market prices of investment securities.

### Liabilities and Total Equity

Total liabilities declined ¥17,175 million as a result of decreases in trade payables and certain other items, to ¥632,932 million. The ratio of interest-bearing debt increased to 37.4%, from 29.5% at the end of the previous fiscal year, because of a rise in commercial paper outstanding and other factors. Total equity was positively impacted by the reporting of net income, but this was offset by changes in the foreign currency translation adjustments account because of currency rate fluctuations and by changes in the net unrealized (loss) gain on available-for-sale securities account owing to fluctuations in market prices of securities. Total equity therefore declined ¥75,501 million, to ¥484,486 million.

As a consequence, the ratio of shareholders' equity to total assets declined to 42.2%, compared with 45.1% at the end of the previous fiscal year, and net assets per share declined to ¥1,615.98, versus ¥1,867.79 at the end of the prior year.

## Cash Flows

### Capital Investment

In accordance with the Daikin Group's fundamental strategy of "concentrating management assets in business fields that offer higher profitability," the Company implemented capital investments during fiscal 2009 with a total value of ¥61,381 million, largely in the air-conditioning and chemicals business fields. In fiscal 2010, to reform Daikin's business position to enable it to move flexibly and nimbly to win in a fast-changing environment, all capital investments, with the exception of those related to major corporate themes, have been suspended. As a result, capital investments for fiscal 2010 are expected to amount to ¥35.0 billion.

| Business segment | Company name | Investment amount (¥ million) |
|---|---|---|
| Air-conditioning | Daikin | 14,603 |
| | O.Y.L. Industries Group | 10,916 |
| | Daikin Europe N.V. | 4,404 |
| | Daikin Industries (Thailand) Ltd. | 2,581 |
| Chemicals | Daikin | 8,579 |
| | Daikin America, Inc. | 3,295 |
| Others | Daikin | 1,615 |

Net cash provided by operating activities amounted to ¥62,238 million, reflecting the reporting of income before income taxes and minority interests as well as depreciation and amortization.

Net cash used in investing activities amounted to ¥99,302 million, mainly owing to payment for purchases of property, plant and equipment and the acquisition of Rotex.

Net cash provided by financing activities amounted to ¥48,382 million, mainly from the increase in commercial paper and other factors.

Consequently, cash and cash equivalents at March 31, 2009, amounted to ¥104,323 million.

## Dividends

Regarding returns to shareholders, Daikin 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. The Company employs internal reserves for strategic investments designed to further strengthen its managment structure as well as to accelerate its global business development, accelerate its development of products that contribute to the global environment with the objectives of increasing the scale of its business operations, and raising the level of its competitiveness.

Dividends applicable to fiscal 2009 amounted to ¥38 per share (¥19 per share interim dividend and ¥19 per share year-end dividend), the same as for the previous fiscal year. Because of uncertainties regarding the future business environment, no decision has yet been finalized regarding the proposed level of dividends for the current fiscal year.

## Principal Risks Associated with the Daikin Group's Operations

There are diverse factors with the potential for affecting the Daikin Group's performance and financial condition as well as the Company's share price and investment decisions. Principal business risks associated with the Group's development of operations in Japan and overseas include the following:

- Sharp changes in politico-economic conditions or supply-demand relationships in principal markets (Japan, Europe, North America, and China and other Asian countries other than Japan, etc.)
- Cold summer weather and other unusual weather patterns accompanied by reduced demand for air conditioners
- Major product quality claims
- Major problems with manufacturing systems
- Major changes in the market prices of negotiable securities and other assets
- Improper use of the Group's intellectual property by third parties
- Leakage of personal information or other confidential information
- Unforeseen accidental damage to manufacturing or other facilities due to earthquakes or other natural disasters
- Lawsuits filed against the Company
- Other risks that are difficult to foresee

# Consolidated Balance Sheets

Daikin Industries, Ltd. and Consolidated Subsidiaries
March 31, 2009 and 2008





| | Millions of yen | |
|---|---|---|
| **ASSETS** | **2009** | 2008 As Restated (Note 1) |
| **Current assets:** | | |
| Cash and cash equivalents | **¥ 104,323** | ¥ 110,484 |
| Short-term investments (Note 7) | **919** | 1,173 |
| Trade receivables (Notes 6 and 7): | | |
| Notes | **15,878** | 15,027 |
| Accounts | **162,370** | 211,167 |
| Allowance for doubtful receivables | **(5,104)** | (5,453) |
| Inventories (Notes 3 and 7) | **216,645** | 236,554 |
| Deferred tax assets (Note 11) | **9,782** | 13,365 |
| Prepaid expenses and other current assets (Note 7) | **27,021** | 28,318 |
| **Total current assets** | **531,834** | 610,635 |
| **Property, plant and equipment** (Note 7): | | |
| Land | **27,825** | 28,649 |
| Buildings and structures | **168,758** | 160,069 |
| Machinery and equipment | **340,612** | 345,159 |
| Furniture and fixtures | **107,324** | 108,400 |
| Lease assets (Note 14) | **3,169** | |
| Construction in progress | **21,891** | 19,070 |
| Total | **669,579** | 661,347 |
| Accumulated depreciation | **(426,496)** | (418,205) |
| **Net property, plant and equipment** | **243,083** | 243,142 |
| **Investments and other assets:** | | |
| Investment securities (Note 4) | **89,472** | 116,224 |
| Investments in and advances to unconsolidated subsidiaries and associated companies | **5,275** | 5,031 |
| Goodwill (Note 5) | **193,405** | 200,734 |
| Deferred tax assets (Note 11) | **18,961** | 5,137 |
| Other assets | **35,388** | 29,191 |
| **Total investments and other assets** | **342,501** | 356,317 |
| **Total** | **¥1,117,418** | ¥1,210,094 |

See notes to consolidated financial statements.

| LIABILITIES AND EQUITY | Millions of yen 2009 | Millions of yen 2008 As Restated (Note 1) |
|---|---|---|
| **Current liabilities:** | | |
| Short-term borrowings (Note 7) | ¥ 194,880 | ¥ 131,951 |
| Current portion of long-term debt (Note 7) | 29,418 | 8,781 |
| Current portion of long-term lease obligations (Note 14) | 1,237 | 108 |
| Trade payables (Note 6): | | |
| Notes | 8,645 | 9,725 |
| Accounts | 71,493 | 118,474 |
| Construction payable | 8,978 | 12,470 |
| Income taxes payable | 8,742 | 13,531 |
| Deferred tax liabilities (Note 11) | 3 | 1,436 |
| Accrued expenses | 48,169 | 56,814 |
| Other current liabilities (Note 6) | 57,560 | 59,747 |
| **Total current liabilities** | 429,125 | 413,037 |
| **Long-term liabilities:** | | |
| Long-term debt (Note 7) | 190,779 | 216,166 |
| Long-term lease obligations (Note 14) | 1,606 | 332 |
| Liabilities for retirement benefits (Note 8) | 3,939 | 4,291 |
| Deferred tax liabilities (Note 11) | 1,266 | 7,130 |
| Long-term accounts payable | 5,768 | 8,842 |
| Other long-term liabilities | 449 | 309 |
| **Total long-term liabilities** | 203,807 | 237,070 |
| **Commitments and contingent liabilities** (Notes 14 and 16) | | |
| **Equity** (Notes 9, 10 and 19): | | |
| Common stock—authorized, 500,000,000 shares; issued 293,113,973 shares in 2009 and 2008 | 85,032 | 85,032 |
| Capital surplus | 82,977 | 82,977 |
| Stock acquisition rights | 764 | 522 |
| Retained earnings | 366,836 | 351,499 |
| Net unrealized (loss) gain on available-for-sale securities | (15,398) | 10,102 |
| Deferred gain on derivatives under hedge accounting | 465 | 371 |
| Foreign currency translation adjustments | (43,481) | 19,160 |
| Treasury stock, at cost: 1,225,087 shares in 2009 and 981,373 shares in 2008 | (4,744) | (3,500) |
| Total | 472,451 | 546,163 |
| Minority interests | 12,035 | 13,824 |
| **Total equity** | 484,486 | 559,987 |
| **Total** | ¥1,117,418 | ¥1,210,094 |

# Consolidated Statements of Income

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2009 and 2008



| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 As Restated (Note 1) |
| **Net sales** (Note 6) | **¥1,202,420** | ¥1,291,081 |
| **Cost of sales** (Note 6) | **838,760** | 849,532 |
| **Gross profit** | **363,660** | 441,549 |
| **Selling, general and administrative expenses** (Note 6) | **302,266** | 313,451 |
| **Operating income** | **61,394** | 128,098 |
| **Other income (expenses):** | | |
| Interest and dividend income | **4,574** | 4,568 |
| Interest expense | **(7,033)** | (10,160) |
| Exchange losses | **(5,556)** | (444) |
| Gain on sales of land | | 20 |
| Loss on disposals of property, plant and equipment | **(1,705)** | (879) |
| Gain on sales of investment securities | **3** | 15 |
| Write-down of investment securities | **(2,775)** | (2,434) |
| Equity in earnings of unconsolidated subsidiaries and associated companies | **538** | 744 |
| Loss on termination of defined benefit pension plan | **(1,222)** | |
| Other—net | **(2,244)** | (1,392) |
| **Other expenses—net** | **(15,420)** | (9,962) |
| **Income before income taxes and minority interests** | **45,974** | 118,136 |
| **Income taxes** (Notes 2 and 11): | | |
| Current | **21,392** | 35,413 |
| Prior years | | 3,521 |
| Deferred | **(202)** | 1,194 |
| Total | **21,190** | 40,128 |
| **Minority interests** | **(3,029)** | (3,186) |
| **Net income** | **¥ 21,755** | ¥ 74,822 |

| | Yen | |
|---|---|---|
| **Amounts per common share** (Notes 2 and 17): | | |
| Basic net income | **¥74.51** | ¥262.24 |
| Diluted net income | **74.50** | 262.04 |
| Cash dividends applicable to the year | **38.00** | 38.00 |

See notes to consolidated financial statements.

# Consolidated Statements of Changes in Equity

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2009 and 2008

| | Outstanding Number of Common Shares Issued | Millions of yen | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Common Stock | Capital Surplus | Stock Acquisition Right | Retained Earnings As Restated (Note 1) | Unrealized Gain (Loss) on Available-for-Sale Securities | Deferred Gain (Loss) on Derivatives under Hedge Accounting | Foreign Currency Translation Adjustments | Treasury Stock | Total | Minority Interests | Total Equity As Restated (Note 1) |
| **Balance, April 1, 2007** | 263,016,549 | ¥28,023 | ¥25,968 | ¥219 | ¥285,938 | ¥ 33,780 | ¥ (26) | ¥ 26,227 | ¥(2,367) | ¥397,762 | ¥12,191 | ¥409,953 |
| Issuance of new shares (Note 9) | 29,300,000 | 57,009 | 57,009 | | | | | | | 114,018 | | 114,018 |
| Effect of change of the fiscal year-end of certain consolidated subsidiary (Note 2) | | | | | 39 | | | | | 39 | | 39 |
| Net income | | | | | 74,822 | | | | | 74,822 | | 74,822 |
| Cash dividends, ¥33 per share | | | | | (9,233) | | | | | (9,233) | | (9,233) |
| Repurchase of treasury stock | (293,837) | | | | | | | | (1,495) | (1,495) | | (1,495) |
| Disposal of treasury stock | 109,888 | | | | (67) | | | | 362 | 295 | | 295 |
| Net change in the year | | | | 303 | | (23,678) | 397 | (7,067) | | (30,045) | 1,633 | (28,412) |
| **Balance, March 31, 2008** | 292,132,600 | 85,032 | 82,977 | 522 | 351,499 | 10,102 | 371 | 19,160 | (3,500) | 546,163 | 13,824 | 559,987 |
| Adjustment of retained earnings due to an adoption of PITF No. 18 (Note 2) | | | | | **4,750** | | | | | **4,750** | | **4,750** |
| Effect of change of the fiscal year-end of certain consolidated subsidiary (Note 2) | | | | | **(14)** | | | | | **(14)** | | **(14)** |
| Net income | | | | | **21,755** | | | | | **21,755** | | **21,755** |
| Cash dividends, ¥38 per share | | | | | **(11,097)** | | | | | **(11,097)** | | **(11,097)** |
| Repurchase of treasury stock | **(310,281)** | | | | | | | | **(1,487)** | **(1,487)** | | **(1,487)** |
| Disposal of treasury stock | **66,567** | | | | **(57)** | | | | **243** | **186** | | **186** |
| Net change in the year | | | | **242** | | **(25,500)** | **94** | **(62,641)** | | **(87,805)** | **(1,789)** | **(89,594)** |
| **Balance, March 31, 2009** | **291,888,886** | **¥85,032** | **¥82,977** | **¥764** | **¥366,836** | **¥(15,398)** | **¥465** | **¥(43,481)** | **¥(4,744)** | **¥472,451** | **¥12,035** | **¥484,486** |

See notes to consolidated financial statements.

# Consolidated Statements of Cash Flows

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31, 2009 and 2008



| | Millions of yen | |
|---|---|---|
| | 2009 | 2008 As Restated (Note 1) |
| **Operating activities:** | | |
| Income before income taxes and minority interests | ¥ 45,974 | ¥118,136 |
| Adjustment for: | | |
| Income taxes—paid | (31,952) | (39,108) |
| Depreciation and amortization | 56,931 | 51,370 |
| Gain on sales of investment securities | (3) | (15) |
| Write-down of investment securities | 2,775 | 2,434 |
| Gain on sales of land | | (20) |
| Loss on disposals of property, plant and equipment | 1,705 | 879 |
| Equity in earnings of unconsolidated subsidiaries and associated companies | (538) | (744) |
| Changes in assets and liabilities, net of effects of the purchase of subsidiaries: | | |
| Trade notes and accounts receivable | 21,376 | (17,695) |
| Inventories | (3,885) | (27,541) |
| Other current assets | 169 | (3,468) |
| Prepaid pension cost | (893) | (711) |
| Trade notes and accounts payable | (31,191) | 7,661 |
| Accrued expenses | (972) | 7,863 |
| Other current liabilities | 4,271 | 6,559 |
| Liabilities for retirement benefits | (248) | (931) |
| Account payable for transaction to defined contribution pension plan | (707) | (3,460) |
| Other—net | (574) | 2,120 |
| Total adjustments | 16,264 | (14,807) |
| Net cash provided by operating activities | 62,238 | 103,329 |
| **Investing activities:** | | |
| Payment for purchases of property, plant and equipment | (61,381) | (47,339) |
| Proceeds from sales of property, plant and equipment | 442 | 2,331 |
| Payments for acquisition of newly consolidated subsidiaries, net of cash and cash equivalents acquired (Note 12) | (8,792) | (2,862) |
| Payments for transfer of business | (731) | |
| Increase in investments in and advances to unconsolidated subsidiaries and associated companies | (3,685) | |
| Payments for acquisition of investment securities | (19,287) | (26,016) |
| Proceeds from sales of investment securities | 5 | 19 |
| Other—net | (5,873) | (2,561) |
| Net cash used in investing activities | (99,302) | (76,428) |
| **Financing activities:** | | |
| Net increase (decrease) in short-term borrowings | 66,728 | (242,987) |
| Increase in long-term debt | 11,260 | 164,683 |
| Repayments of long-term debt | (13,660) | (18,126) |
| Payments of cash dividends | (11,097) | (9,233) |
| Proceeds from issuance of new shares | | 113,314 |
| Other—net | (4,849) | (4,284) |
| Net cash provided by financing activities | 48,382 | 3,367 |
| **Effect of exchange rate changes on cash and cash equivalents** | (17,394) | (2,459) |
| **Net (decrease) increase in cash and cash equivalents** | (6,076) | 27,809 |
| **Effect of change of the fiscal year-end of consolidated subsidiaries** | (85) | 16 |
| **Cash and cash equivalents, beginning of year** | 110,484 | 82,659 |
| **Cash and cash equivalents, end of year** | ¥104,323 | ¥110,484 |

See notes to consolidated financial statements.

## 1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements of Daikin Industries, Ltd. (the "Company") have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Act and its related accounting regulations and in conformity with accounting principles generally accepted in Japan (the "Japanese GAAP"), which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

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.

Inappropriate accounting practices were performed by front-loaded recording of sales and work-in-process installations in the Company's After Sales Service Division and certain consolidated subsidiaries. As a result of impartial investigation, the Company restated the 2008 consolidated financial statements.

The impact of the restatement on the 2008 consolidated financial statements is as follows:

| | Millions of yen | | |
|---|---|---|---|
| | As Previously Reported (A) | As Restated (B) | Restatement (B–A) |
| March 31, 2008: | | | |
| Net sales | ¥1,290,893 | ¥1,291,081 | ¥ 188 |
| Operating income | 128,497 | 128,098 | (399) |
| Income before income taxes and minority interests | 118,535 | 118,136 | (399) |
| Net income | 75,224 | 74,822 | (402) |
| Total assets | 1,213,649 | 1,210,094 | (3,555) |
| Total equity | 563,557 | 559,987 | (3,570) |
| April 1, 2007: | | | |
| Retained earnings | ¥ 289,106 | ¥ 285,938 | ¥(3,168) |
| Total equity | 413,121 | 409,953 | (3,168) |

In addition, certain reclassifications have been made in the 2008 consolidated financial statements to conform to the classification used in 2009.

## 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 or accounted for using the equity method, respectively, the effect on the accompanying consolidated financial statements would not have been material.

For the year ended March 31, 2009, the Company consolidated the operating results of a consolidated subsidiary, Daikin Sweden AB for the 15-month period ended March 31, 2009, because that subsidiary changed its fiscal year-end from December 31 to March 31.

For the year ended March 31, 2008, the Company consolidated the operating results of a consolidated subsidiary, Daikin Airconditioning Netherlands, for the 15-month period ended March 31, 2008, because that subsidiary changed its fiscal year-end from December 31 to March 31.

The Company included the subsidiaries' operating results for the 12-month period in the consolidated statements of income, and included their operating results for the 3-month period in the consolidated statements of changes in equity as effect of change of the fiscal year-end of consolidated subsidiaries.

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 being 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.

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

In May 2006, the Accounting Standards Board of Japan (the "ASBJ") issued ASBJ Practical Issues Task Force (PITF) No. 18, "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements". PITF No. 18 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 of America 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) scheduled amortization of actuarial gain or loss of pensions that has been directly recorded in the equity; 3) expensing capitalized development costs of research and development; 4) cancellation of the fair value model accounting for property, plant and equipment and investment properties and incorporation of the cost model accounting; 5) recording the prior years' effects of changes in accounting policies in the income statement where retrospective adjustments to financial statements have been incorporated; and 6) exclusion of minority interests from net income, if contained. PITF No. 18 was effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted.

The Group applied this accounting standard effective April 1, 2008. The effect of this change was to decrease operating income by approximately ¥2,166 million and income before income taxes and minority interests by approximately ¥672 million. In addition, the Group adjusted the beginning balance of retained earnings at April 1, 2008 by approximately ¥4,750 million as if this accounting standard had been retrospectively applied.

**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 3 months of the date of acquisition.

Marketable debt securities that mature or become due in more than 3 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**

Prior to April 1, 2008, inventories of the Company and its consolidated domestic subsidiaries were stated at cost, determined by the average method. Inventories of consolidated foreign subsidiaries were principally stated at the lower of cost, determined by the average method, or market.

In July 2006, the ASBJ issued ASBJ Statement No. 9, "Accounting Standard for Measurement of Inventories". 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. The standard was effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted.

The Group applied this new accounting standard for measurement of inventories effective April 1, 2008. The effect of this change was to decrease operating income and income before income taxes and minority interests by ¥4,229 million.

**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. 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.

Property, plant and equipment acquired on and after April 1, 2007 by the Company and its consolidated domestic subsidiaries are depreciated by the declining-balance method in accordance with the revised corporate tax law, which was effective on and after April 1, 2007. The effect of this treatment was to decrease operating income and income before income taxes and minority interests for the year ended March 31, 2008 by ¥733 million.

Property, plant and equipment of the Company and its consolidated domestic subsidiaries had been depreciated up to 95% of acquisition cost with 5% of residual value carried until the fiscal year ended March 31, 2007. However, such 5% portion of property, plant and equipment is systematically amortized over 5 years starting in the following year in which the carrying value of property, plant and equipment reaches 5% of the acquisition cost in accordance with the revised corporate tax law. The effect of this treatment was to decrease operating income and income before income taxes and minority interests for the year ended March 31, 2008 by ¥1,171 million.

The range of useful lives is from 15 to 50 years for buildings and structures, from 5 to 15 years for machinery and equipment.

**Long-Lived Assets**

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.

**Leases**

In March 2007, the ASBJ issued ASBJ Statement No. 13, "Accounting Standard for Lease Transactions", which revised the previous accounting standard for lease transactions issued in June 1993. The revised accounting standard for lease transactions was 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.

Under the previous accounting standard, finance lease transactions that deem to transfer ownership of the leased property to the lessee were to be capitalized. However, other finance lease transactions were 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 to recognize lease assets and lease obligations in the balance sheet. In addition, the accounting standard permits lease transactions which existed at the transition date and do not transfer ownership of the leased property to the lessee to be accounted for as operating lease transactions.

The Company and its consolidated domestic subsidiaries applied the revised accounting standard effective April 1, 2008. In addition, the Company and its consolidated domestic subsidiaries accounted for leases which existed at the transition date and do not transfer ownership of the leased property to the lessee as operating lease transactions. The effect of this change to operating income and income before income taxes and minority interests was minor.

All other leases are accounted for as operating leases.

**Investment Securities**

Under Japanese accounting standards 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.

**Stock Issue Costs**

Stock issue costs are charged to income as incurred.

**Employees' Retirement Benefits**

The Company and its consolidated domestic subsidiaries have non-contributory funded pension plans 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. Some foreign subsidiaries have pension plans.

Based on an agreement between labor and management in October 2008, certain of the Company's consolidated subsidiaries implemented a defined benefit pension plan and a defined contribution pension plan effective January 1, 2009, and then terminated the former qualified defined benefit pension plan. The effect of this transfer was to decrease income before income taxes and minority interests by ¥1,222 million and was recorded as a loss on termination of the defined benefit pension plan in the consolidated statements of income for the year ended March 31, 2009.

**Stock Options**

The ASBJ issued ASBJ Statement No. 8, "Accounting Standard for Stock Options" and related guidance 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.

The Company has applied this new accounting standard for stock options to those granted on and after May 1, 2006.

**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**

Bonuses to directors and corporate auditors are accrued at the year-end to which such bonuses are attributable.

**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. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. 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.

The Group uses mainly interest rate swaps and interest rate options to manage its exposures to fluctuations in interest rates.

The Group uses 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 are recognized and included in interest expense or income.

**Amounts per Common Share**

Basic net income per common 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 at the beginning of the year (or at the time of issuance).

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.

**New Accounting Pronouncements**

**Business Combinations**

On December 26, 2008, the ASBJ issued a revised accounting standard for business combinations, ASBJ Statement No. 21, "Accounting Standard for Business Combinations". Major accounting changes under the revised accounting standard are as follows:

(1) The current accounting standard for business combinations allows companies to apply the pooling of interests method of accounting when certain specific criteria are met such that the business combination is essentially regarded as a uniting-of-interests. The revised standard requires to account for such business combination by the purchase method and the pooling of interests method of accounting is no longer allowed.

(2) The current accounting standard accounts for the research and development costs to be charged to income as incurred. Under the revised standard, in-process research and development acquired in a business combination is capitalized as an intangible asset.

(3) The current accounting standard accounts for a bargain purchase gain (negative goodwill) to be systematically amortized within 20 years. Under the revised standard, the acquirer recognizes a bargain purchase gain in profit or loss on the acquisition date after reassessing whether it has correctly identified all of the assets acquired and all of the liabilities assumed with a review of such procedures used.

This standard is applicable to business combinations undertaken on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or after April 1, 2009.

**Unification of Accounting Policies Applied to Foreign Associated Companies for the Equity Method**

The current accounting standard requires unification of accounting policies within the consolidated group. However, the current guidance allows application of the equity method to the financial statements of foreign associated companies which have been prepared in accordance with generally accepted accounting principles in their respective jurisdictions without unification of accounting policies.

On December 26, 2008, the ASBJ issued ASBJ Statement No. 16 (Revised 2008), "Revised Accounting Standard for Equity Method of Accounting for Investments". The new standard requires adjustments to be made to conform the associate's accounting policies for similar transactions and events under similar circumstances to those of the parent company when the associate's financial statements are used in applying the equity method unless it is impractible to determine adjustments. In addition, financial statements prepared by foreign associated companies in accordance with either International Financial Reporting Standards or the generally accepted accounting principles in the United States tentatively may be used in applying the equity method if the following items are adjusted so that net income is accounted for in accordance with Japanese GAAP unless they are not material: 1) amortization of goodwill; 2) scheduled amortization of actuarial gain or loss of pensions that has been directly recorded in the equity; 3) expensing capitalized development costs of research and development; 4) cancellation of the fair value model accounting for property, plant, and equipment and investment properties and incorporation of the cost model accounting; 5) recording the prior years' effects of changes in accounting policies in the income statement where retrospective adjustments to the financial statements have been incorporated; and 6) exclusion of minority interests from net income, if contained.

This standard is applicable to equity method accounting for investments on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or after April 1, 2009.

**Asset Retirement Obligations**

On March 31, 2008, the ASBJ published a new accounting standard for asset retirement obligations, ASBJ Statement No. 18 "Accounting Standard for Asset Retirement Obligations" and ASBJ Guidance No. 21 "Guidance on Accounting Standard for Asset Retirement Obligations". Under this accounting standard, an asset retirement obligation is defined as a legal obligation imposed either by law or contract that results from the acquisition, construction, development and the normal operation of a tangible fixed asset and is associated with the retirement of such tangible fixed asset.

The asset retirement obligation is recognized as the sum of the discounted cash flows required for the future asset retirement and is recorded in the period in which the obligation is incurred if a reasonable estimate can be made. If a reasonable estimate of the asset retirement obligation cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when a reasonable estimate of asset retirement obligation can be made. Upon initial recognition of a liability for an asset retirement obligation, an asset retirement cost is capitalized by increasing the carrying amount of the related fixed asset by the amount of the liability. The asset retirement cost is subsequently allocated to expense through depreciation over the remaining useful life of the asset. Over time, the liability is accreted to its present value each period. Any subsequent revisions to the timing or the amount of the original estimate of undiscounted cash flows are reflected as an increase or a decrease in the carrying amount of the liability and the capitalized amount of the related asset retirement cost. This standard is effective for fiscal years beginning on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or before March 31, 2010.

### Measurement of Inventories

On September 26, 2008, the ASBJ issued ASBJ Statement No. 9 (revised 2008), "Accounting Standard for Measurement of Inventories". Under this accounting standard, the Last-In, First-Out (LIFO) method is no longer permitted. This standard is applicable for fiscal years beginning on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or before March 31, 2010.

### Construction Contracts

Under the current Japanese GAAP, either the completed-contract method or the percentage-of-completion method is permitted to account for construction contracts. In December 2007, the ASBJ issued a new accounting standard for construction contracts. Under this new accounting standard, the construction revenue and construction costs should be recognized by the percentage-of-completion method, if the outcome of a construction contract can be estimated reliably. When total construction revenue, total construction costs and the stage of completion of the contract at the balance sheet date can be reliably measured, the outcome of a construction contract can be estimated reliably. If the outcome of a construction contract cannot be reliably estimated, the completed-contract method shall be applied. When it is probable that total construction costs will exceed total construction revenue, an estimated loss on the contract should be immediately recognized by providing for loss on construction contracts. This standard is applicable to construction contracts and software development contracts and effective for fiscal years beginning on or after April 1, 2009 with early adoption permitted for fiscal years beginning on or before March 31, 2009 but after December 27, 2007.

## 3. Inventories

Inventories at March 31, 2009 and 2008 consisted of the following:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Finished products and merchandise | **¥133,741** | ¥147,315 |
| Semi-finished products and work-in-process | **44,451** | 50,818 |
| Raw materials and supplies | **38,453** | 38,421 |
| Total | **¥216,645** | ¥236,554 |

## 4. Investment Securities

The acquisition costs and aggregate fair values of marketable available-for-sale securities included in investment securities at March 31, 2009 and 2008 were as follows:

| | Millions of yen | | | |
|---|---|---|---|---|
| | **2009** | | | |
| | Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| Securities classified as available-for-sale: | | | | |
| Equity securities | **¥106,638** | **¥8,466** | **¥(34,777)** | **¥80,327** |
| Other | **503** | | **(138)** | **365** |
| Total | **¥107,141** | **¥8,466** | **¥(34,915)** | **¥80,692** |

| | Millions of yen | | | |
|---|---|---|---|---|
| | 2008 | | | |
| | Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| Securities classified as available-for-sale: | | | | |
| Equity securities | ¥95,085 | ¥23,011 | ¥(6,082) | ¥112,014 |
| Other | 504 | 118 | (31) | 591 |
| Total | ¥95,589 | ¥23,129 | ¥(6,113) | ¥112,605 |

Available-for-sale securities whose fair value was not readily determinable as of March 31, 2009 and 2008 were as follows:

| | Millions of yen | |
|---|---|---|
| | Carrying Amount | |
| | **2009** | 2008 |
| Available-for-sale: | | |
| Equity securities | **¥7,200** | ¥2,150 |
| Other | **1,580** | 1,469 |
| Total | **¥8,780** | ¥3,619 |

Proceeds from sales of available-for-sale securities for the years ended March 31, 2009 and 2008 were ¥5 million and ¥19 million, respectively. Gross realized gains on these sales principally computed on the moving average cost basis were ¥3 million and ¥15 million for the years ended March 31, 2009 and 2008, respectively. Write-down amounts of marketable available-for-sale securities were ¥2,633 million and ¥2,407 million for the years ended March 31, 2009 and 2008, respectively.

The carrying values of debt securities by contractual maturities for securities classified as available-for-sale at March 31, 2009 are as follows:

| | Millions of yen |
|---|---|
| | Available-for-Sale |
| Due in one year or less | ¥ |
| Due in one to five years | 100 |
| Due in five to ten years | 100 |
| Due after ten years | |
| Total | ¥200 |

## 5. Goodwill

Goodwill at March 31, 2009 and 2008 consisted of the following:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Consolidation goodwill | **¥192,295** | ¥199,828 |
| Other | **1,110** | 906 |
| Total | **¥193,405** | ¥200,734 |

Amortization of goodwill was ¥12,120 million and ¥12,348 million for the years ended March 31, 2009 and 2008, respectively.

## 6. Related Party Transactions

Receivables and payables, with respect to transactions with unconsolidated subsidiaries and associated companies at March 31, 2009 and 2008 were as follows:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Trade notes and accounts receivable | **¥2,032** | ¥1,489 |
| Trade notes and accounts payable | **565** | 691 |

Sales to and purchases from unconsolidated subsidiaries and associated companies for the years ended March 31, 2009 and 2008 were as follows:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Sales | **¥15,887** | ¥15,391 |
| Purchases | **10,673** | 10,195 |

On October 17, 2006, the ASBJ issued ASBJ Statement No. 11, “Accounting Standard for Related Party Disclosures” and its related guidance. The new accounting standard 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.

The Group applied this new accounting standard effective April 1, 2008. As a result, transactions between the Company’s consolidated subsidiaries and related individuals were newly disclosed for the year ended March 31, 2009.

Material transactions and balances with related individuals for the years ended March 31, 2009 and 2008 were as follows:

**(1) 2009**

(a) The Company

| | | | Millions of yen | | | |
|---|---|---|---|---|---|---|
| | | | Transactions | | Resulting Account Balances | |
| Name | Description of Post | Ownership of the Company (%) | Description of Transaction | 2009 | Account | 2009 |
| Chiyono Terada | Outside Director/CEO and President of Art Corporation | 0.00 | Commission of move business and delivery business | **¥217** | Other current liabilities | **¥33** |

(b) The Company's consolidated subsidiaries

| | | | Millions of yen | | | |
|---|---|---|---|---|---|---|
| | | | Transactions | | Resulting Account Balances | |
| Name | Description of Post | Ownership of the Company (%) | Description of Transaction | 2009 | Account | 2009 |
| Chiyono Terada | Outside Director/CEO and President of Art Corporation | 0.00 | Commission of move business and delivery business | **¥40** | Other current liabilities | **¥ 3** |
| | | | Sales of products and other | **79** | Accounts receivable | **¥14** |

**(2) 2008**

| | | | Millions of yen | | | |
|---|---|---|---|---|---|---|
| | | | Transactions | | Resulting Account Balances | |
| Name | Description of Post | Ownership of the Company (%) | Description of Transaction | 2008 | Account | 2008 |
| 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 | ¥ 5 | | |
| | Director General of Kansai Philharmonic Orchestra | | Donation and support money to Kansai Philharmonic Orchestra | 49 | | |
| Chiyono Terada | Outside Director/CEO and President of Art Corporation | 0.00 | Commission of move business and delivery business | 45 | Other current liabilities | ¥2 |

## 7. Short-Term Borrowings and Long-Term Debt

Short-term borrowings of the Group at March 31, 2009 and 2008 consisted of the following:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Bank overdrafts and notes to banks | **¥ 74,880** | ¥ 73,951 |
| Commercial paper | **120,000** | 58,000 |
| Total | **¥194,880** | ¥131,951 |

Unused short-term bank credit lines were ¥75,000 million at March 31, 2009. Weighted average interest rates of bank overdrafts and notes to banks at March 31, 2009 and 2008 were 1.51% and 3.06%, respectively.

Weighted average interest rates of commercial paper at March 31, 2009 and 2008 were 0.46% and 0.65%, respectively.

Long-term debt at March 31, 2009 and 2008 consisted of the following:

| | Millions of yen | |
|---|---|---|
| | 2009 | 2008 |
| 0.82% unsecured bonds, due October 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%, due through 2012 | 1,500 | 2,000 |
| Collateralized loans from banks and others, payable in foreign currencies, with interest ranging from 4.00% to 7.63% (2009), and interest 4.00% (2008), due through 2012 | 1,012 | 124 |
| Collateralized loans from banks with: | | |
| Floating interest at 1.14% (2009), and ranging from 1.45% to 1.47% (2008), due through 2010 | 2,290 | 6,190 |
| Unsecured loans from banks and others, payable in foreign currencies, with interest ranging from 2.00% to 7.91% (2009), and from 1.59% to 6.46% (2008), due through 2014 | 21,317 | 22,335 |
| Unsecured loans from banks and others with interest ranging from 0.71% to 6.10% (2009), and from 0.91% to 6.10% (2008), due through 2027 | 172,878 | 173,098 |
| Total | 220,197 | 224,947 |
| Less current portion | (29,418) | (8,781) |
| Long-term debt, less current portion | ¥190,779 | ¥216,166 |

Annual maturities of long-term debt outstanding at March 31, 2009 were as follows:

| Years ending March 31, | Millions of yen |
|---|---|
| 2010 | ¥ 29,418 |
| 2011 | 13,277 |
| 2012 | 8,333 |
| 2013 | 55,127 |
| 2014 | 8,966 |
| 2015 and thereafter | 105,076 |
| Total | ¥220,197 |

At March 31, 2009, property, plant and equipment, trade accounts receivables, inventories and prepaid expense and other current assets with a book value of ¥46,618 million, ¥9,036 million, ¥5,315 million and ¥833 million, respectively, were pledged as collateral for short-term borrowings and long-term debt, and short-term investments with a book value of ¥900 million were pledged as collateral for a supplier's borrowings of ¥637 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 these rights with respect to debt of the Group.

## 8. 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 October 2008, certain of the Company's consolidated subsidiaries implemented a defined benefit pension plan and a defined contribution pension plan effective January 1, 2009, and then terminated the former qualified defined benefit pension plan.

The liabilities for employees' retirement benefits at March 31, 2009 and 2008 consisted of the following:

| | Millions of yen | |
|---|---|---|
| | 2009 | 2008 |
| Projected benefit obligation | ¥64,422 | ¥74,896 |
| Fair value of plan assets | (59,368) | (80,619) |
| Unrecognized prior service cost | 280 | 219 |
| Unrecognized actuarial gain | (15,502) | (3,676) |
| Net asset | (10,168) | (9,180) |
| Prepaid pension cost | (14,107) | (13,471) |
| Liabilities for retirement benefits | ¥ 3,939 | ¥ 4,291 |

The components of net periodic benefit costs for the years ended March 31, 2009 and 2008 were as follows:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Service cost | **¥3,071** | ¥2,984 |
| Interest cost | **2,491** | 2,491 |
| Expected return on plan assets | **(2,702)** | (3,136) |
| Amortization of prior service cost | **(25)** | (31) |
| Recognized actuarial loss (gain) | **588** | (309) |
| Net periodic benefit costs | **3,423** | 1,999 |
| Loss on transfer to a defined contribution pension plan | **1,222** | |
| Contribution to defined contribution pension plan and other | **2,287** | 1,888 |
| Total | **¥6,932** | ¥3,887 |

Assumptions used for the years ended March 31, 2009 and 2008 were set forth as follows:

| | **2009** | 2008 |
|---|---|---|
| Discount rate | **Mainly 2.0%** | Mainly 2.5% |
| Expected rate of return on plan assets | **Mainly 2.5%** | Mainly 2.5% |
| Amortization period of prior service cost | **Mainly 10 years** | 10 years |
| Recognition period of actuarial gain/loss | **Mainly 10 years** | Mainly 10 years |

## 9. Equity

Since May 1, 2006, Japanese companies have been subject to the Companies Act of Japan (the “Companies Act”). The significant provisions in the Companies Act that affect financial and accounting matters are summarized below:

### (a) Dividends

Under the Companies Act, 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) at any time during the fiscal year if the company has prescribed so in its articles of incorporation. However, the Company cannot do so because it does not meet all the above criteria.

The Companies Act 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 Companies Act 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.

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

The Companies Act 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 Companies Act, the total amount of additional paid-in capital and the legal reserve may be reversed without limitation. The Companies Act 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.

### (c) Treasury Stock and Treasury Stock Acquisition Rights

The Companies Act 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 Companies Act, stock acquisition rights are presented as a separate component of equity.

The Companies Act 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.

On June 22, 2007, the Company issued and publicly offered 25,500 thousand shares at ¥3,891 per share. The amount of the issuance was ¥99,230 million in total, ¥49,615 million of which was recorded in common stock and the remaining ¥49,615 million was recorded in capital surplus.

On July 23, 2007, the Company issued and allocated 3,800 thousand shares to a third party at ¥3,891 per share. The amount of the issuance was ¥14,788 million in total, ¥7,394 million of which was recorded in common stock and the remaining ¥7,394 million was recorded in capital surplus.

## 10. Stock Option

The stock option outstanding for the year ended March 31, 2009 was as follows:

| Stock Option | Persons Granted | Number of Options Granted | Date of Grant | Exercise Price | Exercise Period |
|---|---|---|---|---|---|
| 2002 Stock Option | 20 directors<br>19 employees | 118,000 shares | 2002.7.26 | ¥2,330 | From July 1, 2004<br>to June 30, 2008 |
| 2003 Stock Option | 20 directors<br>19 employees | 118,000 shares | 2003.7.30 | ¥2,405 | From July 1, 2005<br>to June 30, 2009 |
| 2004 Stock Option | 9 directors<br>40 employees | 144,000 shares | 2004.7.27 | ¥2,957 | From July 1, 2006<br>to June 30, 2010 |
| 2005 Stock Option | 9 directors<br>44 employees | 153,000 shares | 2005.7.29 | ¥2,852 | From July 1, 2007<br>to June 30, 2011 |
| 2006 Stock Option | 9 directors<br>44 employees | 298,000 shares | 2006.7.18 | ¥3,790 | From July 19, 2008<br>to July 18, 2012 |
| 2007 Stock Option | 9 directors<br>42 employees | 292,000 shares | 2007.7.17 | ¥4,640 | From July 18, 2009<br>to July 17, 2013 |
| 2008 Stock Option | 8 directors<br>44 employees | 308,000 shares | 2008.7.14 | ¥5,924 | From July 18, 2010<br>to July 14, 2014 |

The stock option activity was as follows:

| | 2001 Stock Option | 2002 Stock Option | 2003 Stock Option | 2004 Stock Option | 2005 Stock Option | 2006 Stock Option | 2007 Stock Option | 2008 Stock Option |
|---|---|---|---|---|---|---|---|---|
| | (Shares) | | | | | | | |
| **For the year ended March 31, 2008** | | | | | | | | |
| Vested | | | | | | | | |
| March 31, 2007—Outstanding | 27,300 | 21,000 | 56,000 | 128,000 | 151,000 | 298,000 | | |
| Granted | | | | | | | 292,000 | |
| Exercised | 27,300 | 6,000 | 21,000 | 28,000 | 27,500 | | | |
| Canceled | | | | | | | | |
| March 31, 2008—Outstanding | | 15,000 | 35,000 | 100,000 | 123,500 | 298,000 | 292,000 | |
| **For the year ended March 31, 2009** | | | | | | | | |
| Vested | | | | | | | | |
| March 31, 2008—Outstanding | | 15,000 | 35,000 | 100,000 | 123,500 | 298,000 | | |
| Granted | | | | | | | 292,000 | 308,000 |
| Exercised | | 15,000 | 13,000 | 10,000 | 22,200 | 6,000 | | |
| Canceled | | | | | | | | |
| March 31, 2009—Outstanding | | | 22,000 | 90,000 | 101,300 | 292,000 | 292,000 | 308,000 |
| Exercise price | ¥2,451 | ¥2,330 | ¥2,405 | ¥2,957 | ¥2,852 | ¥3,790 | ¥4,640 | ¥5,924 |
| Average stock price at exercise | ¥4,307 | ¥5,160 | ¥5,270 | ¥5,323 | ¥4,998 | ¥4,842 | | |
| Fair value price at grant date | | | | | | ¥ 736 | ¥1,035 | ¥ 803 |

The assumptions used to measure fair value of 2008 Stock Option

| | |
|---|---|
| Estimate method: | Black-Scholes option pricing model |
| Volatility of stock price: | 32.9% |
| Estimated remaining outstanding period: | 4 years |
| Estimated dividend: | ¥38 per share |
| Interest rate with risk free: | 1.0% |

## 11. 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, 2009 and 2008.

The tax effects of significant temporary differences and tax loss carryforwards which resulted in deferred tax assets and liabilities at March 31, 2009 and 2008 were as follows:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Deferred tax assets: | | |
| Unrealized loss on available-for-sale securities | **¥11,067** | |
| Inventories | **8,252** | ¥11,206 |
| Tax loss carryforwards | **6,982** | 1,685 |
| Warranty reserve | **4,812** | 5,379 |
| Software and other assets | **4,646** | 4,982 |
| Accrued bonus | **3,083** | 3,428 |
| Investment securities | **2,565** | 1,179 |
| Long-term account payable | **2,273** | 2,891 |
| Account payable other | **1,804** | 1,470 |
| Liabilities for retirement benefits | **1,399** | 1,955 |
| Allowance for doubtful receivables | **968** | 859 |
| Property, plant and equipment | **517** | 888 |
| Business tax payable | | 1,052 |
| Foreign tax credit | | 983 |
| Other | **7,836** | 5,106 |
| Less valuation allowance | **(8,365)** | (2,103) |
| Total deferred tax assets | **¥47,839** | ¥40,960 |
| Deferred tax liabilities: | | |
| Undistributed earnings of consolidated subsidiaries | **¥ 9,250** | ¥11,790 |
| Prepaid pension cost | **5,738** | 6,006 |
| Deferred gains on sales of property | **2,202** | 2,174 |
| Unrealized gain on available-for-sale securities | | 6,917 |
| Other | **3,175** | 4,137 |
| Total deferred tax liabilities | **¥20,365** | ¥31,024 |
| Net deferred tax assets | **¥27,474** | ¥ 9,936 |

At March 31, 2009, the Company and certain consolidated subsidiaries have deferred tax assets aggregating ¥6,982 million for tax loss carryforwards which are available to be offset against taxable income of such companies in future years. These tax loss carryforwards, if not utilized, will expire mainly in 2015 and thereafter.

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 years ended March 31, 2009 and 2008 was as follows:

| | **2009** | 2008 |
|---|---|---|
| Normal effective statutory income tax rate | **40.6%** | 40.6% |
| Difference in foreign subsidiaries' tax rate | **(21.6)** | (11.0) |
| Unrecognized tax effect on foreign income tax credit | **12.7** | |
| Valuation allowance | **10.1** | |
| Amortization of goodwill | **9.2** | 4.0 |
| Undistributed earnings of consolidated subsidiaries | **(5.6)** | |
| Income taxes—prior years | | 2.9 |
| Elimination of exchange losses from reorganization of consolidated subsidiaries | | (2.7) |
| Tax credit for research and development cost | | (1.8) |
| Write-down of investment securities | | 0.8 |
| Other—net | **0.7** | 1.2 |
| Actual effective income tax rate | **46.1%** | 34.0% |

Additional tax amounts estimated to result from the transfer pricing taxation assessment regarding the transaction between the Company and its foreign subsidiary is presented as income taxes—prior years in the consolidated statements of income for the year ended March 31, 2008. On June 26, 2008, the Company received a transfer pricing taxation assessment, however, the difference from the estimated amount was minor. The Company has taken appropriate action on the assessment.

## 12. Supplemental Cash Flow Information

The Company acquired certain companies during the year ended March 31, 2009. ROTEX Heating Systems GmbH and its 9 subsidiaries were the major component of the acquisitions.

A reconciliation between cash paid for the shares of ROTEX Heating Systems GmbH and its 9 subsidiaries and payment for the acquisition of these newly consolidated subsidiaries, net of cash and cash equivalents acquired, was as follows:

| | Millions of yen |
|---|---|
| | **2009** |
| Assets | **¥9,914** |
| Goodwill | **4,287** |
| Liabilities | **(6,753)** |
| Cash paid for the capital | **7,448** |
| Cash and cash equivalents of consolidated subsidiaries | **(209)** |
| Payment for acquisition of shares of newly consolidated subsidiaries, net of cash and cash equivalents acquired | **¥7,239** |

## 13. Research and Development Costs

Research and development costs were ¥30,535 million and ¥32,075 million for the years ended March 31, 2009 and 2008, respectively.

## 14. Leases

The Group leases certain computer equipment and other assets.

Obligations under finance leases and future minimum payments under noncancelable operating leases were as follows:

| | Millions of yen | |
|---|---|---|
| | **2009** | |
| | Finance Leases | Operating Leases |
| Due within one year | **¥1,237** | **¥1,080** |
| Due after one year | **1,606** | **6,872** |
| Total | **¥2,843** | **¥7,952** |

### Pro Forma Information for the Year Ended March 31, 2009

As discussed in Note 2, the Company and its domestic consolidated subsidiaries account for leases which existed at the transition date and do not transfer ownership of the leased property to the lessee as operating lease transactions. Pro forma information of such leases existing at the transition date, such as acquisition cost, accumulated depreciation, obligations under finance leases and depreciation expense on an “as if capitalized” basis for the year ended March 31, 2009 was as follows:

| | Millions of yen | | |
|---|---|---|---|
| **As of March 31, 2009** | Furniture and Fixtures | Others | Total |
| Acquisition cost | **¥3,985** | **¥1,902** | **¥5,887** |
| Accumulated depreciation | **2,585** | **1,118** | **3,703** |
| Net leased property | **¥1,400** | **¥ 784** | **¥2,184** |

Obligations under finance leases:

| | Millions of yen |
|---|---|
| | **2009** |
| Due within one year | **¥1,022** |
| Due after one year | **1,162** |
| Total | **¥2,184** |

The amounts of acquisition cost and obligations under finance leases include the imputed interest expense portion.

Lease payments and depreciation expense under finance leases:

| | Millions of yen |
|---|---|
| | **2009** |
| Lease payments | **¥1,799** |
| Depreciation expense | **1,799** |

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

### Pro Forma Information for the Year Ended March 31, 2008

Pro forma information of leased property such as acquisition cost, accumulated depreciation, obligations under finance lease and depreciation expense that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the year ended March 31, 2008 was as follows:

| | Millions of yen | | |
|---|---|---|---|
| As of March 31, 2008 | Furniture and Fixtures | Others | Total |
| Acquisition cost | ¥5,822 | ¥2,144 | ¥7,966 |
| Accumulated depreciation | 3,004 | 1,003 | 4,007 |
| Net leased property | ¥2,818 | ¥1,141 | ¥3,959 |

Obligations under finance leases:

| | Millions of yen |
|---|---|
| | 2008 |
| Due within one year | ¥1,787 |
| Due after one year | 2,172 |
| Total | ¥3,959 |

Lease payments and depreciation expense under finance leases:

| | Millions of yen |
|---|---|
| | 2008 |
| Lease payments | ¥2,201 |
| Depreciation expense | 2,201 |

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

## 15. 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 substantially 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 price 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, 2009 and 2008 were as follows:

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2009 | | | 2008 | | |
| | Contract Amount | Fair Value | Unrealized Gain (Loss) | Contract Amount | Fair Value | Unrealized Gain (Loss) |
| Forward exchange contracts: | | | | | | |
| Selling: GBP | **¥ 4,035** | **¥ 4,189** | **¥(154)** | ¥ 4,514 | ¥ 4,273 | ¥241 |
| EUR | **14,644** | **14,721** | **(77)** | 30,822 | 31,046 | (224) |
| USD | **8,820** | **8,967** | **(147)** | 9,540 | 9,481 | 59 |
| ZAR | **1,638** | **1,671** | **(33)** | 2,033 | 1,890 | 143 |
| CZK | **7,997** | **8,103** | **(106)** | 2,290 | 2,418 | (128) |
| PLN | **521** | **516** | **5** | 528 | 539 | (11) |
| MYR | **475** | **494** | **(19)** | 923 | 927 | (4) |
| AUD | **2,444** | **2,536** | **(92)** | 1,834 | 1,791 | 43 |
| HKD | **520** | **515** | **5** | 193 | 177 | 16 |
| SGD | **620** | **621** | **(1)** | 1,234 | 1,236 | (2) |
| THB | **330** | **332** | **(2)** | | | |
| CAD | **122** | **149** | **(27)** | | | |
| INR | **277** | **276** | **1** | | | |
| Buying: EUR | **125** | **128** | **3** | | | |
| CZK | **192** | **202** | **10** | | | |
| USD | **295** | **305** | **10** | | | |
| Currency swaps: | | | | | | |
| Receive JPY/Pay HKD | **330** | **13** | **13** | 413 | (2) | (2) |
| Receive JPY/Pay USD | **962** | **16** | **16** | 889 | 74 | 74 |
| Total | **¥44,347** | **¥43,754** | **¥(595)** | ¥55,213 | ¥53,850 | ¥205 |

| | Millions of yen | | | | | |
|---|---|---|---|---|---|---|
| | 2009 | | | 2008 | | |
| | Contract Amount | Fair Value | Unrealized Gain (Loss) | Contract Amount | Fair Value | Unrealized Gain (Loss) |
| Commodity future contracts: | | | | | | |
| Metal | | | | | | |
| Buying | **¥2,124** | **¥989** | **¥(1,135)** | ¥2,280 | ¥2,149 | ¥(131) |

Information related to derivative contracts that qualify for hedge accounting and forward contracts that are assigned to associated assets and liabilities and recorded in the consolidated balance sheets at March 31, 2009 and 2008 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.

## 16. Commitments and Contingent Liabilities

Commitments for capital expenditures outstanding at March 31, 2009 totaled ¥15,631 million.

Guarantees of bank loans and items of a similar nature at March 31, 2009 were ¥1,264 million.

## 17. Net Income Per Share

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the years ended March 31, 2009 and 2008 was as follows:

| | Millions of yen | Thousands of shares | Yen |
|---|---|---|---|
| **For the year ended March 31, 2009** | Net Income | Weighted Average Shares | EPS |
| Basic EPS | | | |
| Net income available to common shareholders | **¥21,755** | **291,971** | **¥ 74.51** |
| Effect of dilutive securities | | | |
| Stock options | | **45** | |
| Diluted EPS | | | |
| Net income for computation | **¥21,755** | **292,016** | **¥ 74.50** |
| For the year ended March 31, 2008 | | | |
| Basic EPS | | | |
| Net income available to common shareholders | ¥74,822 | 285,321 | ¥262.24 |
| Effect of dilutive securities | | | |
| Stock options | | 221 | |
| Diluted EPS | | | |
| Net income for computation | ¥74,822 | 285,542 | ¥262.04 |

## 18. 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, 2009 and 2008 was as follows:

### (1) Industry Segments

#### a. Sales and Operating Income

| | Millions of yen | | | | |
|---|---|---|---|---|---|
| | **2009** | | | | |
| | Air Conditioning | Chemicals | Others | Eliminations and Corporate | Consolidated |
| Sales to customers | **¥1,059,435** | **¥101,910** | **¥41,075** | | **¥1,202,420** |
| Intersegment sales | **546** | **4,684** | **15** | **¥(5,245)** | |
| Total sales | **1,059,981** | **106,594** | **41,090** | **(5,245)** | **1,202,420** |
| Operating expenses | **988,332** | **116,103** | **41,908** | **(5,317)** | **1,141,026** |
| Operating income (loss) | **¥ 71,649** | **¥ (9,509)** | **¥ (818)** | **¥ 72** | **¥ 61,394** |

#### b. Assets, Depreciation and Capital Expenditures

| | Millions of yen | | | | |
|---|---|---|---|---|---|
| | **2009** | | | | |
| | Air Conditioning | Chemicals | Others | Eliminations and Corporate | Consolidated |
| Assets | **¥857,539** | **¥126,871** | **¥29,335** | **¥103,673** | **¥1,117,418** |
| Depreciation | **29,064** | **13,595** | **2,095** | | **44,754** |
| Capital expenditures | **47,896** | **13,300** | **2,402** | | **63,598** |

**a. Sales and Operating Income**

| | Millions of yen 2008 | | | | |
|---|---|---|---|---|---|
| | Air Conditioning | Chemicals | Others | Eliminations and Corporate | Consolidated |
| Sales to customers | ¥1,131,932 | ¥116,096 | ¥43,053 | | ¥1,291,081 |
| Intersegment sales | 507 | 3,019 | 22 | ¥(3,548) | |
| Total sales | 1,132,439 | 119,115 | 43,075 | (3,548) | 1,291,081 |
| Operating expenses | 1,008,256 | 115,623 | 42,672 | (3,568) | 1,162,983 |
| Operating income | ¥ 124,183 | ¥ 3,492 | ¥ 403 | ¥ 20 | ¥ 128,098 |

**b. Assets, Depreciation and Capital Expenditures**

| | Millions of yen 2008 | | | | |
|---|---|---|---|---|---|
| | Air Conditioning | Chemicals | Others | Eliminations and Corporate | Consolidated |
| Assets | ¥913,240 | ¥139,992 | ¥29,853 | ¥127,009 | ¥1,210,094 |
| Depreciation | 24,795 | 12,649 | 1,499 | | 38,943 |
| Capital expenditures | 35,450 | 13,945 | 2,057 | | 51,452 |

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

The effect of the application of the new accounting standard for measurement of inventories as stated in Note 2 was to decrease operating income of Air Conditioning by ¥3,202 million and to increase operating loss of chemical and Others by ¥884 million and ¥143 million, respectively, for the year ended March 31, 2009.

The effect of the Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements as stated in Note 2 was to decrease operating income of Air Conditioning by approximately ¥2,027 million and to increase operating loss of Chemicals by approximately ¥139 million for the year ended March 31, 2009.

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, 2009 and 2008 were summarized below:

| | Millions of yen **2009** | | | | | | |
|---|---|---|---|---|---|---|---|
| | Japan | Asia and Oceania | Europe | Americas | Other | Eliminations and Corporate | Consolidated |
| Sales to outside customers | **¥476,067** | **¥285,746** | **¥300,801** | **¥124,747** | **¥15,059** | | **¥1,202,420** |
| Interarea transfers | **102,838** | **84,153** | **8,998** | **9,296** | **873** | **¥(206,158)** | |
| Total sales | **578,905** | **369,899** | **309,799** | **134,043** | **15,932** | **(206,158)** | **1,202,420** |
| Operating expenses | **583,006** | **337,661** | **285,640** | **137,911** | **15,334** | **(218,526)** | **1,141,026** |
| Operating income (loss) | **¥ (4,101)** | **¥ 32,238** | **¥ 24,159** | **¥ (3,868)** | **¥ 598** | **¥ 12,368** | **¥ 61,394** |
| Assets | **¥507,388** | **¥358,151** | **¥205,505** | **¥122,774** | **¥10,251** | **¥ (86,651)** | **¥1,117,418** |

| | Millions of yen 2008 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Japan | Asia and Oceania | Europe | Americas | Other | Eliminations and Corporate | Consolidated |
| Sales to outside customers | ¥498,447 | ¥284,546 | ¥367,140 | ¥131,677 | ¥9,271 | | ¥1,291,081 |
| Interarea transfers | 156,587 | 108,990 | 7,794 | 7,727 | 21 | ¥(281,119) | |
| Total sales | 655,034 | 393,536 | 374,934 | 139,404 | 9,292 | (281,119) | 1,291,081 |
| Operating expenses | 603,500 | 353,874 | 336,777 | 138,658 | 9,111 | (278,937) | 1,162,983 |
| Operating income | ¥ 51,534 | ¥ 39,662 | ¥ 38,157 | ¥ 746 | ¥ 181 | ¥ (2,182) | ¥ 128,098 |
| Assets | ¥511,841 | ¥402,128 | ¥212,509 | ¥164,648 | ¥6,223 | ¥ (87,255) | ¥1,210,094 |

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

The effect of the application of the new accounting standard for measurement of inventories as stated Note 2 was to increase operating loss of Japan by ¥4,229 million for the year ended March 31, 2009.

The effect of the Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements as stated in Note 2 was to decrease operating income of Asia and Oceania and Europe by approximately ¥369 million and ¥1,705 million, respectively, and to increase the operating loss of Americas by approximately ¥92 million for the year ended March 31, 2009.

**(3) Sales to Foreign Customers**

Sales to foreign customers for the years ended March 31, 2009 and 2008 were as follows:

| | Millions of yen | |
|---|---|---|
| | **2009** | 2008 |
| Asia and Oceania | **¥301,832** | ¥311,399 |
| Europe | **282,434** | 354,554 |
| Americas | **134,707** | 134,210 |
| Other | **35,389** | 29,305 |
| Total sales to foreign customers | **¥754,362** | ¥829,468 |

## 19. Subsequent Events

**(1) Resolutions Approved by the Company's Shareholders at the General Shareholders' Meeting Held on June 26, 2009**

**a. Appropriation of Retained Earnings**

The shareholders approved payment of a year-end cash dividend of ¥19 per share to holders of record at March 31, 2009, totaling ¥5,546 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 ¥1,500 million) as treasury stock until the next general shareholders' meeting.

**(2) Stock Option Plan**

At the meeting of the Company's Board of Directors held on June 26, 2009, 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 294 thousand shares of the Company's common stock in the period from July 14, 2011 to July 13, 2015. 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.

Deloitte.

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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, 2009 and 2008, 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, 2009 and 2008, 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 2 to the consolidated financial statements, the Group applied the new accounting standard for measurement of inventories effective April 1, 2008.

As discussed in Note 2 to the consolidated financial statements, the Group applied the new accounting standard for unification of accounting policies applied to foreign subsidiaries for the consolidated financial statements effective April 1, 2008.

Deloitte Touche Tohmatsu

June 26, 2009

| | |
|---|---|
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| **Tokyo Office** | JR Shinagawa East Bldg., 2-18-1, Konan, Minato-ku, Tokyo 108-0075, Japan<br>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** | ¥85,032 million |
| **Number of Shares of Common Stock Issued** | 293,113 thousand |
| **Number of Shareholders** | 36,928 |
| **Major Shareholders** | Japan Trustee Services Bank, Ltd.<br>The Master Trust Bank of Japan, Ltd.<br>Panasonic Corporation<br>State Street Bank and Trust Company<br>Sumitomo Mitsui Banking Corporation<br>Trust & Custody Services Bank, Ltd.<br>Northern Trust Company<br>The Bank of Tokyo-Mitsubishi UFJ, Ltd.<br>The Bank of New York Mellon Corporation<br>Mitsui Sumitomo Insurance Co., Ltd. |
| **Number of Subsidiaries and Affiliated Companies** | Subsidiaries: 202 Affiliates: 13 |
| **Number of Employees** | 36,300 (Consolidated) |
| **Stock Exchange Listings** | Tokyo, Osaka |
| **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.<br>2-4-6, Kitahama, Chuo-ku, Osaka 541-8583, Japan |
| **Ordinary General Meeting of Shareholders** | June |
| **Auditor** | Deloitte Touche Tohmatsu |

**DAIKIN INDUSTRIES, LTD.**

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