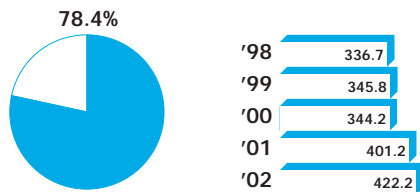


Air Conditioning

Sales (% of net sales, ¥ billion)



In fiscal 2002, ended March 31, 2002, sales in the Air Conditioning and Refrigeration Equipment Division amounted to ¥422.2 billion, a 5.2% increase compared with the previous term. The division's sales accounted for 78.4% of consolidated net sales. Operating income increased 31.8% compared with the previous term, to ¥32.2 billion, and the ratio of operating income to segment sales was 7.6%.

Although sales in Japan were virtually unchanged from the previous year, sales overseas grew at a double-digit rate.

The Japanese Market

Overview

In fiscal 2002, the Japanese economy was adversely impacted by the slowdown in the U.S. economy and the bursting of the IT bubble. These factors notwithstanding, Japan experienced its second consecutive hot summer, which helped to drive up demand for air-conditioning systems during the first half of the term. However, in the middle of August, demand began to falter due to stagnation in the domestic economy, and this trend was exacerbated by the terrorist attacks that occurred in the United States shortly thereafter. During the second half of the term, overall demand for air-conditioning systems declined compared with the previous year. In particular, sales of commercial air-conditioning systems suffered from reduced capital investment and a correction in demand, which had temporarily risen during the previous year when companies rushed to purchase air-conditioning systems prior to the enactment of the Law Concerning the Measures by Large-Scale Retail Stores for Preservation of Living Environment. In addition, sales of residential air-conditioning systems suffered from a decrease in the number of new housing starts and a change in demand,

which had temporarily risen during the previous year when companies rushed to purchase air-conditioning systems prior to the enactment of the Specified Household Appliances Recycling Law.

Despite these adverse conditions, Daikin sold more commercial air-conditioning systems and residential air-conditioning systems than it had during the previous term and achieved stronger growth than the industry average. This is attributable to the value our customers place on our comprehensive line of product and service offerings. For example, we have enhanced our air-conditioning sales network, focusing on specialized retailers, provided unique



products, including those capable of meeting the growing demand for replacement products, and implemented a service system operating 24 hours a day, 365 days a year.

In commercial air-conditioning systems, Daikin provides an array of environment-friendly commercial air-conditioning systems that facilitate energy conservation and are designed to suit virtually any market. We expanded the SUPER INVERTER SERIES, a major driver of market share expansion through the end of the previous term, by adding the SUPER INVERTER ZEAS II, featuring high user-value and enhanced performance capabilities. We succeeded in increasing our market share by focusing on the development of extremely efficient Ve-up multi-split systems for office buildings and ZEAS systems for factories that are trying to cut back on energy use.

In residential air-conditioning systems, Daikin has won praise from customers for its URURU & SALALA systems, the industry's first air-conditioning system capable of drawing moisture from the air outside to humidify air inside



without a water supply, and this was linked to an increase in the sale of residential air-conditioning systems.

During the term under review, Daikin

increased its share of the markets for residential air-conditioning systems as well as commercial air-conditioning systems. Due to favorable summer weather, Daikin's products made up a large share of sales at large-scale electronics retailers. In addition, we made strong efforts to expand sales via our outstanding sales network, which spans the entire country.

Outlook

The domestic economy is caught in a deflationary spiral, which is driving down prices, the value of assets, and overall product demand. In addition, we fear that there will be a decrease in demand, which, during fiscal 2002, benefited from an exceptionally hot summer. Thus, the air-conditioning industry is facing an uncertain future.

On the other hand, Daikin anticipates increased demand for commercial air-conditioning systems, as many companies become more attuned to environmental problems and the importance of energy conservation and will soon need to replace units purchased during the bubble era. We realize that the provision of total solutions is extremely impor-



tant and, in fiscal 2003, will strive to acquire the requisite products, consulting knowledge, and service and development systems to provide such services. For example, in February 2002, we introduced

the RAKU PITA ZEAS, a new upward-blowing external unit that can be neatly installed in front of shops facing the street or used in narrow urban spaces where conventional units cannot be installed. Daikin will supply not only hardware but also air-conditioning solutions.

There are two reasons why demand for room air-conditioning systems is not expected to increase significantly in fiscal 2003. First, many people already purchased air-conditioning systems during the summer of fiscal 2002 due to exceptionally hot weather. Second, it is not clear when the market for new housing starts will recover. Daikin will strive to expand product sales by focusing on its distinctive URURU & SALALA systems. Furthermore, with demand for residential air-conditioning systems expected to decline,

in February 2002, Daikin introduced "ecocute," a natural refrigerant for use in heat pump boilers, as part of efforts to increase sales of units for residential use.

Global Market

Overview

Despite the high growth rates seen in previous terms, growth in the global air-conditioning market tapered off during fiscal 2002. Although growth in the Chinese market remained strong, demand in the European market, which had been the major engine of growth through fiscal 2001, suffered from falling sales of IT products, climatic irregularities, the adverse effects of the terrorist attacks in the United States, and other factors. Added to this, ASEAN countries were unable to shake off the effects of economic stagnation, and price competition intensified for compact residential air-conditioning systems due to changes in the industry, particularly in China, where manufacturers are exploiting cost advantages to expand overseas at a remarkable pace.

However, looking at the industry as a whole, even in the flagging European market, growth in France, Spain, and other countries



remained steady. Demand in Australia was strong, enabling Daikin to expand sales of residential air-conditioning systems. And in China, Daikin expanded sales of

Variable Refrigerant Volume (VRV) systems and commercial air-conditioning systems for office buildings. As a result, the Company delivered on plans to expand overall sales of residential and commercial air-conditioning systems and VRV systems. In addition, in November 2001, Daikin reached a basic agreement with the Trane Company to form a comprehensive strategic alliance, thus initiating efforts to improve the Company's global performance. This alliance will help strengthen our lineup of large-scale air-conditioning systems. Taken together with our alliance with Matsushita Electric Industrial Co., Ltd. in 1999, which improved our lineup of small-scale systems, we now have a system in place that will facilitate the provision of a full lineup of air-conditioning systems, from compact to super large-scale models.

Outlook

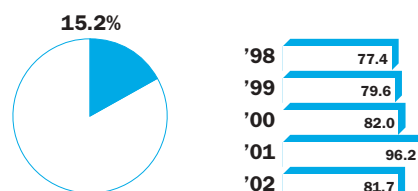
Demand for air-conditioning systems continues to grow in China, other regions of Asia, Europe, Central America, and South America, making prospects for high growth likely in these markets. During fiscal 2003, air-conditioning manufacturers from the United States and Japan as well as China, South Korea, and other countries will accelerate efforts to develop these high-growth markets, resulting in intensified competition.

In anticipation of such competition, Daikin is targeting improved competitiveness in every area of its business. Thus, it is implementing a flexible production system that is responsive to fluctuations in market demand and currency values, providing products to meet global standards and specifications, and reducing costs associated with products and manufacturing by expanding its facilities in China and Thailand. In conjunction with these efforts, Daikin is considering the establishment of manufacturing units in such emerging markets as South America and Eastern Europe to facilitate the provision of products to regional markets. With sales expansion in view, the Company is implementing policies calling for the continued expansion of its sales routes and seeking to take over existing external sales agencies to strengthen its sales systems. In accordance with our mission as a manufacturer, additional efforts will be made to continue generating demand through the provision of distinctive cutting-edge products. In addition to selling air-conditioning systems, we will provide maintenance services and take steps to expand our revenue streams through the development of related businesses dedicated to providing detailed solutions for our customers' needs.

The planned strategic alliance with the Trane Company will go into effect in fiscal 2003. We intend to use the alliance to maximize synergies, which will necessitate collaboration in the provision of superior products, strengthen our alliance on a regional basis, and take concrete steps to integrate our operations.

Chemicals

Sales (% of net sales, ¥ billion)



In fiscal 2002, sales in the Chemicals Division amounted to ¥81.7 billion, a 15.1% decrease compared with the previous term, and accounted for 15.2% of consolidated net sales. Operating income amounted to ¥9.3 billion, a 41.7% decrease, and the ratio of operating income to net sales totaled 11.4%.

Overview

In fiscal 2002, the U.S. IT bubble burst, the Japanese economy continued to stagnate, and, in September, the United States experienced a series of terrorist attacks. As a result, our operating environment underwent momentous changes at an unprecedented rate. Fiscal 2002 was the first year of our strategic management plan, "Fusion 05," which was implemented to facilitate rapid business expansion. However, although we aggressively expanded our business and achieved a substantial sales increase in China, which is the world's fastest growing market, segment sales decreased for the first time in seven years due to the drastic deterioration of our operating environment.

In fluoropolymers and fluoroelastomers, sales declined more than 10% compared with the previous term as global demand for IT products and semiconductor manufacturing devices dropped precipitously and demand in the U.S. market for LAN cables decreased substantially. In Japan and the rest of Asia, demand for semiconductor etching agents decreased substantially, resulting in lower sales.

Sales of fluorocarbons increased for the second straight term, as Japanese and other air-conditioning



manufacturers switched to R-410A, R-407C, and other alternative refrigerants, driving up demand.

Daikin has begun using its U.S. subsidiary Daikin America, Inc., to produce oil- and water-repellant finishes, thereby establishing a supply system that covers both the United States and Japan and serves as a basis for global development. As a result of these efforts, sales of oil- and water-repellant finishes increased dramatically compared with the previous term.

Outlook

It is estimated that the fluorochemicals market contracted by approximately 15% in fiscal 2002. In fiscal 2003, as economic prospects remain uncertain and manufacturers need to carry out inventory adjustments, an overall market recovery is unlikely, although a partial recovery is possible. That said, the long-term outlook is quite good, as demand from manufacturers of such cutting-edge products as semiconductors and telecommunication devices as well as automobiles, consumer electronics, and textiles is expected to drive long-term growth.

In line with the operational policies set forth in "Fusion 05," Daikin is taking measures to develop new applications for semiconductors, telecommunications, and other fields, accelerate development on a global basis, and establish peripheral businesses.

Anticipating slow growth, Daikin has established a business plan for fiscal 2003 that calls for the expansion of sales and market share for such products as oil- and water-repellant finishes, fluoroelastomers, and PTFE fluoropolymer. At the same time, the Company is trying to reduce fixed costs and carry out other structural reforms to ensure a stronger foundation for future earnings.

Also on track are plans to create a more powerful operating infrastructure through the implementation of an improved supply system. To accomplish this, the Company will set up new manufacturing bases, enhance the capabilities of existing bases, strengthen sales networks, and enlarge its scale of business.

In oil- and water-repellant finishes, Daikin is aiming for higher sales and a larger market share. To this end, we are planning to augment the capabilities of our manufacturing bases in the United States and Japan in 2002 and provide better technical services.



In fluoroelastomers, the Company has established a new manufacturing subsidiary, Daikin Chemical France S.A.S. The new subsidiary will complement Daikin Chemical Europe

GmbH, a subsidiary specializing in the sale of fluorochemicals, and Daikin Chemical Netherlands B.V., which operates a pre-compound production plant for fluoroelastomers. As a result, in Europe, the production and sale of fluoroelastomers will generate an integrated system, thus accelerating the pace of the Company's global development.

Daikin is now building a manufacturing plant in Changshu, Jiangsu Province, China, which is scheduled to begin production in the second half of fiscal 2004 and will supply products for both the Chinese and global markets. In preparation for the start of operations, we are working to expand sales in China and the rest of Asia and lay the groundwork for the creation of new markets.

Daikin America, which completed its 10th year of operations in January 2001, is working to strengthen its position in the United States, home to the world's largest fluorochemical market and some of the most advanced applications developments. To this end, we are improving our technological services and enhancing our product development capabilities.

In August 2001, we established Taiwan Daikin Advanced Chemicals Inc. in Taipei, Taiwan, which is a global center



for the production of semiconductors and IT products, to carry out general sales of fluorochemical products. In conjunction with Formosa Daikin Advanced Chemicals Co., Ltd., which pro-

duces and sells semiconductor etching agents, Daikin will work to extend the range of its operations in Taiwan.

To expedite the execution of management decisions, we have implemented a management policy that stresses the importance of our strategic alliances. Under this policy, we are considering alliances with companies in virtually every

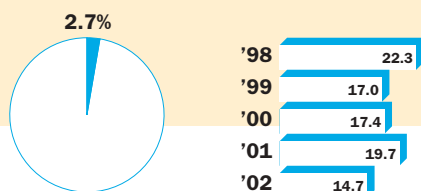
field of business, including production, sales, materials procurement, and R&D. For example, to expedite the development of new applications and improve the Company's technological capabilities, Daikin is forming a global research network that includes academic and industrial partnerships as well as stronger contributions from the Daikin Institute of Advanced Chemistry and Technology, Inc., which outsources research projects to venture businesses and research institutions.

In July 2001, Daikin formed a strategic alliance with OMNOVA Solutions Inc., based in Ohio, the United States, to jointly develop and commercialize fluorochemical products for surface modification and surfactant applications. The joint effort will focus on fusing OMNOVA's fluoropolymer production technology with Daikin's fluorochemical technology to develop products that benefit from distinctive fluorosurfactants and coatings modifiers.

Daikin will continue to conduct its fluorochemical operations safely with due consideration given to the environment and reinforce its frameworks for providing services and supplying safe, high-quality products on a global scale.

Oil Hydraulics

Sales (% of net sales, ¥ billion)



In fiscal 2002, sales in the Oil Hydraulics Division decreased 25.3% compared with the previous term, to ¥14.7 billion, and accounted for 2.7% of consolidated net sales.

Overview

•Oil Hydraulics Equipment

Aggregate sales in Japan's oil hydraulics equipment industry fell 16.5% compared with the previous term, to ¥194.4 billion.

Daikin focused on studying the nature of the end-user market and cultivating new market segments and latent needs by continuing to develop inverter oil cooling units and the ECORICH series, a line of distinctive, energy-saving products.



Daikin has teamed up with Sauer-Danfoss Inc. (U.S.A.) to form two joint-venture companies that will produce and sell oil-hydraulics products for construction machinery at Daikin's Yodogawa Plant in Japan. Both joint ventures got off to a good start during the term under review.



•Parking Systems

Demand for Daikin's mechanical multi-level car-parking systems, which is strongly influenced by the supply of new condominiums, remained virtually unchanged from the previous term. However, as Daikin was forced to implement extreme price reductions in response to decreased condominium prices, sales from parking systems declined.

•Lubrication

Lubricant sales remained virtually unchanged from the previous term despite dwindling demand in the iron and steel industry, which is one of the largest markets for lubricants. This is attributable to our success in establishing a stable earnings base through the integration of our lubricant operations with those of Nabco, Ltd., in April 2000.

Outlook

•Oil Hydraulics Equipment

Market fluctuations notwithstanding, demand in the market for oil hydraulics equipment will most likely decline over the medium-to-long term due to competition from electrical and pneumatic devices and the global expansion of companies making the products in which our oil hydraulics equipment is installed. Furthermore, with the increase in the number of global manufacturers based in Japan, our operating environment may worsen in the future. In light of these factors, aggregate sales in Japan's oil hydraulics equipment

industry are expected to decrease 2.0%, to ¥190.7 billion.

The following strategies have been implemented to ensure success in this tough environment.

1. We will produce new hybrid products through the fusion of our conventional hydraulics technologies with technologies using electrical and pneumatic platforms, thus expanding the scope of our operations to cover an entire range of functions from power control to power motion control.
2. We will develop our business in promising Asian markets while seeking opportunities for business alliances and tie-ups. In line with this strategy, we have strengthened our relationship with Sauer-Danfoss Inc. through the establishment of two joint ventures, which will benefit from the strengths of both companies. Our aim is to secure the No. 1 position in the Asian market for mobile hydraulics by 2005.

•Parking Systems

In the medium term, demand for parking systems will remain stable but price competition will intensify.

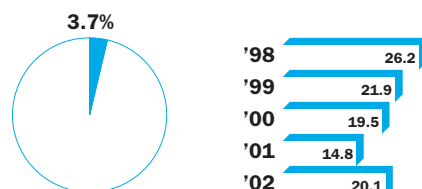
Moreover, the hydraulics-based systems market in which Daikin's products are sold comprises slightly less than 15% of the overall market for multi-level car-parking systems.

Therefore:

1. Daikin will form alliances with manufacturers of electric motor-driven parking systems. At present, we are probably the third or fourth largest manufacturer in Japan but an alliance would enable us to jump to the first or second position in the industry.
2. As Daikin has the industry's No. 1 service system, the Company must derive a substantial portion of its earnings from servicing mechanical multi-level car-parking systems.

Defense

Sales (% of net sales, ¥ billion)



In fiscal 2002, sales in Daikin's defense-related operations amounted to ¥20.1 billion, a 36.0% increase com-

pared with the previous term. The division's sales accounted for 3.7% of consolidated net sales, up from 2.8% in the previous term.

Overview

In fiscal 2002, Japan's defense budget remained fairly constant, and there were no significant improvements in the Company's operating environment. In fiscal 2001, Japan's Self Defense Agency placed an order for tank ammunition, which we had begun mass producing during the same year. Unfortunately, we were forced to postpone delivery of the order due to an accident that occurred at one of our subcontractor's plants in fiscal 2001. As a result, the delivery was made during the term under review and sales benefited accordingly. In addition, Daikin is making structural changes to its private-sector business, which includes conventional fiber-reinforced plastic (FRP) composite vessels, oxygen regulators, and, since 2001, ICU devices for small animals. However, these changes notwithstanding, private-sector sales remained virtually unchanged from the previous term due to harsh market conditions.

Outlook

Fiscal 2003 is the second year covered by the New Medium-Term Defense Plan, which provides for a defense budget that is 3.8% higher than that of the previous defense plan. The defense budget for fiscal 2003 amounts to ¥4.94 trillion, a modest increase compared with the previous term and, of this, expenses related to combat equipment are forecast to be ¥766.0 billion, a ¥1.0 billion decrease. However, the budget for ammunition and other products made by Daikin is expected to remain unchanged, which means that prospects for the Defense Division are stable for fiscal 2003.

Defense

In the face of constrained defense spending, Daikin will act to maximize the number of orders it receives for ammunition and other products that it began mass-producing in fiscal 2002. At present, Japan's Self Defense Agency is revising its incentive contract system in an attempt to lower costs, and Daikin is taking vigorous action to use the revised system to improve the efficiency and stability of its operational framework.



Private-Sector Business

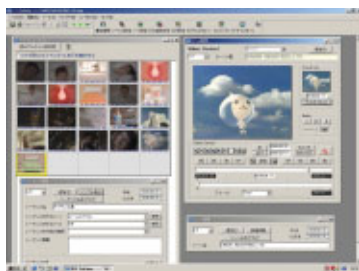
Daikin first entered the market for residential oxygen medical equipment in 1996, and in the past few years a number of new companies have followed suit, resulting in tough competition. In fiscal 2003, Daikin plans to

expand the scope of its operations by implementing extensive cost reductions, increasing sales of distinctive oxygen regulators, and introducing new FRP composite vessels. Furthermore, in anticipation of increased demand for high-oxygen medical treatment for pets, Daikin will develop a sales strategy for its ICU device DIA M10.

Electronics

In fiscal 2002, demand in the computer graphics industry contracted, reflecting stagnation in the semiconductor market, dwindling demand for computer graphics animation software, reduced investment in computer systems, and a shift to Windows NT® operating systems. Despite these adverse conditions, Daikin's Electronics Division sales changed little from the previous fiscal year due to the launch of a new IT network solutions business and a virtual digital broadcasting studio. Furthermore, by shutting down our DVD department in the United States and focusing on the Japanese market, we recorded profits on the sale of DVD-authoring software.

In the years ahead, IT and network proliferation will accelerate, and the use of broadband and mobile communications will continue to evolve. This trend represents a significant business opportunity insofar as it will increase demand for the computer graphics products we have worked so hard to develop. To build a solid computer graphics business, we



are enlarging the scope of our operations and striving to become a total solutions provider.

In network solutions, Daikin is seeking to provide better con-

sulting services and is broadening the scope of its solutions business by providing LSF software, which enables individual computers to share their processing burdens by means of a network. In addition, Daikin's IND and IDD network surveillance systems are used by a wide range of universities, institutes, and corporations. At present, the Company is optimizing the technological platform underpinning such systems and setting up a business that will provide solutions and services related to the management of IT assets.

In 2001, we initiated efforts to market the Vi(z) Virtual Studio, which is used by broadcasting companies. In addition, Daikin is taking steps, sometimes in conjunction with other companies, to construct new ways of handling workflow during the creation of computer games and broadcasting content, data management, streaming-video transmissions, and other aspects of the computer graphics business. Some of the products we have produced in this area include Softimage/DS, a non-linear editing system that enables users to digitize and edit images, and SCENARIST, a DVD-authoring system.

With the No. 1 share of the market for CAD design and genetic engineering software, we are building the world's best portal site enabling users to rent FINDER CAD software via the Internet. Furthermore, anticipating the implementation of the Japanese government's E-JAPAN Strategy and CALS/EC policy, we have built a framework for the provision of IT services and are aiming to attract 2,000 users.

Daikin is closely monitoring the technologies it has developed for three-dimensional interactive TV and bi-directional digital content, making technological adjustments where necessary and forming alliances to facilitate the establishment of new businesses related to such technologies in fiscal 2004.