

Fiscal 2005, the year ended March 31, 2006, marked Penta-Ocean's 56th business term. During this period, the Japanese economy showed signs of a gentle recovery, thanks to industry-wide increases in capital investment related projects, backed by favorable corporate earnings and improvement in the employment and income situations across the economy.

Despite the protracted downturn in public sector construction projects, once the main business area for the Group, Penta-Ocean found growth in projects in the private sector, where a trend of steady growth in corporate capital investment is underway. The steady growth in urban housing projects also helped to strengthen sales for the Group.

In the overseas construction market, sales were not as favorable as in the past, with a falloff in new construction occurring throughout the Southeast Asian region. Economic growth in the Chinese market, however, remained robust, and the Penta-Ocean Group continued to expand its project line-up in that burgeoning region. Business also continued to improve in the Middle East, promising a solid growth trend for the future.

Business Results for the Term under review

Under these circumstances, Penta-Ocean and its Consolidated Subsidiaries formulated a three-year mid-term management plan, "Evolution 21," that began in the term under review. Under the plan, all employees and company directors are endeavoring to reinforce profit-making capabilities in the Group's main business areas and strengthen its financial base, aiming at further development in the future. Owing to the dedication of every employee, the Group met its goals for the first year of the plan.

Consolidated net sales in fiscal 2005 amounted to ¥354,657 million (US\$3,019.1 million), a 2.7% increase from the previous term. Consolidated operating income increased by 18.1% year-on-year to ¥14,177 million (US\$120.7 million). Consolidated ordinary income also increased, by 27.9%, to ¥11,341 million (US\$96.5 million). Consolidated income before income taxes rose by 5.5% from the previous term, to ¥10,019 million (US\$85.3 million) and as a result of these increases, consolidated net income in the term under review produced profit of ¥3,876 million (US\$33.0 million), a year-on-year increase of 64.2%.

Regrettably, however, owing to the adverse conditions present in our operating environment, it was decided not to pay a dividend to shareholders again this year. It is our belief that priority should be given to increasing the Group's capital and retained earnings in order to solidify Penta-Ocean's financial base in order to secure future profits for our shareholders.

Future Prospects and Challenges

Efforts to reform the Group's tendering and contracting system for public works projects continued to be a top priority for Penta-Ocean during the term under review. Continued efforts were also made to expand private sector competitive bidding; to adopt a comprehensive evaluation system based on construction quality and advanced technological capabilities, rather than conventional bidding, which involved pricing only; and reinforce measures against unreasonably low price bidding by including revised penalty codes. The business environment surrounding the construction industry underwent substantial changes during the term under review, including the

revision and reinforcement of the Antimonopoly Law, in January 2006. Although severe competition continues to be an obstacle to growth and sustainable profitability, Penta-Ocean continues to believe that companies possessing advanced technological capabilities and effective management protocols will prevail over the long term.

The Group has already begun to restructure corporate systems in order to comply with revisions being made to the tendering and contracting requirements for public works projects. It is also strengthening and expanding its business areas, and continues to seek out new business opportunities in Japan and in overseas construction markets.

During the term under review, Penta-Ocean continued to strengthen its financial position by enhancing capital strength and reducing interest-bearing debt. These measures will continue to ensure that the Group meets the goals it has set for both the mid-term and long-term future.

Further Corporate Compliance

As a basic policy, corporate compliance forms the basis for corporate social responsibility (CSR) and all members of the Penta-Ocean Group are required to adhere to high standards of conduct. In March 2006, however, an indictment was filed against one of our employees for tampering with a competitive bidding for a public works project ordered by Japan's Defense Facilities Administration Agency. Owing to the violation, Penta-Ocean has been suspended from tendering bids for federal and local government sponsored projects. As part of strenuous, ongoing efforts to ensure that this type of tampering does not occur again, the Company is improving transparency and establishing rigorous self-auditing practices.



On May 1, 2006, I replaced Kazujiro Tetsumura as President and Representative Director and shall do my very best to strengthen and develop the businesses of the Penta-Ocean Group in the challenging business environment surrounding the construction industry. In these efforts, I would like to take this opportunity to ask our shareholders for their continued support and patronage.

June 29, 2006

A handwritten signature in black ink that reads "Y. Murashige".

Yoshio Murashige,
President