

S Foods Shareholders' Letter

Review of the Interim of the 37th fiscal year

(2002.3.1—2002.8.1)
(PDF Version)

Message and Report to Our Stockholders

Overview

During the term under review, the government declared that the economy bottomed out in May. Despite this announcement, the Japanese economy continued to be in doldrums due to a chain of negative events, where the deflation of assets and falling prices adversely affect income and employment, which in turn lead businesses to cut back on capital investment. While signs of recovery are seen in the Euro region and Asia, the future of the United States economy has become increasingly uncertain due to the distrust of corporate accounting and the collapse of a major telecommunications carrier. As a result, the global economy was unstable during the period under review.



November 2002
Hayao Morishima
President and CEO

Recovery of business performance

The food industry continues to face an extremely severe environment. While there has been a marked rebound from the effects of BSE, personal consumption remains sluggish and, due to the series of unfortunate controversies in the industry since last year, consumers have become extremely weary of the industry and meat.

Against such a backdrop, according to our group's management philosophy, we have aimed to win greater customer trust by providing customers with products that are delicious, safe, healthy, and appealing. As a facet of this activity, and to coincide with the establishment of S Foods Code of Conducts, we asked all employees to carefully comply with the law and regulations. In sales, as a result of engaging in such positive activities as the Kotetchan 20-year Anniversary Campaign, our sales recovered from 48.9% in February compared to sales in the same month last year to 88.4% in August compared to sales in the same month last year. We analyze the trend to indicate that we have generally overcome the BSE problem.

Reinforcement of management

Furthermore, we have followed through with reengineering (reconstruction of business by destruction and creation), in an effort to build a slim and strong business. Due to such managerial efforts during the term under review, sales volume made a strong recovery. Sales revenue, on the other hand, fell to 19,829 million Yen (down 28.8% from the same period last year) due to falling unit prices. Operating Income, in the mean time, recovered to last year's level due to our efforts to cut costs. As nearly all of our raw materials are imported, we had to post as a non-operating expense the loss from foreign exchange in the derivative transaction that we use to hedge foreign currency fluctuation risk. Despite such expense, consolidated income before extraordinary items, at 431 million Yen (down 44.3% from the same term last year), exceeded our forecast. Due to a change in the U.S. accounting standard, the U.S. subsidiary had to deplete good will. As a result, the interim net profit amounted to 146 million Yen, or down 56.7% from the same term last year.

Future outlook and business strategy

Despite the government's plan to resurrect the economy, the people of Japan have yet to regain confidence in their economy. As a result, we feel that consumption will continue to be sluggish for some time. Our industry feels that consumers still have a strong distrust, and the severe conditions will not change for some time. In order to materialize our business philosophy, our group intends to actively pursue marketing activities with "trust" and "value-added" as the keywords. To be more specific, we will build a new business model (one with value of existence, one that will allow us to be number one, and one that will not be destroyed) to become number one in the world in variety meat and number one in Japan in barbeque meats (Yakiniku) by pushing ahead with reengineering. We will strive to build a solid business foundation that is profitable even in a severe environment to increase our value as a company. Furthermore, amidst the deflationary environment, we will place our priority not on sales revenue but on sales quantity, and strive to increase our market share.

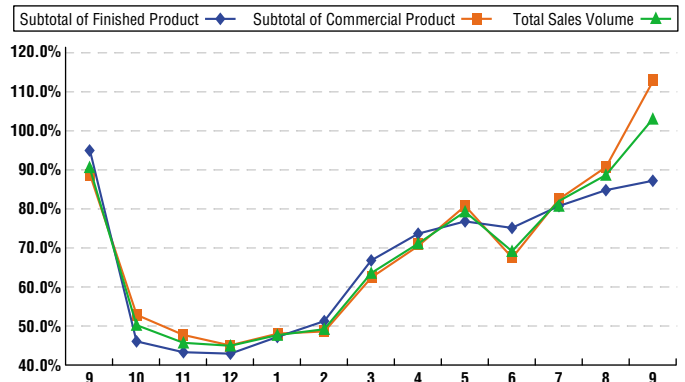
Q1. What is your outlook for the 37th term?

A. Whereas sales volume in February this year amounted to 48.9% compared to February last year, it rose to 88.4% in August compared to August last year. Therefore, we feel that we have generally recovered from the BSE problem. From September, sales have been strong, partly due to the 10th anniversary campaign for Gyumotsunabe, which entered the tenth year on the market. Therefore, we predict consolidated revenue for the term ending in February 2003 to reach 42,000 million Yen, or down 2.9% from last term, income before extraordinary items of 1,200 million Yen, or up 505.3% from last term, and net profit of 550 million Yen, or up 2,785 million Yen from the last term.

Q2. What about the individual business performance of S Foods?

A. We have begun to see the fruit of reengineering, and the Kotetchan 20th Year Campaign, which we have held to commemorate the 20th year anniversary of Kotetchan, has been successful. As a result, sales volume in September amounted to 102.5% of the same month last year (although it was the month when the case of BSE broke out, it had no impact on sales) and to 92.9% of the same month year before last year. I would also like to add that sales continue to be strong in October as planned.

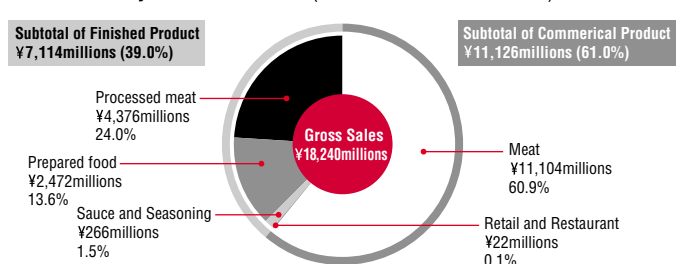
■ Sales volume (% of comparison with last year)



Q3. What about performance by department?

A. By department, sales of commercial department amounted to 18,620 million Yen, or down 29.4% from the same period last year. Sales of retail department amounted to 1,198 million Yen, or down 18.7% from the same period last year. Business performance by region is as follows: In Japan, sales amounted to 19,198 million Yen, or down 28.9% from the same term last year, and operating income amounted to 558 million Yen, or down 4.8% from the same period last year. In the United States, sales amounted to 374 million Yen, or down 24.8% from the same period last year, and operating income amounted to 11 million Yen, or down 62.4% from the same period last year.

■ Net Sales by Product Division (2002/08 semiannual term)



Q4. How are you working on product development and market development?

A. We begin our product development and market development with a story. For this story, we pinpoint problems from an analysis of the current situation. Then, we pick out the negative effects that arise from the problems. Next, we propose solutions and verify them. Without this story, we feel that there is no success. For example, the general perception is that thick cuts of barbecue meats (Yakiniku) are juicier and taste better. Some meats, however, lose their tenderness when they are sliced thick. The ways the meats are cut also affect the tenderness. Based on the story, we solve these problems, such as by placing incisions, cutting the meat into sticks, or adding a touch of "hand-made" by hand cutting the meat. In other words, we thoroughly research the qualities of a material to develop a product that is delicious without losing its juiciness or tenderness, that is easy to eat, and that appeals to customers.

Q5. Are you making progress in cultivating new channels and developing a new production system?

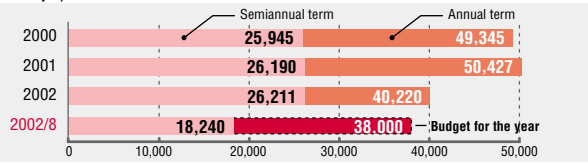
A. S Foods Group as a whole is working together to smoothly cater to the increasingly diversified needs and to develop new business models. Group companies also work individually to produce products for specific channels and shift production of principle products to increase production through sales areas.

Q6. What do you do to boost employee morale?

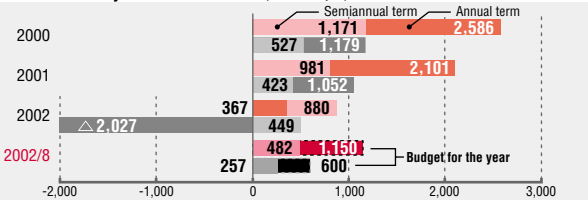
A. We have established the S Foods Code of Conducts based on the corporate creed and company mottoes, and asked all employees to become thoroughly familiar with them. Furthermore, to ensure compliance of the entire group, including affiliates on an organizational level, we formed a Compliance Committee. We are proceeding with such a plan as we are confident that improving customer trust and corporate value will help us achieve the management vision of realizing a strong company.

Financial Summary (unconsolidated)

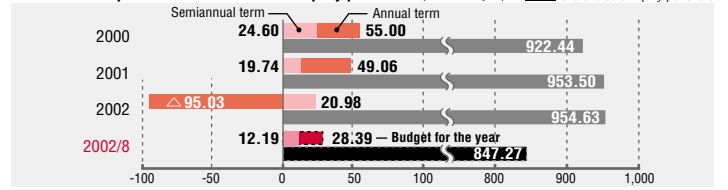
● Net sales (Million of yen)



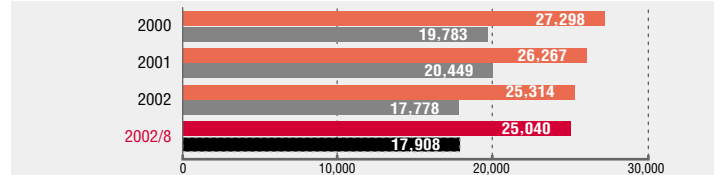
● Income before extraordinary items/Net income (Million of yen)



● Net Income per Share/Shareholders' Equity per Share (Million of yen)



● Total Assets/Shareholders' Equity (Million of yen)



Balance Sheet & Income Statement

● Individual Balance Sheet (Summary)

	August 31 2002	August 31 2001	February 28 2002
Assets			
Current assets	10,660	12,240	10,480
Fixed assets	14,380	15,567	14,834
Total assets	25,040	27,808	25,314
Liabilities			
Current liabilities	6,746	6,904	7,145
Fixed liabilities	384	429	390
Total liabilities	7,131	7,334	7,536
Shareholders' Equity			
Common stock	4,226	4,226	4,226
Additional paid-in capital	4,171	4,171	4,171
Earned surplus	590	590	590
Retained earnings	9,126	11,472	8,995
Total shareholders' equity	17,908	20,473	17,778
Total liabilities & shareholders' equity	25,040	27,808	25,314

● Individual Statements of Income (Summary)

	2002/08 semiannual term	2001/08 semiannual term	2002/02 annual term
Above the line			
Net sales	18,240	26,211	40,220
Cost and expenses	17,656	25,607	40,355
Operating income	584	604	△135
Non-operating income	142	293	553
Non-operating expenses	244	16	51
Income before extraordinary items	482	880	366
Below the line			
Extraordinary gains	10	60	166
Extraordinary losses	19	210	4,026
Income before income taxes	474	730	△3,493
Income taxes-current	9	317	60
-deferred	207	△36	△1,526
Net income	257	449	△2,027
Retained earnings carried forward	806	960	960
Unappropriated retained earnings	1,064	1,410	△1,066

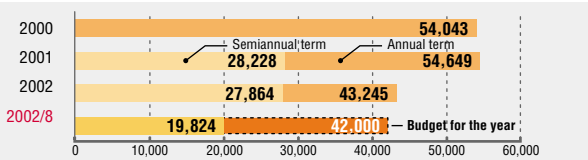
● 2003/02 (Projected)

	(Million of yen)
Sales	38,000
Income before extraordinary items	1,150
Net income	600
Dividends per share	¥12

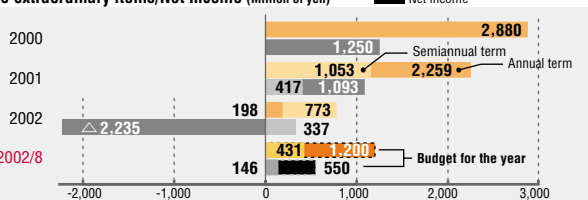
Consolidated Financial Summary

Consolidated Subsidiary: Mr. Stamina KK, KK Kenshoku, Naruo Kosan KK, FOEM Shokuhin KK, Fremont Beef Company

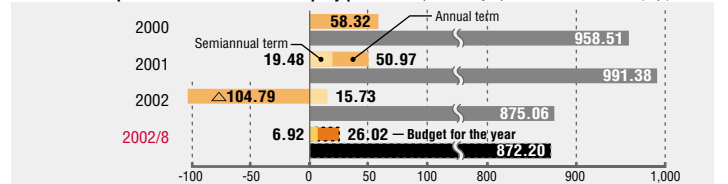
● Net sales (Million of yen)



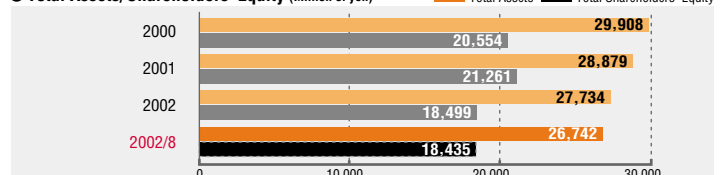
● Income before extraordinary items/Net income (Million of yen)



● Net Income per Share/Shareholders' Equity per Share (Million of yen)



● Total Assets/Shareholders' Equity (Million of yen)



Consolidated Balance Sheet & Income Statement

Consolidated Subsidiary: Mr. Stamina KK, KK Kenshoku, Naruo Kosan KK, FOEM Shokuhin KK, Fremont Beef Company

● Consolidated Balance Sheet (Summary)

	August 31 2002	August 31 2002	February 28 2002
Assets			
Current assets	11,759	13,826	12,129
Fixed assets	14,983	16,493	15,604
Total assets	26,742	30,319	27,734
Liabilities			
Current liabilities	7,252	7,427	8,067
Fixed liabilities	419	986	434
Total liabilities	7,672	8,413	8,502
Minority interests	633	666	732
Shareholders' Equity			
Common stock	4,226	4,226	4,226
Additional paid-in capital	4,171	4,171	4,171
Consolidated retained earnings	10,219	12,773	10,200
Treasury stocks	△196	△0	△194
Total shareholders' equity	18,435	21,238	18,499
Total liabilities, minority interest & shareholders' equity	26,742	30,319	27,734

● Consolidated Statements of Income (Summary)

	2002/08 semiannual term	2001/08 semiannual term	2002/02 annual term
Above the line			
Net sales	19,824	27,864	43,245
Cost and expenses	19,238	27,260	43,465
Operating income	586	603	△220
Non-operating income	93	211	499
Non-operating expenses	249	41	80
Income before extraordinary items	431	773	198
Below the line			
Extraordinary gains	18	81	114
Extraordinary losses	85	212	3,958
Income before income taxes	364	642	△3,646
Income taxes-current	19	356	114
-deferred	206	△59	△1,558
Net income	146	337	△2,235

● 2003/02 (Projected)

	(Million of yen)
Sales	42,000
Income before extraordinary items	1,200
Net income	550

● **Summary of Cash Flows Statement** (Millions of Yen)

Subject	2002/08 semiannual term	2001/08 semiannual term
Net Cash providedg by Operatin Activities	2,077	△638
Net Cash used in Investing Activities	△249	82
Net Cash used in Financing Activities	△2,176	298
Cash and Cash Equivalents at End of Year	1,972	1,168

Company Profile

■ **Line of business**

Manufacturing, processing, wholesale and retail of meat products, sauce and seasoning

■ **Offices**

Head office:

1-22-13 Naruohama, Nishinomiya City, Hyogo

Phone No.+81-798-43-1065 Fax NO.+81-798-43-1067

Tokyo Head office:

38-24 Takasecho, Funabashi City, Chiba

Phone No.+81-47-435-0811 Fax NO.+81-47-433-3301

■ **Year of foundation**

May 22, 1967

■ **Paid in capital**

¥4,226.64million (as of end February, 2002)

■ **Directors & Auditors** (effective May 28,2002)

Representative Director	Hayao Morishima
Director	Susumu Tomisawa
Director	Naoki Tomonaga
Director	Motohiro Tanaka
Director	Kunitaka Dan
Director	Masatsugu Tanaka
Auditor	Yujiro Ohiro
Auditor	Hideo Konishi
Auditor	Masanobu Nakano

■ **Number of employee**

376 (as of end August, 2002)

■ **Annual sales**

¥40.2 billion

■ **Affiliates**

Mr. Stamina KK

KK Kenshoku

Naruo Kosan KK

FOEM Shokuhin KK

Fremont Beef Company

KK Ajicho

Goai Yakiniku Concept KK

Sukoyaka Shokuhin KK

KK Shizuoka Ajicho