

Aiming to Secure the Competitive Advantage in the Global Market by Boosting Marketing Capabilities

Company President Tatsuhiko Izumi discusses Clarion's strategy to drive stable growth amid major changes in the market environment.

How do you evaluate Clarion's performance for the fiscal year?

We achieved consolidated net sales of ¥184,176 million for the fiscal year ended March 31, 2006 (fiscal 2005), an increase of 3.3% compared with the previous fiscal year. Sales increases in navigation systems for the domestic OEM (Original Equipment Manufacturers) market and aftermarket, audio-visual equipment for buses as well as increased sales in our EMS (Electronic Manufacturing Services) business in North and Central America and Europe contributed to this increase, overcoming price erosion caused by intense competition.

Consolidated operating income, however, stood at ¥5,228 million, down 45.4% year-on-year, due to the impact on profits of a decline in market prices, an increase in strategic investment in R&D and facilities, higher logistics and advertisement and sales promotion expenses in line with aggressive advertising campaigns. Nonetheless, net income rose 14.7% to ¥5,862 million mainly on account of a gain on sales of property, plant and equipment including the sale of the land of the Saitama Head Office in line with plans to move operational headquarters and a gain on sales of securities for investments.

Three key changes characterized the market environment during the fiscal year. First, prices declined dramatically in the overseas aftermarket, which had significant negative impacts on our profitability. Second, there was a shift of demand to subcompact and smaller vehicles (what we call "kei" category cars) in Japan, leading to a sharp increase in the proportion of lower-end products installed in these vehicles. As we have a



Tatsuhiko Izumi
President

high percentage of OEM business, the impact of this was by no means small. Third, there was an accelerated shift in product mix from audio equipment to car navigation systems. Increased demand for car navigation systems meant an increase in demand for integrated navigation/audio systems, and accordingly, demand for basic audio products decreased. Fiercer competition in the aftermarket overseas also negatively impacted profitability.

Clarion products that used to boast high added value turned into mere commodities as a result of these changes. And because the changes came around at a pace far more rapidly than we had expected, we found it difficult to keep up.

Taking such factors as a serious warning, we have started to take action to implement major reforms aimed at creating a corporate structure that can generate stable profits under any market circumstances.

Financial Highlights

Clarion Co., Ltd. and Subsidiaries
Years ended March 31

	Millions of Yen		Thousands of U.S. Dollars
	2006	2005	2006
For the Year:			
Net sales	184,176	178,325	1,567,863
Operating income	5,228	9,582	44,508
Net income	5,862	5,111	49,910
At Year-end:			
Total assets	122,119	119,527	1,039,578
Total shareholders' equity	34,484	26,729	293,560
	Yen		U.S. Dollars
	2006	2005	2006
Per Share:			
Net income	20.76	18.09	0.177
Cash dividends	2.00	—	0.017

Note: U.S. dollar amounts have been translated from yen, for convenience only, at the rate of US\$1=117.47, the approximate exchange rate on March 31, 2006.

Please explain the challenges facing Clarion and your efforts to overcome these.

The biggest challenge for us at moment is our marketing capabilities in two distinct areas—product planning and user analysis.

With regard to product planning, product concepts have recently changed considerably in light of increased integration of audio and navigation functions and more digitally operated

or controlled in-vehicle devices. Also, there is a variety of recording media on offer other than CDs. At the same time, required functions and features are becoming more sophisticated and diversified with the advance of such applications as terrestrial digital broadcasting reception and iPod® compatibility. More new media are emerging into the market everyday at a phenomenal pace. As features and functions centered on “entertainment” become increasingly important in the market, we will seek to further strengthen our product planning ability in the entertainment sector. Historically, this sector has been our primary area of expertise, as we have constantly striven to make the in-vehicle experience more comfortable. We aim to boost the appeal of our products in this market and will continue to swiftly deliver items based on unique and exciting concepts that fulfill the dreams of our customers.

In the field of user analysis, we will move away from our conventional full-lineup strategy and deploy a marketing strategy with enhanced user segmentation and analysis. Diversification in media and the shift to digital electronics that I mentioned earlier have also led to diversification in user groups. In order to cope with such a market situation, it is imperative that we enhance our user analysis to make the most effective use of limited resources. We will clarify target user groups for each individual product and promote the development of such products that deliver user satisfaction to the targeted users.

The same approach will also apply for professional-use and OEM products. What’s more, in addressing the issues around these market segments, we believe a pressing task is to promote what we call “mono-zukuri,” literally meaning “making products,” the whole process from planning and development to production and distribution that can generate sufficient profit with products containing less added value. In other words, based on the assumption that the market for subcompact and smaller cars will continue to grow, an important issue for us is to strengthen marketing capabilities to cope with the situation.

We will also promote marketing activities connecting us with customers and users in each market by taking advantage of our worldwide network. This will also apply to our specialty equipment segment.

What fields hold the most promise for future growth?



In the OEM market, the most promising field will be the market for car navigation systems, where continued expansion is predicted. The popularity of in-vehicle integrated AV navigation systems is increasing, and this trend is spreading from Japan to

other countries. We see this as a great opportunity and will try to secure new business with customers in China, North America and Europe. Meanwhile, in line with increased safety awareness of drivers, we expect car navigation systems will integrate features and functions for ITS (Intelligent Transportation Systems) and increased demand for camera monitoring systems. As we have highly advanced camera and image recognition technology, we will try to expand our range of safety assistance applications such as parking assistance and obstacle warning/avoidance systems. We also expect growth in satellite radios (XM, Sirius) in North America and expect to secure more large-scale business from car manufacturers in the area, which will be the next largest market after Japan.

Another promising field stems from the continued growth in sales of audio equipment in emerging markets such as Thailand and Brazil, where we have already established bridgeheads.

In the aftermarket, our primary target is the expanding entertainment market, which includes audio equipment, digital broadcasting receivers and car navigation systems. The importance of contents is increasing as the communication infrastructure improves, and accordingly, we will push ahead with the development of our content business. With regard to overseas markets, we have positioned the BRICs (Brazil, Russia, India, and China), Africa and the Middle East as strategic target areas with high growth potential. Another key objective is to firmly establish the market for our portable navigation systems, which we are currently promoting aggressively in North America and Europe.

Could you explain the significance of the alliance with Hitachi in relation to what you have spoken about today?

The alliance with Hitachi is aimed at enhancing and expanding the business around in-vehicle information systems beginning with navigation systems and devices. With these in mind, we concluded a business alliance with Hitachi, Ltd in April of last year. We are currently moving ahead with joint efforts in various fields from advanced development, materials procurement and manufacturing to sales and after-sales services.

We have splendid product planning and development capabilities in in-vehicle entertainment systems, such as audio and navigation systems, and have built up longstanding business relationships with numerous car manufacturers in Japan, North America, Central and South America, Europe and Asia. In the aftermarket as well, we have been supplying products all around the world. Furthermore, we are expanding into the wide-ranging car multimedia business arena, which includes vehicle safety monitoring systems using CCD cameras. Hitachi, on the other hand, has technologies and capabilities, including abundant software and product development know-how in built-in software especially for digital home appliances. These technologies are essential for the in-vehicle information system in the future, and Hitachi is developing business in the automotive systems field aimed at realizing integrated control in ITS. Therefore, we believe both companies can compliment each other's expertise and needs by this strategic alliance. The growing in-vehicle information systems business, which includes ITS-related and telematics services, demands us to quickly meet diversifying market needs for sophisticated technologies. As a way for both companies to cope with such heightened market demand, we are jointly developing basic software platforms for products as well as advanced technologies with a view to future trends. We are specifically targeting the development of new products to be introduced into the market in 2008 and beyond, and for this we are integrating and concentrating resources and devising development tools. We are sure that these efforts will further increase investment efficiency in R&D and accelerate the speed of development. As a result, we can secure an overwhelming competitive edge in the global market.

What is Clarion's stance on corporate governance?

We formulated our management policy with a view to bringing forth more efficient and competitive management to ensure higher value of the enterprise to our shareholders over the long term, execute business strategies clearly bearing in mind this value, and properly return profit earned through our activities to our shareholders. We intend to raise the effectiveness of our corporate governance through building up fair and smooth relationships with stakeholders, disclosing important management information in a timely and appropriate manner, enhancing compliance management and managing the Board of Directors appropriately and efficiently.

We worked to enhance the following areas during the fiscal year in light of the enactment of the Corporate Law and the Financial Instruments and Exchange Law: (a) review of internal control systems and promotion of documentation of internal controls related to financial reporting; (b) promotion of



CSR with an emphasis on enhancing social contribution; (c) strengthening of compliance activities in order to reduce risk by instilling awareness from the system creation stage and undertaking other efforts; and (d) creation of a management

support system with the introduction of independent, unbiased outside directors.

These efforts have culminated in the creation of an infrastructure that can lead us toward more sound management. We will pour efforts into ensuring a corporate culture that appreciates stronger corporate governance and social responsibility.

Please tell us about specific measures to increase corporate value and return profits to shareholders.

First, I believe that the creation of a good corporate brand image will lead directly to greater corporate value. The first of the measures is to boost corporate value by promoting effective brand management.



Second, we must have improved operating results so we can ensure the stable return of profits in the form of dividends for all shareholders, and this in turn will raise corporate value. For this purpose, we will create and provide excellent products

through integrated efforts at each level of the "mono-zukuri" process.

As the third measure, we aim to increase corporate value by adding value to our products. We will deliver one-of-a-kind products filled with unique and advanced technology and quality as well as exciting design and functions to not only satisfy but also give "Fresh Pleasure" to customers. Customers will then recognize the philosophy that lies behind our business, which in turn will drive up corporate value. At the same time, we will make efforts to create a better work environment for employees, as we believe excellent products can only be created in such an environment by highly motivated employees.

These are the measures we see as necessary for us to return profits to all shareholders at the level that reflects operating results. It goes without saying, however, the key priority will be to pass on the benefits of Clarion's added value in a stable and ongoing manner.

I would like to ask for your continued support and guidance as we work toward our goals for the future.

June 2006

Tatsuhiko Izumi
President