

Creation of New Global Environment Business Department

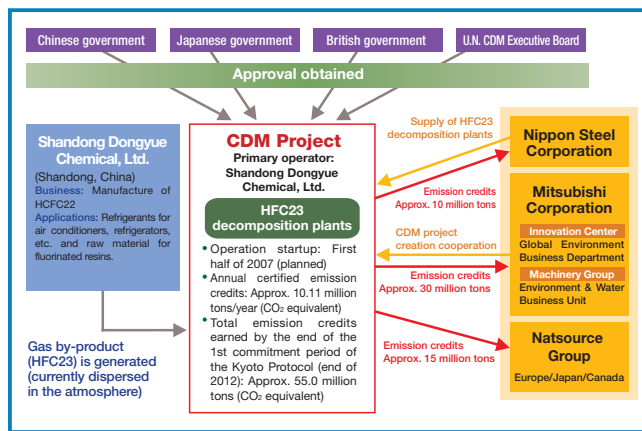
In response to the increasing urgency of global environmental issues, MC implements a range of environmental businesses throughout its business groups. The company's involvement spans various fields ranging from recyclable energy sources to industrial waste processing and recycling. Prior to the establishment of the Global Environment Business Department, initiatives were undertaken primarily within each respective business group. The new department better positions the company to tackle complex initiatives that cut across multiple business groups and to implement initiatives that require a medium to long-term vision. With the establishment of the Global Environment Business Department in April 2006, the company is now positioned to take a more active approach to global environmental issues. The new department is part of the Innovation Center within the Corporate Staff section and its task is to develop next generation businesses and new technologies.

Addressing Global Issues through Environmental Businesses

The Global Environment Business Department is comprised of an Emissions Reduction Business Office and an Environment Business Office. The Emissions Reduction Business Office works in cooperation with the Machinery Group and other internal groups to develop the company's numerous emissions trading projects. The list of projects includes those in China and other parts of Asia as well as projects in Eastern Europe and South America. One such project is a hydrofluorocarbon 23 (HFC23) reduction project owned by Shandong Dongyue Chemical Co., Ltd., in the Shandong Province of China. When completed, the Shandong Dongyue will be one of the world's largest projects by volume of emissions credits. The Emissions Reduction Business Office is also advancing similar emissions trading projects in Pakistan and the Philippines, as it strives to identify and promote businesses relating to emissions credits.

The Environment Business Office analyzes and surveys the status of the company's environmental businesses and the internal initiatives implemented in Japan and abroad. It examines environmental businesses from a company-wide perspective in order to advance comprehensive initiatives that cut across business groups. For example, the department created a network for employees involved in

Shandong Dongyue Project: Clean Development Mechanism (CDM) for HFC23 Processing



environmental fields to share their knowledge and expertise. The department also faces the task of leveraging the financial resources and vast and diverse global network of MC.

Emissions Trading Business

MC has been involved in emissions trading from when the business first began to evolve, recognizing the need for economic activities to coexist with the global environment through the use of market mechanisms. In 2000, the company invested in the Prototype Carbon Fund, which was established under the leadership of the World Bank. The company also established Natsource Japan Co., Ltd., through a joint venture with Natsource LLC, a US firm that is a pioneer in the field of emissions trading. It enabled MC to gain valuable expertise in this developing new field.

The EU launched its emissions trading program in January 2005, closely followed by the enactment of the Kyoto Protocol in February of the same year. These events led to a global acceleration of initiatives under the Kyoto Mechanism. The Kyoto Mechanism enables countries to acquire emissions credits through market mechanisms and apply them to their own targets for emissions reductions. The three components of the Kyoto Mechanism are the Clean Development Mechanism (CDM), Joint Implementation (JI) and Emissions Trading. In addition to the trading of emissions credits, the company is deploying its emissions trading and related business focusing on the CDM and JI sectors. MC is ideally positioned to develop emissions trading and related business through its six business groups, which have 195

Global Environment Business Department



offices across the globe. The vast reach of the company's network includes contacts with governments of various countries and global firms involved in all segments of industry.

World's Largest CDM Project

A leading example of the company's CDM business is its involvement in the Shandong Dongyue Project which will be one of the largest trading projects in the world when completed. The project is owned by the Chinese firm Shandong Dongyue Chemical, which is China's largest producer of CFCs. Shandong Dongyue Chemical manufactures the gas refrigerant HCFC22 which generates the air pollutant HFC23 through its manufacturing process. Under the project, HFC23 gas byproducts will be collected and subjected to thermal decomposition using facilities engineered by Nippon Steel Corporation. MC's role is to provide the overall coordination for the CDM business.

The project was officially approved in March 2006 after satisfying the strict requirements set by the CDM Executive Board of the United Nations Framework Convention on Climate Change (UNFCCC) and the facilities are scheduled to go online in the first half of 2007. The project is estimated to earn emissions credits equivalent to 10 million tons of CO₂ emissions annually through HFC23 processing. Calculated through 2012, which is the last year of the initial period of commitment to the Kyoto Protocol, the project is projected to earn 55 million tons of emissions credits. These numbers will make it one of the largest emissions credit-earning projects in the world. All emissions credits from the project will be purchased by MC, Nippon Steel Corporation and the Natsource Group.

Medium to Long-term Vision

The major emissions credit purchasers are Japan, the EU and Canada, whose current annual emissions

performance is estimated at a combined 700 million tons over the targets set by the Kyoto Protocol. The situation has led to an urgency to vitalize the emissions market, with national governments and leading energy companies already becoming active players in the market.

Under the Kyoto Protocol, Japan is committed to reducing its greenhouse gas emissions level by 6% compared with 1990 levels. The Kyoto Protocol Target Achievement Plan announced by the Japanese government in 2005 predicts that Japan will fall approximately 1.6 percentage points short of this commitment. Reductions from domestic countermeasures and from forest absorption will not be enough to meet Japan's reduction commitment. The plan by the Japanese government calls for the country to assume the responsibility of purchasing emissions credits through the Kyoto Mechanism. However, the situation demands a strategic approach in order for Japan to strike a balance between global environmental issues and economic activity.

Satisfying the reduction commitments of the Kyoto Protocol through 2012 is just one step toward addressing the issue of global warming, a solution for which requires countermeasures that span several decades. The emissions trading business at MC is therefore positioned as a medium to long-term business requiring a steady level of commitment.

Manager's View	<p>Ichiro Keida</p> <p>GM, Global Environment Business Department</p> <p>The establishment of the Global Environment Business Department provides us with an infrastructure for promoting environmental businesses from a company-wide perspective. Working with the company's business groups, the department has already short-listed and is considering over 30 priority business projects involving emissions trading in various parts of the world. Given MC's heavy involvement in the resources and energy sectors, we are actively working to ensure that employees throughout the company have the necessary knowledge on global warming issues. We are committed to helping the company achieve the right environmental balance in its corporate activities.</p>
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Overview of Operations

