TO OUR SHAREHOLDERS

HAJIME SATO
President and CEO

REVIEW OF BUSINESS PERFORMANCE

In fiscal 2010, the year ended February 28, 2010, Star Micronics posted severe business results with reduced sales and earnings for the second consecutive year due to the global economic slowdown. Demand dropped significantly in all our major markets mainly due to restrained capital investment and sluggish consumer spending reflecting the financial instability and the deteriorating real economy.

As a result of these factors, Star Micronics reported consolidated sales of ¥29,181 million, a substantial drop of 48.8% year-on-year, in fiscal 2010. As regards profits, we reported an operating loss of ¥3,985 million. The net loss for the year was ¥8,555 million, mainly due to the posting of a loss on impairment of long-lived assets of ¥2,308 million and the cancellation of posting of deferred tax assets of ¥2,858 million.

To compensate our shareholders, Star Micronics decided to pay a full-year dividend of ¥22 per share.

REVIEWING MY FIRST YEAR IN OFFICE

Understanding Market Conditions

Star Micronics reached a milestone this year: the 60th anniversary of its founding. However, fiscal 2010, the fiscal year under review, was our harshest year ever due to worsening worldwide business conditions.

Looking at the markets by region, it seems that the U.S. market needs a little more time to improve, despite expectations of an economic recovery generated by the arrival of the Obama administration. One concern is the unemployment rate: consumer spending comprises more than 70% of the U.S. GDP and therefore I assume that if the employment figures do not improve then consumer spending will also be slow to recover.

As regards Europe, there is no change to last year's forecast that economic recovery in Europe will come later than in the U.S. Furthermore, because a high proportion of Star Micronics' exports are to Europe, we are concerned that the low euro will negatively impact on our business results.

Turning to China, it is here that the market has shown the quickest recovery. However, the current competitive environment in China is extremely tough, since China is the only market that is recovering from the financial crisis. Going forward, I consider that our competitiveness in terms of price will be the issue, because I expect our focus to move from competing with Japanese manufacturers, as we have been until now, to competing with Chinese manufacturers.

Although the economic recoveries in Europe and the U.S. are slow to materialize, I think there will be no significant change to our existing business approaches of preserving earnings in our major markets of Europe and the U.S. and of developing businesses in emerging nations.

Major Initiatives

One management target for fiscal 2010 was to ensure that our financial structure did not deteriorate. In a harsh business environment, we realized that we would be forced to post an operating loss due to the decline in net sales, but we worked rigorously to make sure that our balance sheet remained absolutely undamaged.

To be specific, we acted to reduce inventories by keeping an awareness about cash flows. Initially we aimed to reduce inventories by ¥5.0 billion – an amount that corresponded to our business loss. In the end, however, we successfully reduced inventories by more than this, leaving our balance sheet undamaged. I consider that this represents a certain level of achievement.

Two of our medium-term targets were to expand our business fields and to create a fifth pillar of business. We worked at these targets during fiscal 2010, including through M&As, but were not able to find any good business partners. I am, however, committed to continuing to explore the possibilities of technological tie-ups, including business capital tie-ups.

FISCAL 2011 OUTLOOK AND FUTURE INITIATIVES

It seems that the severe business environment will continue throughout the fiscal year ending February 28, 2011, in the light of the sudden worsening of business conditions until now, which was more severe than we expected, and the slow tempo of the economic recovery. For the fiscal year ending February 28, 2011 outlook, Star Micronics projects net sales of ¥30,100 million, an operating loss of ¥1,000 million and a net loss of ¥1,800 million. Considering the business environment, it is difficult to reasonably expect any substantial recovery in Europe and the U.S. We will therefore work to lower our break-even point by cutting back on fixed expenses, including by reducing personnel in our manufacturing plant in Dalian, China, and by curbing capital investment.

My basic policy for Star Micronics is not to merely expand our net sales but rather to give importance to profitability. We will therefore adopt a cautious approach to regions, products and customers that are associated with low profit margins, and we will focus management resources on those which will enable us to steadily secure earnings. In particular, I believe that consideration of our current situation as regards net sales shows that it is vital for us to select the regions and products where we can emphasize profitability.

From this viewpoint, I would cite China, Southeast Asia and South America as regions on which we should place importance. However, I think the products that we will succeed with will be low-priced with only certain selected functions, because there is a strong trend in these emerging nations for consumers to prioritize prices. Price competitiveness is particularly important in China where we also face competition from local manufacturers. In light of this, I believe it is essential for Star Micronics to strengthen its price competitiveness in China in the case of machine tools by lowering manufacturing costs by increasing the percentage of raw materials that are procured locally from inside China.

To give more detail, I would like now to describe the issues facing each of our business segments together with future strategies.

SPECIAL PRODUCTS

One issue facing this business is our approach to the markets of emerging nations such as China, Southeast Asia and South America. Because price competition is severe in these markets, Star Micronics is developing products targeting these emerging nations and building a corporate structure to rigorously achieve low costs. Based on our solid product lineup and sales routes established worldwide, we will identify and develop new channels in the markets of emerging nations.

Star Micronics is committed to developing high added-value products possessing differentiated functionality, mainly by utilizing software technologies.

COMPONENTS

In this business segment, the important issues are to rebuild product strategies with an emphasis on profitability and to develop new markets. This is because market needs are changing significantly and in the mobile phone market there is an increasingly marked polarization between demand for advanced functionality and demand for low prices. Leveraging its existing technologies, Star Micronics is developing the automobile-component and other markets by shifting from individual parts to composite high added-value products. Because users in the automobile-component market demand extremely rigorous levels of quality, our products do not seem to be succumbing to price competition with those of manufacturers in China and South Korea. Moreover, the number of installed audio products for cars has been increasing compared to the past, and so this will be a priority market going forward.

MACHINE TOOLS

The development of new products is one important issue in this business. In this context, Star Micronics expects to announce in the near future the development of products other than sliding headstock automatic lathes (Swiss-type automatic lathes). The market for conventional sliding headstock automatic lathes has been around ¥100 billion, whereas the market for the new products being developed is in the range of ¥300–400 billion. Consequently, we will enter and develop this new market.

Another issue in this business is our response to the increasing price competitiveness of the Chinese and other Asian markets. Star Micronics plans to launch machines with selected functions and an even better cost performance than our existing low-priced models.

PRECISION PRODUCTS

The important issue in the precision products business is to expand our sales overseas. Although our subsidiaries in Ayutthaya in Thailand and Shanghai in China produced a strong business performance, we will work to reduce costs through further rationalization and to stabilize quality and production.

At the same time, in Japan the precision products business mainly produces wristwatch components, and this is a mature industry. We will therefore transform the business structure to one facilitating low-cost operations.

In the medium and long term, Star Micronics will give greater importance to the three bases of Ayutthaya in Thailand and Shanghai and Dalian in China.

Through the steady implementation of these initiatives in these businesses, Star Micronics aims to return to profitability during the fiscal year ending February 29, 2012.

TOGETHER WITH OUR SHAREHOLDERS AND OTHER INVESTORS

The fundamental management policy of Star Micronics is not to merely pursue expansion of business size, but to develop businesses in growth industries and in global niche markets. We will always position ourselves in growth industries, and carefully observe which industries and sectors are growing and what products are needed. Furthermore, we will steadily implement realistic management, that is, implement effective growth strategies after properly evaluating our management resources.

Star Micronics will maintain the existing soundness of its financial structure, which is the foundation for improving these strategies. In the medium term, we are committed to preserving an equity ratio of at least 80%, and a ratio of net cash to total assets of at least 25%.

As regards the distribution of profits to shareholders, we still believe that the fact that we are a listed stock means we are supported by all our shareholders, and this in turn entails compensating them with dividend payments. Therefore, we are determined to achieve our target of a dividend payout ratio of at least 40% while taking into account our dividend on equity (DOE).

I expect the harsh business environment to continue throughout the fiscal year ending February 28, 2011. Nevertheless, Star Micronics aims to restore its business performance at an early date. I ask for the continued support and understanding of our shareholders and other investors as we work to meet their expectations.

May 2010

Hajime Sato
President and CEO