

## LETTER FROM THE PRESIDENT AND CEO

The sole objective function of a public company is to create growing sustainable value. Nissan is no exception; our market capitalization, which is the value of what our shareholders own, has increased from 1.2 trillion yen at the end of fiscal 1999 to 6.3 trillion at the end of fiscal 2005.

We approach shareholder value creation in a systematic manner, and have implemented Value-Based Management (VBM) as the strategic tool to achieve long-term value creation.

At Nissan, our three-year business plans are built around VBM. They clearly define a corporate objective with value-oriented operational and financial commitments. Under our third and current business plan, Nissan Value-Up, we aim to keep the "value-up" by building on the value created under the Nissan Revival Plan and Nissan 180.

Nissan's share performance since 1999 has been, in large part, a measure of our effectiveness in implementing VBM. Management systems are now fully consistent with VBM. And a value creation mindset is now pervasive throughout the company.

### **VBM at Nissan**

Our VBM has two stages. We first try to maximize our intrinsic value or the present value of risk-adjusted, expected future free cash flow. Through investor communications, we then try to manage the expectations of the capital market in order to ensure that our market value matches with our intrinsic value.

The first stage has three steps, planning, performance measurement, and compensation system.

Planning is the critical starting point in our VBM process. We look ahead three years and beyond to identify opportunities for growth and operational improvement. From this process, we determine our corporate objectives and value-oriented performance commitments.



For example, under Nissan Value-Up, we are focused on key value drivers, such as profitability, growth, and investment efficiency.

The other two steps, performance measurement and compensation system, are defined by our commitments. Each top-level commitment in the business plan is backed by specific commitments at every level of the organization. Everyone throughout Nissan knows what he or she must achieve. Close monitoring of performance creates an objective basis for a pay-for-performance compensation system. Our compensation system has played a key role in cultivating the value creation mindset in our company.

Our stock option plan is the best example. Employees must meet specific value-based

operational targets in order to exercise their options. This way, the interests of shareholders and employees are closely aligned.

But whether maximizing our intrinsic value in the first stage leads to maximizing shareholder value depends on the second stage, investor communications. Obviously, if the improvement in intrinsic value is not reflected in the market value, it does not reward shareholders at all. Therefore, the role investor communications plays in our VBM is significant.

The role of investor communications is to ensure that our market value tracks our intrinsic value. The benefit of being fairly valued is that we can learn from market signals. Since we believe that our share price is the most objective measure of our future performance, we use that feedback at the highest levels of the company. Obviously, obtaining this objective view is a benefit of being a public company. Therefore, if our share price fails to reflect our fundamentals due to noise and speculation, we lose the benefit of this effective tool. This is why we aim to maintain equity between our intrinsic value and market value.

#### **Result of shareholder value creation in fiscal 2005**

Although our share price appreciated 27.2 percent from the end of March 2005 to March 2006, it is clear that our financial performance has failed to meet the market expectations. Our share performance was lower than those of our key competitors and the overall market.

One apparent reason is that our profit growth appears to have flattened, despite another record year in terms of operating profit and net income.

Through reverse-engineering our share price at fiscal year-end – ¥1398 – another factor we identified is that the market expects lower long-term

earnings growth from Nissan, when compared to our key competitors. Since long-term earnings growth is a key value driver, this pessimistic market expectation resulted in the significantly lower share performance.

While our fiscal 2005 financial performance, as a snapshot of the company, was an average performance, we have made progress in terms of maximizing our intrinsic value. And as data from several third-party sources show, our non-financial leading indicators are moving in the right direction.

For example, our product value has been increasing. In the U.S., according to the J.D. Power and Associates 2005 Automotive Performance, Execution and Layout (APEAL) Study, a measure of owners' delight with the design, content, layout and performance of their new vehicles, both Nissan and Infiniti advanced their scores. Nissan maintained a significant gap against the non-luxury average and Infiniti moved past the luxury average. In addition, according to the Automotive Leasing Guide (ALG), key models for both Nissan and Infiniti are now fully competitive in their respective segments in terms of 36-month residual value. By model, the Altima has steadily improved its competitiveness in its segment and the Infiniti G35 sedan, the G35 coupe, and the M are competitive against well-established luxury models.

In China, Teana and Tiida were awarded the Car of the Year in 2004 and 2005 respectively. In addition, according to the J.D. Power Asia Pacific 2005 China APEAL Study, the two cars were ranked at the top in their segments. We also demonstrated significant improvements in customer service. According to the J.D. Power Asia Pacific 2005 China Customer Satisfaction Index (CSI) Study, Nissan was ranked as the top automaker and set a new benchmark with user-friendly service and service quality.

In terms of brand value, the overall value and strength of our brand is increasing. Measuring economic worth from 2003 to 2005, the BusinessWeek Global Brand Scoreboard shows Nissan as the fastest-growing automotive brand.

In order to succeed in the auto industry, a company must have strong products and a strong brand. Although improvement in those leading indicators is not fully reflected in our current profit, we believe that they are the drivers of our future growth.

#### **Outlook**

Fiscal 2006 will be a year of two distinct halves. Growth will be hard to achieve in the first half. Volumes will be down and our operating profit will be lower. In the second half, however, volume growth will increase and we expect our operating profit to accelerate as we launch eight all-new vehicles around the world.

The most important of these introductions will be in the U.S. We will launch all-new versions of the Altima, Sentra and the Infiniti G35 sedan, key models that will spearhead a product blitz that continues beyond Nissan Value-Up. During fiscal 2006, we will have 23 regional product-launch events around the world.

#### **Evolving VBM for the future**

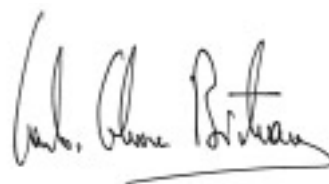
Although we have created shareholder value since 1999, in the past three years, our total return to shareholders has been lower than the overall market. Interestingly, our financial performances have improved over the same period. We interpret this to mean that we could not meet higher market expectations raised by the success of our revival. Even in our new phase, however, the measures we take to create shareholder value remain the same: further progress on key value drivers. Given our

improvement in non-financial leading indicators, we believe that we are moving in the right direction.

By contrast, our approach to investor communications must change to meet the needs of a new era. When we were in our recovery phase, investors naturally focused on our short-term health. As long as we talked in detail about our short-term goals and results, investors were satisfied.

As we enter a new era, investors' needs for transparency have changed significantly and our past level of transparency has become insufficient. Given that the majority of our current share price comes from expected future free cash flow beyond three years, it is reasonable for investors to want to understand our future vision and strategy. This change in focus has meant that investor communications has become a much more important task for the senior leadership team.

In recent years, we have seen an increasingly volatile and challenging business environment around the world. In this environment, only companies that create long-term shareholder value can survive. Therefore, value creation is no longer a mere expression of goodwill but must be the sole objective function of a public company. We will continue to pursue this objective based on our VBM: maximizing our intrinsic value and managing market expectations. Shareholder value creation is a never-ending quest at Nissan.



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