

An Interview with the President



MUTSUTAKE OTSUKA

President and CEO
May 2005

▶▶ OVERVIEW OF FISCAL 2005

Q. Looking back, what kind of year did JR East face in fiscal 2005, ended March 31, 2005?

A. Fiscal 2005 was the fourth year of our five-year *New Frontier 21* medium-term management plan. In light of our performance over the previous three years, from the start of the year under review I sought to bring forward the realization of *New Frontier 21*'s five numerical targets or to bring their achievement well within reach.

In the first half of the year, operations steadily progressed in line with projections. However, we struggled in the second half due to numerous natural disasters. The most damaging of those was the Niigata Chuetsu Earthquake on October 23, 2004. Also, a large number of typhoons and heavy snowfall posed challenges. Unfortunately, decreased revenue due to those disasters overshadowed steps taken during the year. Nevertheless, the measures that we rolled out in fiscal 2005 steadily produced tangible results.

Against that backdrop, JR East's revenues and earnings declined in fiscal 2005. We incurred losses totaling ¥60.3 billion including ¥14.1 billion of estimated decrease in operating revenues due to the Niigata Chuetsu Earthquake, and our decision to adopt accounting standards for impairment of fixed assets one year early resulted in the recording of impairment losses on fixed assets of ¥46.4 billion. Neither of those factors will have a residual effect on JR East's results in the current fiscal year or in subsequent years.

Despite the year's challenging operating conditions and decreases in revenues and earnings, based on

our policy of steadily enhancing returns to shareholders in light of performance trends while securing retained earnings, we raised the year-end cash dividend ¥500 per share, giving an annual cash dividend of ¥6,500. Further, because the achievement of *New Frontier 21* targets has been brought within reach, in January 2005 we announced our next medium-term management plan: *New Frontier 2008*.

Q. Could you please recount the specific measures implemented by JR East in fiscal 2005?

A. In railway operations, our October 2004 revision of service schedules generated positive results. Previous schedule changes have concentrated on enhancing the Tokyo metropolitan network. Moreover, the improvement of through services and seating services characterized our revision in October 2004. For example, we substantially increased through services on the Shonan-Shinjuku line, which led to a sharp upturn in passenger numbers. Before the schedule change, 60 thousand passengers a day used the line. Since the change, 130 thousand people a day travel on the line. Moreover, a JR East survey has shown that of those 130 thousand users, roughly 25% have switched over from the services of other railway companies. Thus, rescheduling has benefited revenues appreciably.

In seating services, we increased the number of line sections offering local train services with *Green Cars* (first class cars). In catering to passengers' seating needs and generating revenues from *Green Car* charges, those services have outperformed our projections. We estimate that stepped-up through services and *Green Car* services had added ¥2.5 billion to revenues for half a year by the end of March 2005.

In non-transportation operations, our shopping centers and office buildings businesses performed extremely well, posting improved revenues and earnings. Moreover, in the station space utilization segment, the March 2005 launch at Omiya station of *Ecute Omiya*, which we created guided by a new station retailing development paradigm, testified to the large potential for marketing activities in unified spaces within station concourses. In that sense, the unveiling of *Ecute Omiya* was an epoch-making event.



Further, because the achievement of *New Frontier 21* targets has been brought within reach, in January 2005 we announced our next medium-term management plan: *New Frontier 2008*.



Also, we continued to focus efforts on developing *Suica*, which has steadily grown in popularity since its November 2001 debut. Passing the 10-million landmark in October 2004, the number of *Suica* issued continues to climb and currently stands at more than 12 million cards. In *Suica* operations, we advanced the functionality of *Suica* by aggressively expanding the usage base of *Suica* electronic money and by forging alliances with companies in other industries in fiscal 2005. To give just one example, from September 2004 it became possible to make purchases using *Suica* electronic money at certain outlets of the major convenience store chain FamilyMart. Furthermore, *Suica* electronic money will be introduced into 1,000 FamilyMart stores in the *Suica* usage area during the current fiscal year.

In tandem with efforts to spread usage outside stations, we are expanding the areas in which *Suica* electronic money can be used inside stations. For instance, customers can now shop using *Suica* electronic money at all of *Ecute Omiya*'s 68 stores and the 21 stores of the *Dila* shopping mall at Nishi-Funabashi station. Moreover, by the end of fiscal 2005, customers will be able to use *Suica* electronic money anywhere within all 36 stations within the Yamanote line. Regarding card alliances, we have begun issuing *JALCARD Suica* based on a tie-up with Japan Airlines Corporation. Also, JR East has concluded alliance agreements with several banks and is proceeding with preparations. Such developments over the past year gave me a real sense of *Suica*'s future as JR East's third operational pillar.

▶▶ NIIGATA CHUETSU EARTHQUAKE

Q. Although the effects of the Niigata Chuetsu Earthquake have been accounted for in fiscal 2005 financial settlements, please give an overview of how the Niigata Chuetsu Earthquake affected JR East.

A. A massive earthquake struck the Niigata Chuetsu region at 17:56 on Saturday, October 23, 2004. At its strongest, the Niigata Chuetsu Earthquake had a seismic intensity of 7 on the Japanese scale of 0-7, registering a high of 2,515 gal, which is a unit of acceleration for measuring the momentary shock experienced by people and buildings.

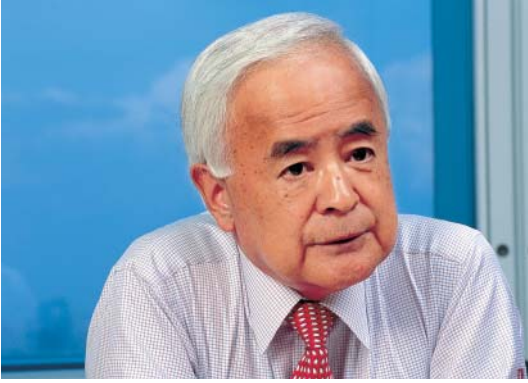
The Great Hanshin-Awaji Earthquake of January 1995 also had a seismic intensity of 7 at its strongest, but its maximum acceleration was 818 gal. Further, while the Great Hanshin-Awaji Earthquake hit early in the morning, before people had begun their day, the Niigata Chuetsu Earthquake occurred around 6 p.m., a time of day when people were still going about their daily lives.

At the time of the earthquake, seven Shinkansen and numerous conventional line services were operating in and around the area of the epicenter. Of those, the *Toki* No. 325 Shinkansen was running directly over the epicenter and derailed. Traveling at 200km/h, the Shinkansen took the full brunt of the intensity-7 earthquake, resulting in the first derailment of a Shinkansen since services began in 1964. Thankfully, no one was injured. The earthquake damaged not only trains and railway facilities but also JR East's hydroelectric power plants, which supplied approximately one-quarter of the electricity that we use. Those plants are still not fully operational.

The earthquake therefore dealt a very large blow to our operations. We incurred losses of approximately ¥60 billion due to the earthquake. Figuring in related capital expenditures, those amounts were roughly ¥68 billion. However, because we recorded the impact on profits and losses in the settlement of accounts for fiscal 2005, there will not be a residual effect on JR East's results in the current fiscal year or in subsequent years.

Although the damages it caused were large, the earthquake was a very valuable experience. Based on the lessons of the Great Hanshin-Awaji Earthquake, we had reinforced the earthquake resistance of structures to maintain their integrity in the event of an earthquake of a comparable intensity. At the same time, we constructed a system for the early detection of earthquakes that halts trains as quickly as possible when an earthquake occurs.

This latest earthquake clearly showed the benefits of those two initiatives. Our measures to reinforce structures against earthquakes proved particularly effective. In response to advice from our in-house technical team indicating that the area posed a threat because of a local fault line, we had strengthened the earthquake resistance



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of approximately 10 kilometers of the track segment on which the derailment occurred. As a result, structures were largely unaffected by the earthquake. Furthermore, the seven Shinkansen trains running near the epicenter were able to halt immediately. We were able to confirm the effectiveness of the earthquake countermeasures that we had taken.

I will not deny that it may have been “sheer good luck” or a “miracle” that no one was injured as a result of the derailment. However, the earthquake clearly demonstrated the validity and importance of preemptive measures that JR East had taken. There are no absolutes when it comes to safety, but efforts to minimize damage in the unlikely event of a disaster are important. Therefore, JR East will continue implementing the necessary measures aimed at achieving “ultimate safety” in its railway operations.

Q. How did you initially react to the earthquake, and what were your impressions of the subsequent restoration effort?

A. When the earthquake hit, I was in London as part of an overseas IR road show. It was the same date as Japan, October 23, but it was around 10 a.m. local time.

As soon as I heard the news, I returned to Japan. I took the first available flight, arrived in Japan in the morning of the following day, and went directly to Head Office, arriving here at about half past ten. Looking back on it now, I was in Head Office directing recovery efforts 17 hours after the earthquake struck.

The day after the earthquake, we gathered information and held meetings to formulate measures. However, because I did not know what the situation was on the ground, I visited the area by helicopter the next morning, on October 25. While taking a close look at the area, I sought to encourage our employees engaged in the restoration work.

Meanwhile, we had to maintain normal, safe train operations in the Tokyo metropolitan area and other areas. While attending to that imperative, I joined employees in the effort to restore services as early as possible.

I would like to talk now about my impressions of the recovery effort. It brought home to me anew the quality, sense of duty, loyalty, and professionalism of our employees. On many previous occasions, they had impressed me in this way, but the extreme conditions of an earthquake disaster left me with a profound sense of their commitment.

The crew members onboard trains affected by the earthquake rapidly took appropriate measures, from emergency stop procedures through to dealing with passengers. It would not be an exaggeration to say that their response was flawless. As a result, there was almost no panic among passengers. Thanks to a great number of JR East’s partner companies’ employees and our employees who worked in shifts day and night to restore damaged railway lines, we were able to resume services on Shinkansen and conventional lines by the end of the year. That momentous achievement was made possible by the high quality of each employee and their outstanding abilities and sense of responsibility as professionals; in other words, it was made possible by sound human resources. Going forward, I aim to manage JR East by implementing initiatives to further leverage those personnel capabilities. The earthquake also reaffirmed to us the importance of regular drills and education that enable employees to work as an integrated group and enhance the effectiveness of our organizational responses to emergencies. Accordingly, we intend to upgrade our training programs which bring out personnel capabilities further. Moreover, such educational efforts make an extremely valuable contribution to risk management. In those respects, my aim is to make JR East fundamentally sound and robust.

▶▶ NEW FRONTIER 2008

Q. Could you please explain the thinking behind the *New Frontier 2008* medium-term management plan, which began in April 2005?

A. *New Frontier 2008* is the first management plan that JR East has prepared as an entirely private-sector company.

As soon as it was established in April 1987, JR East sought to become a private company. Following amendment



Through the realization of those goals, our aim is to build an unshakeable management platform for sustainable growth in the medium-to-long term by the end of fiscal 2009.



of the JR Law in December 2001, the Japanese national government sold all of its remaining shares of JR East in a third public sale in June 2002, and we achieved our long-awaited goal of becoming a private-sector company. Soon after becoming president, I prepared our previous management plan, *New Frontier 21*, and launched it in fiscal 2002. The main aim of that plan was to realize full privatization; when I prepared the plan, there was no definite schedule for full privatization. Against the backdrop of an increasing emphasis on consolidated accounting among Japanese corporations, *New Frontier 21* was strongly focused on group management. Although that plan enabled us to aggressively develop group management, there was the risk that, because our performance was comparatively favorable, continuing the same targets would have made it difficult to maintain impetus.

Accordingly, I decided that we needed a new, greater sense of urgency. Establishing ambitious targets and paving the way to the next era were pressing issues. With those ends in mind, we established *New Frontier 2008*, initiating it in April 2005. We aim to meet customer expectations, the management philosophy underpinning *New Frontier 2008*. We have chosen this as a starting point because we realized that fulfilling customers' expectations is not necessarily an easy task. There are a variety of obstacles to realizing customers' expectations. However, we must clear those hurdles and take on the challenge of realizing a range of possibilities.

Further, I have given the plan a clear framework that comprises *3 Reforms*, *6 Challenges*, and *3 Benchmarks*. Through the realization of those goals, our aim is to build an unshakeable management platform for sustainable growth in the medium-to-long term by the end of fiscal 2009.

Of *New Frontier 2008's 3 Benchmarks*, the first is the achievement of total consolidated cash flows from operating activities of ¥2,000 billion over four years. The central plank of the plan's financial strategy is a new approach to the use of those cash flows. *New Frontier 21* gave first priority to debt reduction, and this remains a management issue of paramount importance in *New*

Frontier 2008. The distinctive characteristic of *New Frontier 2008* is that while reducing debt JR East will also use cash flows to undertake active capital expenditures. JR East intends to step up capital expenditures on implementing safety measures and undertaking major projects that increase the company's vitality.

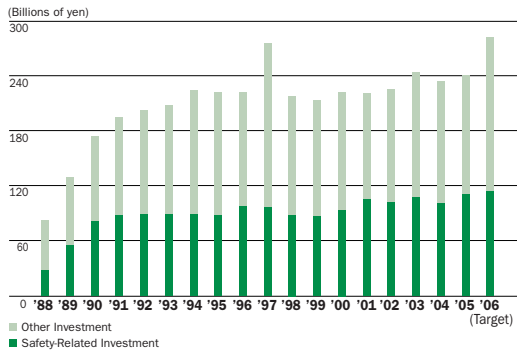
At the same time, we aim to increase returns to shareholders. Our dividend policy has been to conduct stable dividend payments while maintaining adequate retained earnings. During the term of *New Frontier 2008*, I believe that we have reached a point where we can increase returns to shareholders even while reducing debt and implementing investment for growth. Accordingly, in light of dividend payout ratios, I want to steadily increase dividend payments.

In line with our dividend policy of seeking stable dividend payments while considering dividend payout ratios, we plan to raise the cash dividend for fiscal 2006 from ¥6,500 per share to ¥7,000. Guided by *New Frontier 2008*, we will improve our performance and use cash flows to reduce debt, to provide returns to shareholders, and to advance forward-looking capital expenditures.

Q. How will JR East develop its business under *New Frontier 2008*?

- A.** The overriding aim of *New Frontier 2008* is to lay solid management foundations in the coming four years. At the same time, the plan looks beyond 2009 and calls for the pursuit of major projects that will come to fruition between 2010 and 2015. For example, we are undertaking various long-term initiatives to upgrade mainstay railway operations. After the conclusion of *New Frontier 2008's* term, we plan to complete the construction of a route that will join the Ueno-Tokyo segment of the Tohoku line, the Takasaki line, and the Joban line with the Tokaido line in fiscal 2010. The new route, which we call the Tohoku through line, will significantly enhance the convenience of our Tokyo metropolitan network via a different route from the Shonan-Shinjuku line. Further, by fiscal 2016 we plan to free up an extensive area of land in the Shinagawa district of central Tokyo through the reorganization of lines at our rail yard.

SAFETY-RELATED INVESTMENT (nonconsolidated)



In non-transportation operations, plans call for the development of space within the concourses of Shinagawa station and Tachikawa station using *Ecute Omiya*'s new format as a template. In the Tokyo station district, we will complete a series of office buildings that are set to become a solid source of earnings. Those projects include the 170-meter *JR East Tokyo Station Nihombashi Exit Building* (provisional name) and twin 200-meter towers on the station's Yaesu side.

Further, over the next four years, JR East will develop *Suica* operations into the third pillar of its business after transportation and non-transportation operations. To take an example, we plan to accelerate the development of *Suica* electronic money through such initiatives as increasing the number of affiliated stores. At present, *Suica* electronic money accounts for approximately 100 thousand transactions a day. By fiscal 2009, we aim to grow that to 4 million transactions. During fiscal 2007, we will dramatically increase the convenience of *Suica* by beginning joint usage with other railway companies in the Kanto region and bus companies. Also, January 2006 will see the practical application of *Mobile Suica*, which integrates *Suica* and cell phones. By adding communications and display functions of cell phones to *Suica* and through integration with the Internet, *Mobile Suica* will increase the possibilities of *Suica*, realizing such initiatives as the launch of digital Shinkansen tickets scheduled for 2007.

Q. How would you sum up New Frontier 21?

A. Although there are minor issues that remain to be addressed, I think *New Frontier 21* largely fulfilled the goals that I envisaged. However, I would like to make it clear that the principles of *New Frontier 21* have not become invalid. Rather, their effectiveness has enabled us to move on to *New Frontier 2008* a year ahead of schedule.

▶▶ SAFETY MEASURES

Q. What is JR East's safety philosophy?

A. Safety has been JR East's top priority since the company's incorporation. And, there will be absolutely no change in that mind-set.

In April 2005, the derailment of another railway company's rapid-service train at Amagasaki resulted in a catastrophe in which 107 precious lives were lost and more than 500 people were injured. I offer my sincere condolences and hope that the injured make a full and fast recovery.

In light of the lessons of that accident, JR East exhaustively reviewed its adherence to speed limits for trains, adherence to standards for the maintenance of railcars and structures, and supervision of crew members' health. Further, all of our directors visited worksites and exchanged opinions with employees to ascertain if there were any potentially dangerous aspects of our operations that we had overlooked. We categorically must not pass over the accidents of other companies as somehow having nothing to do with us. Ensuring the soundness of safety measures is an unending task. Therefore, aiming for "ultimate safety," we will do our utmost based on accumulated, day-to-day diligence.

Because they often span several years, our safety measures are based on medium-term plans. We are currently in the middle of implementing our fourth five-year plan since JR East was established, *Safety Plan 2008*, which ends in March 2009. Annually, our safety-related capital expenditures have been between ¥80 billion and ¥100 billion. As of fiscal 2005, JR East had spent a cumulative total of approximately ¥1.6 trillion on safety measures since its establishment. And, those investments have produced concrete results. Comparing the year of JR East's establishment, in fiscal 1988, with fiscal 2005, the number of operational railway accidents is about two-thirds lower, including a 75% reduction in accidents at level crossings.

On the other hand, we have not yet reduced accidents to zero. JR East operates more than 12,000 trains daily, and there is always the possibility that something will go wrong. Completely establishing



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absolute safety is very difficult. But, at the very least I want to make major accidents that cause significant damage a thing of the past. Based on the *Safety Plan 2008*, we are taking steps to eliminate fatal accidents involving passengers or employees.

►► CORPORATE GOVERNANCE

Q. Please outline the measures that JR East is taking to enhance corporate governance and to speed up decision making.

A. JR East employs an auditor system of governance comprising directors and auditors.

Companies have the choice of several types of governance system, including committee system forms of governance or systems that incorporate committees responsible for significant assets. In my view, companies should select systems based on a range of considerations, such as their industry type or business format. JR East's mainstay railway operations have certain distinctive features. Returns on investments are extremely long term. Extensive experience is needed to ensure safety—our first priority. Given those characteristics, medium-to-long-term thinking is important. Accordingly, I think that the auditor system of governance is best suited to JR East. At the same time, in my opinion governance is nothing more than a means to an end. Of most importance are the results that a particular system produces.

All governance systems have their demerits, and JR East is doing its utmost to compensate for the failings of its system. The auditor system's deficiencies are said to be slow decision making and the consolidation of, or a lack of clear separation between, operational implementation and the Board of Directors. In response, JR East has reformed its board to encourage free, lively debate and to speed up decision making. At its largest, the Board of Directors comprised 36 directors; at present, it has 23 directors.

Although, we plan to increase the number of directors to 24 in order to appoint a director responsible for a newly established IT operations headquarters in the June 2005 shareholders' annual meeting, there is no change in our commitment to vitalizing debate and accelerating decision making through the reduction of the number of directors.

Also, I believe that outside directors can play an important role. However, I am doubtful of the value of accepting outside directors without clarifying the functions that are expected of them. Obviously, the oversight of directors is one significant role outside directors should fulfill. Over and above that function, what matters is the type of opinions that outside directors convey. JR East has appointed two outside directors who have served as president and chairman in companies outside the railway transportation industry. Those directors offer the Board valuable opinions from the viewpoints of experienced senior executives.

Four of JR East's five corporate auditors are outside corporate auditors, including one legal and one accounting expert. Frequent input from auditors is one of the features of JR East's Board of Directors. Auditors often provide informative opinions and bring issues to the board's attention, which are reflected in management. Although such systems ensure adequate supervision and oversight of JR East's management, we intend to continue efforts to enhance corporate governance.

►► GOALS

Q. Lastly, how is JR East approaching the current fiscal year?

A. Fiscal 2006 is the launch year of *New Frontier 2008*, so we have to sprint forward to establish enough momentum to carry us through the next four years. For that reason, the current fiscal year is crucial—a point that I repeatedly impress upon all employees. By building on that impetus, I think that we could very well reach record net income in fiscal 2006.

Fiscal 2006 is also very important as a year in which we must pave the way to the next era. Although fiscal 2005 was a difficult year, it furnished us with valuable experiences. Therefore, I want to fully capitalize on the energy and confidence that we have gained by overcoming the previous year's adversity. I am fully confident that we will meet the expectations of our shareholders.

In closing, I ask all of our stakeholders for their continued support and understanding.