

Two years into our reforms, we are working to further accelerate the pace of change in order to stabilize profits.



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Steady progress on reforms under harsh market conditions

As the trend toward reducing or eliminating the use of agrochemicals continues in the agrochemicals business, there has been a gradual decline in the amount of agrochemicals used. With no change in the trend toward relocation of color chemicals processing facilities overseas, the domestic market for the color chemicals business continues to shrink. In the explosives business, policies to restrict public works remain in effect, and the market has continued to decrease in size. These conditions have been exacerbated by new problems, such as a squeeze on profits resulting from high materials costs, attributable to the soaring price of oil, and rising import prices due to the increasing value of the Chinese yuan. Under these conditions, the Fine Chemicals Group is working to ensure survival through reforms which will alter the structure of our business. The fundamental strategy behind these reforms is to change our business operations in order to adapt to changes in the market. Specifically, for the agrochemicals business the key is the introduction of new active ingredients and new chemicals, and development of new domestic markets. For the color chemicals business, it is expanding into the Chinese market and other global markets, and for the explosives business it is to expand our business by increasing market share and developing new applications and products. We have already taken steps in these directions. Two years have passed since these reforms were started, and steady progress is being made. However, we must further accelerate the pace of these reforms, and make the changes more substantial.

In the agrochemicals business: Elimination of past debts and rapid marketing of new products in the future

Compared with the previous year, both sales and profits for the agrochemicals business showed large declines in the fiscal year ended May 31, 2006, and were significantly worse numerically. However the primary reason for these results is that we eliminated our past debts, and we were finally able to arrive at a starting point for carrying out true reforms. In the future, we will accelerate the development of new products that are developed in-house, carry out purchases of chemicals and ingredients, and become aggressively involved in M&A and other efforts in order to resolve the greatest issue for this business: the rapid introduction of new products to the market. In the fiscal year ending May 31, 2007, we are planning to market two new products: one new biological pesticide and one plant protection agent. In addition, we are engaged in other top-priority issues, including strengthening and expanding domestic sales and improving the profit structure, and ensuring that these changes are maintained and fully applied.

Higher income and profits for the color chemicals business, with future focus on infrastructure improvements for the China business

For the first time in several years, the color chemicals business achieved both higher income and higher profits, due to factors such as large growth in the China business where our main efforts

have been focused, strong growth in the Japan market, and the effects of cost-cutting measures. Our China subsidiaries Wuxi Advanced Kayaku Chemical Co., Ltd. (WAC) and Zhaoyuan Advanced Kayaku Chemical Co., Ltd. (ZAC) are continuing to deliver both higher production quantities and higher total sales year after year. In the future we will further accelerate the pace of expansion for our business in China. China sales have been increasing at an annual rate of 50% or more, and have reached the point where we are at last aiming for the 1.0 billion yen mark. At this opportunity, we are working faster to create a master plan for the new color chemicals business, focused on achieving profits through this color chemicals business in China. Achieving the goals in this master plan is essential, and we are hastening to complete the necessary infrastructure improvements.

Large increase in profits for the explosives business, with future efforts to focus on using new products to improve market share

The top two priorities for the explosives business have been the

following: achieving cost competitiveness, and developing unique products. To cut costs, we have reviewed our raw materials, and have also conducted complete reviews of items such as changes in production methods, and as a result have successfully achieved our target. In addition, the development division, which succeeded in developing the world's first granular emulsion explosive (Landex), has been involved in on-site use and application of this product, and has developed a safe and inexpensive method of blasting. It is currently on the way to achieving success in full-scale sales. As a result of efforts for reforms such as these, despite a slight decrease in sales, we achieved a large increase in profits. In the future, we will focus on increasing the market share for the new product Landex, and developing new applied products that utilize the technology we have accumulated and refined in the past.

Topics

Construction of new research laboratories at the Kashima Plant, in order to accelerate the pace of product development

In May 2006, Nippon Kayaku completed construction of new agrochemical business research laboratories, which will focus primarily on agrochemicals, within the Kashima Plant in Ibaraki Prefecture. The completion of these new facilities means integration of the Research & Development Division and the Production Division. In order to increase profits under the increasingly difficult conditions of the agrochemicals industry, we will change the pivot point of the agrochemicals business from development of agrochemical active ingredients to improvement and development of chemical products, making full use of the active ingredients our company possesses. Strengthening cooperation between the R&D Division and Production Division is critical for the purpose of improving the speed of product development. In addition, having these laboratories close to the plant has many advantages when conducting effectiveness tests.

Increasing the production capacity for synthetic textile dyes at the China group company Wuxi Advanced Kayaku Chemical Co., Ltd.

Nippon Kayaku took the lead in the Japanese synthetic dye industry with its entry into China, establishing a joint venture company in Zhaoyuan City, Shandong Province in 1995, and in Wuxi City, Jiangsu Province in 1996. Nippon Kayaku provided 75% of the investment in Zhaoyuan Advanced Kayaku Chemical Co., Ltd. (ZAC), which is located in Shandong Province, and produces fluorescent dyes, primarily for paper pulp. Nippon Kayaku provided 80% of the investment in Wuxi Advanced Kayaku Chemical Co., Ltd. (WAC), which is located in Jiangsu Province, and produces and sells disperse dyes and water-soluble dyes for textiles.

WAC has an annual production capacity of 1,800 tons, and the production equipment is approaching full capacity. For this reason, we have introduced new production equipment for water-soluble reactive dyes with an annual capacity of 2,000 tons, which is scheduled to begin operating in 2006. The reactive dye for which production capacity is being expanded is primarily used for cotton, and is named KAYACION. Plans are to sell half of this increased reactive dye production in China, and the remainder in Japan and other countries.

Business Areas

Agrochemicals

We manufacture and sell agrochemicals and similar products.

Major products

- DIAZINON
- MATRIC
- SAFROTIN
- EVISECT
- CYCLOSAL
- MCPB
- CHLOROPICRIN
- CUCUMERIS
- RATDEN
- SIMETRYN
- CHLORPIC-FLOW



Color Chemicals

We manufacture and sell textile dyes and dyes for paper pulp.

Major products

- KAYALON POLYESTER
- KAYACRYL-ED
- KAYACELON REACT
- KAYARUS
- KAYACION
- KAYAFECT
- KAYAPHOR LIQUID
- KAYASET



Explosives

We manufacture and sell explosives, black powder, and pyrotechnic products.

Major products

- Dynamite
- Slurried Explosives
- Ammonium Nitrate Fuel Oil Explosive (ANFO Explosive)
- Black Powder
- Electric Detonators

