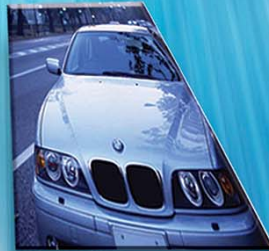
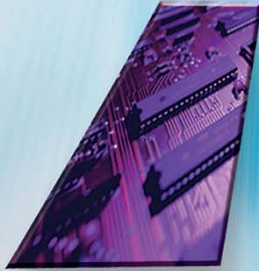


Annual Report 2007

Year ended May 31, 2007



United on the Path for Growth

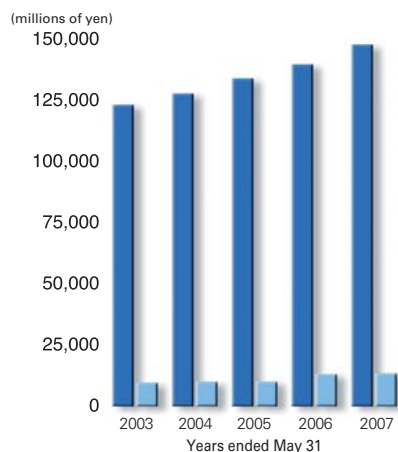


Consolidated Financial Highlights

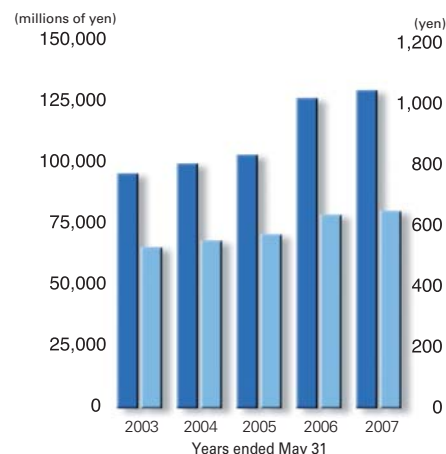
	Millions of yen, except per share amounts				
Years ended May 31	2007	2006	2005	2004	2003
Net Sales	148,124	140,026	134,205	128,016	123,431
Operating Income	13,536	13,219	10,166	10,097	9,697
Income before Income Taxes and Minority Interests	13,608	18,629	10,404	8,941	7,643
Net Income	6,610	9,641	5,315	3,926	2,780
Shareholders' Equity*	130,233	127,030	103,810	100,207	96,204
Shareholders' Equity per Share (Yen)	646.78	634.51	570.31	550.12	527.93
Net Income per Share (Yen)	36.37	52.92	28.87	21.22	14.92

* Shareholders' equity for years ended May 31, 2003, 2004, and 2005 does not include minority interests.

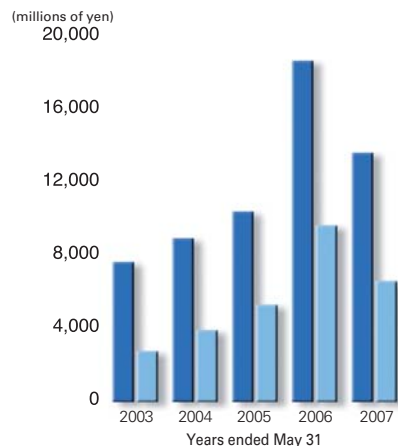
■ Net Sales
■ Operating Income



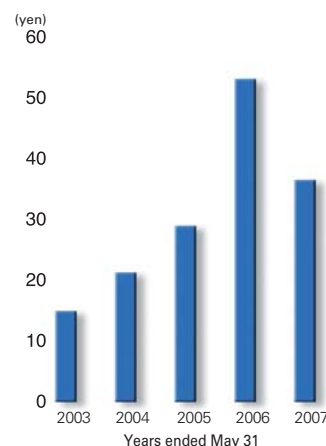
■ Shareholders' Equity
■ Shareholders' Equity per Share (right scale)



■ Income before Income Taxes and Minority Interests
■ Net Income



■ Net Income per Share



* Company information after May 31, 2007 is disclosed as part of company information herein.

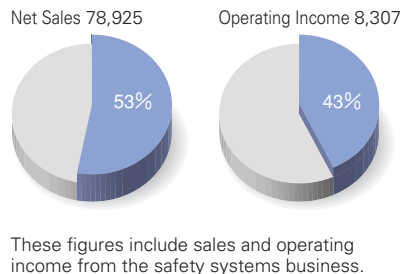
* Descriptions about future results imply uncertainty and risks, and do not guarantee realization of these results as such. There are possibilities that discrepancies will occur between goals and results due to such factors as changes in management environment.

Business at a Glance (year ended May 31, 2007 unit: millions of yen)

Functional Chemicals Business

Manufacturing the parts and materials essential for IT products

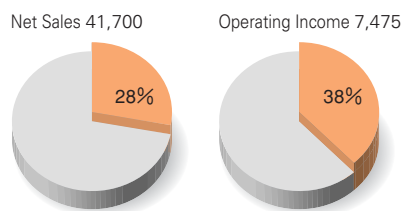
Among Nippon Kayaku's various strengths are the high-performance plastics that are at the heart of cell phone and digital information home electronics, optical functional films, and a wide range of products utilizing applied dye technology. Our products hold an approximate 40% share of the global market for epoxy resins used in the encapsulation of semiconductors, and our materials for liquid crystal projectors are highly rated. In addition, we also manufacture and sell the catalysts that are used in the production of acrylic acid and methacrylic acid.



Pharmaceuticals Business

Specializing and expanding our activities in cancer-related fields

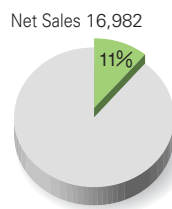
We maintain extensive original expertise related to research and development, production, sales, and aftermarket investigations of anti-cancer drugs, and our lineup of cancer-fighting drugs and related products has reached 27 products (as of July 2007). We are also strengthening our licensing activities, and are introducing generic products in order to expand our cancer-related business.



Safety Systems Business

Manufacturing components for airbags and other automobile safety systems

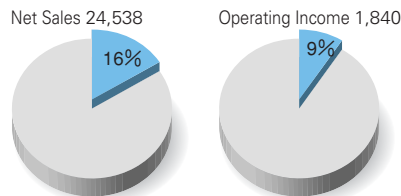
We manufacture and sell the inflators that generate gas for airbags that protect occupants in the event of an automobile accident, micro gas generators for seatbelt pretensioners, and the squibs (igniters) used in these products. We have constructed a global production and supply system based in Japan, North America, and Europe, and are working to expand our business in this area.



Fine Chemicals Business

A field generating stable profits, comprising business fields such as agrochemicals, dyes, and explosives

We operate our agrochemicals business for the development, manufacture, and sale of chemicals used in agriculture; our color chemicals business for handling the dyes for coloring textiles, paper pulp, plastic/resin and other materials; and our explosives business for handling industrial explosives and pyrotechnic products.



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Striving for No. 1 globally in niche markets We are promoting a fusion of technologies, and improving the speed at which we bring products to the market.

Increased income and profits in consolidated results for the year ended May 31, 2007

In the fiscal year ended May 31, 2007, net sales for the Nippon Kayaku Group were 148.124 billion yen, an increase of 8.097 billion yen from the previous fiscal year. Operating income was 13.536 billion yen, an increase of 316 million yen from the previous fiscal year. Net income decreased to 6.61 billion yen, a drop of 3.03 billion yen compared to the previous fiscal year that included the sale of land at a former company housing site.

During the period, several important moves were made involving business transfers and integrations. One involved a polymer coagulant business transfer, which completed the liquidation of subsidiary company Kayafloc Co., Ltd., in November 2006. We also agreed to the integration of our commercial explosives business with Asahi Kasei Chemicals Corporation, and promoted the creation of a stable, high-quality product supply system.

From the top down, we are promoting the introduction of new products to the market through a fusion of technologies.

As an integrated company, Nippon Kayaku fuses together cultivated technologies and has inherited genes that enable us to change with the demands of the times. In recent years we have established a strong position in three growth fields: information/communications, health care, and safety systems; and are promoting a fusion of technologies from each field, as well as efficient business expansion.

It is said that great innovations come not from a single technical field alone but from a mix of multiple technologies, including fields that seem to have no relationship to each other. This was why we opened the “Integrated Research Laboratories” in April of last year. These research facilities for the dual growth fields of pharmaceuticals and functional chemicals physically adjoin each other, enabling interaction to proceed naturally and efficiently. Technological fusion that had once seemed inconceivable has now actually begun.

Moreover, at the end of the year before last, we renovated our R&D system and launched the “Research and Development Management Committee.” As the company’s president, I serve as committee chairman. The committee, whose members include the directors of each research facility, aims to speed up companywide marketing of new products in the three growth fields we target, utilizing an effective top-down approach.

From the successful fusion of our technology platforms, rewarding new technologies such as ultrafine diamonds, dye-sensitized solar cells, and polymer micelle DDS (Drug Delivery System) drug formulations have already come into existence. Ultrafine diamonds have been developed for optical materials and coating applications. Dye-sensitized solar cells, which generate electricity using dyes that react to light, can obtain voltages 1.5 times greater than silicon-based cells, the mainstream type today. And polymer micelle DDS can efficiently deliver cancer-fighting drugs directly to cancerous areas of the body.

One year since the introduction of the project system, we are transforming into a strong company.

In order to quickly grasp the changes of the times and prevail in global competition, we introduced a project system last year. Under this new system, each project is headed by a strong leader, with project members consisting of personnel from related departments who establish achievement targets and time periods, and work together to resolve key issues. As company president, I, along with the director of the Research and Development Group, periodically confirm the status of progress while pushing the project forward.

Starting with R&D projects that are aimed at quickly bringing new products to market, we are presently promoting approximately 150 projects dealing with such issues as business and sales strategies, production improvement, and cost reductions. In the future we will be classifying the projects and providing expanded follow-up, and will create an organizational structure that enables even speedier responsive action.

As we fulfill the corporate social responsibilities, we are striving to be No. 1 in global niche markets.

While we expect that the Japanese economy will continue its present gradual expansion, there are also eventualities that can defy prediction, such as a possible slowdown in the U.S. economy or a spike in the price of oil. In the midst of such difficult circumstances, the Nippon Kayaku Group will fulfill its social responsibilities, work toward fusing technologies and strengthening its structure, and further expand its growth-field businesses as it strives to be No. 1 in global niche markets.

October 1, 2007

Koichiro Shimada

Koichiro Shimada
President



We are working to ensure that a common direction is shared making our strategies more effective to maximize the value of

I. Basic Strategy

We are rapidly advancing our business strategies, utilizing a fusion of technologies from within and beyond the company as a tool that enables us to target niche markets while remaining focused on markets and customers.

In June of last year, the Nippon Kayaku Group celebrated the 90th anniversary of its founding. As we move forward, we will continue to press for uninterrupted progress and conscientious cooperation to deliver the highest-quality products to global niche markets. We aim to maximize the value of our business in every area and meet the expectations of our shareholders, investors, and business partners.

In recent years, the Nippon Kayaku Group has proceeded with concentrating and selecting its business. We nevertheless remain involved in a large number of fields to create an appropriate group of companies and have positioned these activities as important strategies for achieving growth. We maintain a strong presence in the fine chemicals field and target many business areas where we have applied our fine chemicals technologies. We believe that centralized and consistent management of our operations in these fields is key to increasing the value of our business now and into the future.

II. Business Operations

We have established the information/communications field, health care field, and safety field as growth markets, and are operating efficiently in niche global markets that suit the size of our business.

In the information/communications field, we are working to expand sales of environmentally friendly epoxy resins that meet the changing needs of the market, as well as other high-performance materials such as colors for inkjet printers, functional films, and resins for LCD panels. At the same time, we are also working to develop new products with high added value.

In the health care field, we are specialized in cancer-related fields, and will be focusing on the early releases of new products and on expanding sales of our generic pharmaceuticals, while maintaining sales of our existing anti-cancer drugs. We are also accelerating the development of our anti-cancer drug DDS (drug delivery system) that makes extensive use of nanotechnology, and are targeting an early product release. In the safety field, we are working to boost business by expanding sales of new airbag inflator products, and by manufacturing and selling micro gas generators for seatbelt pretensioners using a global production and supply system based in Japan, North America, Europe, and China.

III. Key Policies

(1) We have positioned the functional chemicals, pharmaceuticals, and safety systems business as growth-promotion fields, and the fine chemicals business as a business for delivering stable profits.

For our future operations, we have positioned our functional chemicals business, which is focused on the information/communications field, our pharmaceuticals business, which is focused on the health care field, and our safety systems business, which is focused on the automotive safety field, as growth-promotion areas. On the other hand, we have positioned our fine chemicals business, which involves products such as agrochemicals, dyes, and explosives, as a business expected to deliver stable profits.

We will thus concentrate our business resources primarily in the growth-promotion businesses, aiming to achieve growth and expansion through rapid research and development.

In our business aimed at stable profits, we will take steps in order to secure a stable profit base, such as thorough cost-cutting and marketing new products that meet market needs.

(2) We are strengthening our company-wide R&D system.

For research and development, we will generate new progress by creating a fusion of elements including our core technologies, patents, and production technologies. Nippon Kayaku is accelerating the creation of characteristic new businesses and new products through such R&D activities as the development of inkjet printer colors using applied dye technologies, optical functional films and other electronic information materials using applied color and resin technologies, automotive safety products using applied explosives technologies, and anti-cancer drug DDS pharmaceuticals using applied polymer technologies.

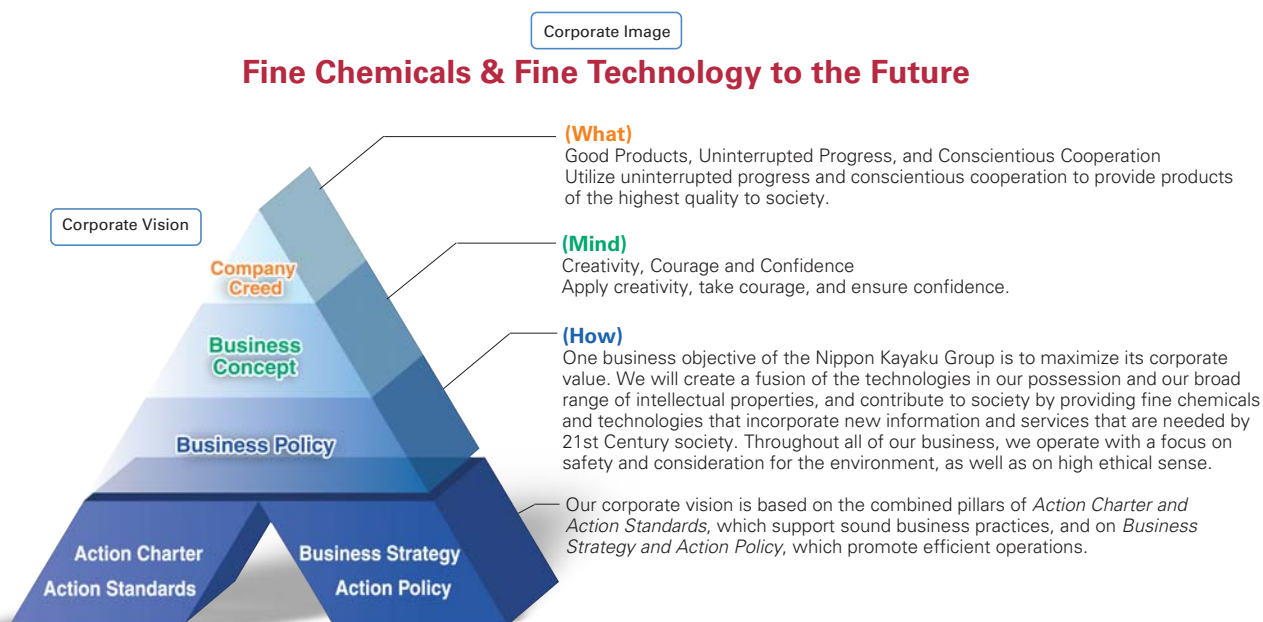
(3) We are working to further improve the health, soundness, and transparency of our operations.

In addition to ensuring safe operations, the Nippon Kayaku Group is focused on concern for the environment, and is continuing to maintain a high ethical sense throughout all of the Group's business operations. We are also strengthening corporate governance and the internal control system, and are working to ensure total compliance and improve the health, soundness, and transparency of our operations.

among all Group companies as well as our business in every area.

We have spawned a company-wide “KAYAKU Spirit,” aimed at strengthening the organizational power of the entire Nippon Kayaku Group, and are working to ensure that the global group shares a common direction.

In addition to the six Nippon Kayaku plants and four research facilities in Japan, the Nippon Kayaku Group is a global enterprise with 46 Group companies (as of May 2007) in Japan, China, Taiwan, the United States, Germany, and the Czech Republic. In order to match the speed of changes in the global markets and accelerate an effective fusion of technologies, we have created a campaign to instill a company-wide “KAYAKU Spirit” to indicate the necessary direction for the Group, and are working to see that it is shared by all Group employees.



Major Group Companies

Polatechno Co., Ltd.

This company was founded in 1991 as a joint venture with Arisawa Manufacturing Co, and in 1999 it became a consolidated subsidiary of Nippon Kayaku. In March 2006, it was listed on the JASDAQ Securities Exchange. Currently its primary products are polarizing films for the LCD displays used to display information on PCs or home electronics. This company has delivered excellent business results.

Kayaku Chemical (Wuxi) Co., Ltd.

This company was founded in 2002 in the city of Wuxi, Jiangsu Province in the People's Republic of China. It manufactures and sells UV-curing resins in the Chinese market.

LifeSparc Inc.

This company was founded in 2000 in Hollister, California in the United States. It manufactures and sells squibs and micro gas generators for use in automotive safety systems. This company functions as part of our global network for the Nippon Kayaku safety systems business.

Indet Safety Systems a.s.

This company began operating in 1999 in the city of Vsetin in the Czech

Republic. It also manufactures and sells squibs and micro gas generators for use in automotive safety systems. This company functions as our base for the Nippon Kayaku safety systems business in the European region.

Nippon Kayaku Food Techno Co., Ltd.

This company was founded in 1995 for the purpose of manufacturing and selling food preservatives and health food products. The food preservative business features an extensive lineup of products, and also provides comprehensive food sanitation management systems, contributing to a safe and rich food culture.

Wuxi Advanced Kayaku Chemical Co., Ltd.

This company was founded in 1996 in the city of Wuxi, Jiangsu Province in the People's Republic of China. It manufactures and sells textile dyes.

Zhaoyuan Advanced Kayaku Chemical Co., Ltd.

This company was founded in 1996 in the city of Zhaoyuan, Shandong Province in the People's Republic of China. It manufactures and sells dyes primarily for use in paper pulp processing.

Functional Chemicals Business

We are taking the lead in global trends such as environmentally friendly electronic components and electronic parts for automobile aiming to gain the No. 1 position in global niche markets.

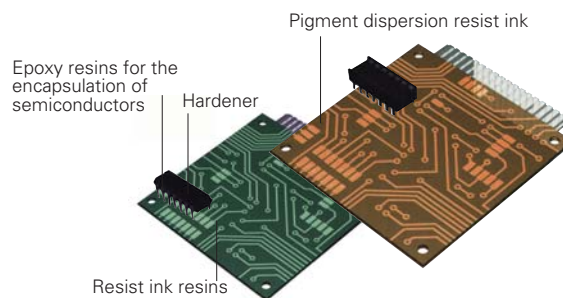


Functional Materials Business

Business Overview

Our functional materials business includes the development, manufacture, and sales of epoxy resins used worldwide for the encapsulation of semiconductors, UV-curing resins, and other functional materials.

This crucial business covers a broad range of functional materials, including epoxy resins used for the encapsulation of semiconductors, RC resins that cure under exposure of ultraviolet light, and polyimide/polyamide resins, the character of which is high durability. Our consolidated subsidiary in this field, Kayaku Chemical (Wuxi) Co., Ltd., produces and sells RC resins in the rapidly expanding Chinese market.



Market Trends and Overview of Operations for the Fiscal Year Ended May 31, 2007

We were able to achieve modest growth despite adverse effects of the declines in the PC and cellular phone industries.

During the first half of the year ended May 31, 2007, the strong performance within the information/communications industry helped the Nippon Kayaku Group deliver good business results. However, the industry was struck by a subsequent fall in demand during the second half of the year, slowing it and limiting our growth over the full year to a more modest level.

In the field of epoxy resins, Nippon Kayaku is almost entirely specialized in the resins used for semiconductor encapsulation, and we were affected by production adjustments among semiconductor manufacturers.

Our RC resin business was similarly affected by production adjustments among semiconductor manufacturers and manufacturers of FPD (flat panel displays) and other digital home electronics. Because RC resins are also used as the hard coating that helps prevent scratches on cellular phones,

production adjustments of cellular phones had an adverse effect on this business as well.

Business Objectives and Strategies

We will actively introduce new products that are adapted to developing market trends, for example by expanding our business in environmentally friendly epoxy resins.

As a top quality epoxy resin, environmentally friendly NC-3000 has established a position as the *de facto* standard in the market. In the future, we intend to introduce this environmentally friendly type epoxy resin to larger markets where specialized quality that matches the purpose of use is required.

In the field of RC resins, we have succeeded in developing photoresist dry film materials. In addition, as the broad transition to electronic parts for automobile continues, we are actively working to develop excellent new products in this field.

For polyimide/polyamide resins, we are expecting to increase sales by developing and producing products that meet customer needs.

Electronic Materials Business

Business Overview

We develop, manufacture, and sell functional films, optical disc materials, and other materials that are used for essential parts of information/communications devices.

Nippon Kayaku is actively expanding its business in the information/communications field, a sector we have identified as an important growth field. Our electronic materials business covers functional films, colors for inkjet printers, optical resins, and resins for LCD (liquid crystal display) panels – all products that are essential in the manufacture of information/communications devices.

Polatechno Co., Ltd. is a consolidated subsidiary of Nippon Kayaku that manufactures the special polarizing films needed for LCD displays. These polarizing films were developed using dye technology that is one of our specialized technologies. Unlike the iodine-type polarizing films used in the production of large LCD panels, these products manifest their strength in the niche market of mid- and small-size panels, such as for automobile displays, where high durability is required.

Nippon Kayaku also markets optical functional films for PDP (plasma display panels), colors for inkjet printers, and adhesives for DVD discs, as well as sealant for LCD panels,

pigment dispersion resins for digital camera CCDs, and numerous other products.



Market Trends and Overview of Operations for the Fiscal Year Ended May 31, 2007

Performance in the functional film and DVD adhesive fields was sluggish as a result of fluctuations in the information/communications industry, however sales of colors for inkjet printers were strong.

Sales of the optical films marketed by Polatechno Co., Ltd. grew steadily, centered primarily on dye-type polarizing films. In the field of optical functional films for PDP, while there were severe demands for cost-cutting as the price of plasma televisions declined, there were also several factors that increased their cost, such as a stronger requirement for high quality. Under these conditions, because Nippon Kayaku was overly focused on profits and did not carry out an expansion strategy, sales fell below the plan targets.

In the same way as the functional materials business, sales of DVD adhesives were affected by production adjustments in the information/communications industry, and fell below the plan targets. However sales of LCD sealant and colors for inkjet printers showed robust growth.

Business Objectives and Strategies

With products such as colors for inkjet printers and products for next-generation DVDs, we are actively working to identify and enter new markets.

In the PDP film field, in August 2006 we constructed a trial model line for high-performance optical films at our Fukuyama Plant, and are aiming to expand business in this field by producing higher-performance films. We are also conducting research related to UV-curing sealants for large LCD panels to permit us to expand into this field as well. The polarizing films sold by Polatechno Co., Ltd. are increasingly used for automobile instrument panels and other purposes, and continued strong sales are expected.

As the size of the market grows, we are also focusing on expanding our business in the field of colors used in inkjet printers.

In addition, with the launch of the next-generation DVD market, we expect growth in the DVD adhesive field as well.

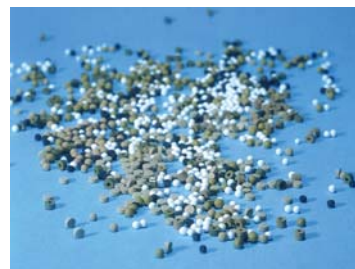
Catalyst Business

Business Overview

We develop, manufacture, and sell catalysts used in the production of acrylic acid and methacrylic acid.

The Nippon Kayaku catalyst business comprises the development, manufacture, and sales of catalysts that play a fundamental role in the production of acrylic and methacrylic acid. Acrylic acid serves as a raw material for a large number of products, including SAP (super absorbent polymers) that are utilized in consumer items such as disposable diapers, and also in acrylic paints, adhesives, and RC resins for automobile production and other purposes. Methacrylic acid is used in FPD light-guide plates and other optical applications, as well as in products such as transparent plastics used for giant aquarium tanks, automotive parts, and artificial marble. Both acrylic acid and methacrylic acid (utilizing the direct-oxidation method) require catalysts for their production, and Nippon Kayaku catalysts are highly popular thanks to their high performance.

In this field, we are also engaged in the plant licensing business, in which we provide the necessary technologies for the start-up and operation of plants that produce acrylic acid and methacrylic acid. In this way, we are putting our catalyst-related expertise to good use.



Market Trends and Overview of Operations for the Fiscal Year Ended May 31, 2007

With increased first-time use of our catalysts by overseas customers, we achieved sales that were significantly higher than the previous year.

The number of plants producing acrylic acid and methacrylic acid has been increasing overseas in recent years, and the Nippon Kayaku catalyst business has adopted a global business strategy. In particular, we have been successful in increasing the use of our catalysts by overseas customers, and this year achieved sales that were significantly higher than the previous year.

Business Objectives and Strategies

We will expand our catalyst business in coordination with our plant licensing business.

We will continue dedicating our efforts to the plant licensing business in the future. We will also complete our third catalyst plant, improve our production capacity, and further expand our business.



Keizo Shimomiya
Member of the Board
Managing Director
Director of Functional
Chemicals Group

Topics

Start of in-house production of films for plasma display

In August 2006, Nippon Kayaku's Fukuyama plant completed the construction of facilities for trial production and in-house production of optical films used for plasma display panels.

Until recently we have produced inks for optical films in-house, and have contracted outside sources to process the films. Now, by having our own preproduction and production facilities, we have created new film processing techniques and established facilities that can carry out consistent development and production, from ink manufacture to film processing. These facilities will be effectively utilized to keep pace with the flat panel television market, which is rapidly expanding worldwide. In the future these preproduction and production facilities will also be used to develop next-generation materials, perform speedy product development, and operate as a model line.



Newly built facilities for optical films

Facility buildup aimed at increased production of LCD films for automobile

By the summer of 2008, Dejima Optical Films B.V. of Holland, a subsidiary of Polatechno Co., Ltd., plans to increase its capacity to produce special phase difference films by four times the current level to at least 200,000 square meters annually to meet rising demand for these films in automobile LCD components.

As well, by the fall of 2008, Polatechno will expand its head office plant facilities in Niigata Prefecture by building a new plant for dye-type polarizing films used in LCDs for automobile. This facility expansion in Japan will boost production capacity, including for iodine-type polarizing films, by one and a half times the current level to 6 million square meters per year.

These enhancements are being made to meet expanding global automobile production as well as widening adoption of LCDs for information panels and other products. Since LCDs installed in automobiles display speed and other important basic information, automotive components are expected to be highly durable.

Production of special phase difference films requires special technical capabilities, which makes it difficult for other companies to participate in its production. In particular, the dyes required to manufacture dye-type polarizing films are a specialty of Nippon Kayaku. In such ways, Polatechno is developing this important business by harnessing the strengths of companies and key specialties within the Nippon Kayaku Group.

Nippon Kayaku products used in constantly evolving cell phone technology

Cell phones are among the most obvious examples of communications devices that are ever increasing in functionality. Our company's functional materials and electronic materials have become absolutely essential for their production.



Pharmaceuticals Business

We are expanding our lineup of products in specialized cancer-related fields and establishing superiority in the supply of highly reliable products and information.



Business Overview

We now have a lineup of 20 anti-cancer products, which began with the marketing of the anti-cancer drug BLEOMYCIN.

The history of Nippon Kayaku anti-cancer drugs began with the marketing of BLEOMYCIN in 1969. BLEOMYCIN is a cancer-fighting compound that was discovered by KyotoBiken Laboratories, Inc. and developed by our company. It was found to be effective against skin cancer and several other forms of cancer. Because at that time cancer was largely thought to be incurable, when it was reported that there were cases of cancer cells being eliminated by the use of BLEOMYCIN, "cancer cured by drugs" became a major news story.

Since that time, we have continued with research and development aimed at overcoming cancer, and our current lineup of cancer-fighting drugs has grown to 22 products, including generic versions. As a cancer specialty firm, we are proud of our lineup of anti-cancer drugs, which is the largest of any pharmaceutical manufacturer in Japan. These potent drugs are effectively used in treating a broad range of cancers, including cancers of the lung, stomach, breast, liver, and prostate. We will work to further expand this extensive lineup, in hope that Nippon Kayaku can be as much help as possible to patients who are battling cancer.

It is important that highly reliable information concerning anti-cancer drugs be provided to medical institutions. Nippon Kayaku maintains a staff of more than 400 MRs (medical representatives), of whom approximate 100 are cancer specialist MRs. A variety of training programs give our cancer specialist MRs a broad range of knowledge about cancer, including the latest treatment methods and academic information. These MRs provide fast and extremely reliable information to doctors, pharmacists, and nurses at specialized cancer facilities, university hospitals, and key regional hospitals.

As a specialty firm in the niche market of cancer-related products, we intend to make full use of the expertise we have developed over many years concerning development, production, and the provision of information in order to contribute to health care.

Major Products The year in parentheses is when the product was first marketed.

Anti-Cancer and Cancer-Related Drugs

- GRANISETORON Inj NK (2007) ①
- LEVOFOLINATE (2007) ②
- PACLITAXEL Inj NK (2006) ③
- GELPART (2006) ④
- CALSED (2005)
- EPIRUBICIN (2005)
- IA CALL (2004)
- ONCOVIN (2004)
- EXAL (2004)
- CARBOMERCK (2003)
- IMMUCYST (2003)
- HYCAMTIN® (2003)
- MS-TWICELON (2001)
- COFORIN (1996)
- FARESTON (1995)
- ODYNE (1994)
- STARASID (1992)
- PINORUBIN (1988)
- LASTET (1987)
- BESTATIN (1987)
- RANDA (1984)
- PEPLEO (1981)
- BLEO (1969)



Immunosuppressants

- SPANIDIN (1994) ⑤



Cardiovascular Drugs

- MILLISROL for Coronary Infusion (2001)
- ADEHL (1999)
- MILLISTAPE (1998)
- NITROPEN TABLETS (1988)
- MILLISROL (1984) ⑥



- NITROGLYCERINE TABLETS (1953)

Neurological Drugs

- SALIGREN (2001)
- MUSCALM (1975)

Other Drugs

- ASTRIC DRY SYRUP (2002) ⑦



Diagnostic Agents

- LANA MAMMO CARD CEA (2002) ⑧



- LANA 1,5AG AUTO LIQUID (2000)
- LANAZYME BFP PLATE (2000)
- LANAZYME ST-439 PLATE (1999)

Status of New Product Development by Stage

(as of October 1, 2007)

Stage	Development code Product name (Generic name)	Dosage form or route of administration	Therapeutic category (Indications)	Domestic developer	
				Origin	Characteristics/Others
NDA	NKT-01/ SPANIDIN (Gusperimus hydrochloride)	Injection	Immunosuppressant (Wegener's granulomatosis)	Own development Institute of Microbial Chemistry	Developed overseas. Designated as an orphan drug (Mar. 2001) by the EMEA.
	NK211/HYCAMTIN® (Nogitecan hydrochloride)	Injection	Anti-cancer (Ovarian cancer)	Own development GSK	Extended indication
Phase III	IMMUCYST PMCJ-9 (Connaught strain BCG)	Bladder instillation	Anti-cancer (for preventing recurrence of bladder cancer)	Own development Sanofi Pasteur (Canada)	Extended indication
Phase II	NK911 (Micelle doxorubicin hydrochloride)	Injection	Anti-cancer	Own development Tokyo Women's Medical University	Macromolecular micelle anti-cancer drug. Basic patent license obtained from Japan Science and Technology Corp. Development in other fields being considered.
	NS75A (Cetrorelix acetate)	Injection	Anti-hormone (Hysteromyoma)	Joint dev. with Shionogi, Kayaku Zentaris Zentaris (Germany)	LHRH (hormone that stimulates secretion of pituitary gonadotropin) antagonist
Phase I	NK105 (Micelle paclitaxel)	Injection	Anti-cancer (Solid cancers)	Own development Joint dev. with NanoCarrier	Macromolecular micelle anti-cancer drug
	NK314	Injection	Anti-cancer (Solid cancers)	Own development	New cytotoxic anti-cancer drug
	NK012 (Micelle camptothecin analogue)	Injection	Anti-cancer (Solid cancers)	Own development	Macromolecular micelle anti-cancer drug. Developed simultaneously in Japan and US.
	NK292	Oral preparation	Anti-cancer (Breast cancer)	Own development	New drug for treatment of breast cancer

Market Trends and Overview of Operations for the Fiscal Year Ended May 31, 2007

We have successfully boosted income and profits by adapting quickly to the market, for example by marketing generic cancer-fighting drugs that meet the market needs.

Negative factors during the fiscal year ended May 31, 2007 included a revision in drug prices and the effects of competitor generic products on our primary products RANDA and MILLISROL. On the other hand, positive factors included higher sales of new and recently introduced products within the first 2 – 3 years after their entrance to the market, and also higher sales of our generic anti-cancer drugs. The positive factors outweighed the negative factors, and as a result we succeeded in boosting overall income and profits.

By marketing generic anti-cancer drugs, Nippon Kayaku hopes to reduce the costs borne by patients. We put the same focus on quality and stable supply for our generic products as we do for the branded pharmaceutical products we developed ourselves. In addition, by regularly providing complete product information to medical institutions, we are working to ensure that our products are highly trusted.

It is also important to shorten the amount of time required to develop and market new drugs. As part of our global strategy, we have started clinical trials in the United States of anti-cancer drugs delivered by polymer micelle drug delivery system (DDS). By conducting development simultaneously in the United States, where the number of cases is large and the speed of clinical trials is greater, as well as in Japan, we expect to be able to deliver anti-cancer drugs to the world more quickly and efficiently.

Business Objectives and Strategies

We are focusing on developing new drugs through a fusion of technologies, and on improving customer satisfaction of both patients and medical institutions.

Nippon Kayaku is working to improve its position as a specialty firm dealing in pharmaceuticals for the treatment of cancer, and also to expand our business into cancer-related medical materials and medical devices. As part of that, sales are climbing of GELPART, an advanced medical material we introduced from Astellas Pharma Inc. GELPART is composed of porous gelatin particles 1 mm or 2 mm in diameter, and is used for the treatment of hepatocellular carcinoma. GELPART is used in a treatment known as “embolization,” in which it is injected into the blood vessels that supply nutrients to hepatocellular carcinoma, blocking them and in effect “starving” the cancer cells.

We are also reinforcing our programs aimed at developing

new drugs through a fusion of technologies. As a chemical company, Nippon Kayaku is distinguished by the fact that we possess technologies in both the low-molecular and macromolecular fields. By creating a fusion of the low-molecular technologies of the Pharmaceuticals Group with the macromolecular technologies of the Functional Chemicals Group and other sources, we have created a polymer micelle anti-cancer drug centered on a new drug delivery system presently undergoing clinical trials. Because this DDS is able to deliver the anti-cancer drug directly to cancer cells, it is expected to reduce side effects and deliver better results.

The ability to apply this type of nanotechnology to anti-cancer drugs is one of our company’s unique strengths, and we will continue to work actively to create fusions of technologies in the future.

We will work to add value to our primary products by such means as adding prescriptive indications and introducing new drug forms based on market needs, by constructing a base of practical clinical data, and by carrying out lifecycle management in order that our pharmaceuticals are always needed in the health care field. For this purpose, communication with health care professionals and responding to the demands of our customers are essential.

We are working to achieve our corporate philosophy of “good products, uninterrupted progress, and conscientious cooperation,” obtain the trust of the customers, and improve customer satisfaction. We expect that these efforts will all further improve our business performance.

Akira Mandai

Member of the Board
Managing Director
Director of
Pharmaceuticals
Group



Topics

Licensing agreement signed for prostate cancer treatment drug

In August, Nippon Kayaku entered into a licensing agreement for exclusive rights in Japan to develop and sell the prostate cancer treatment drug "OZARELIX," developed by the Canadian company Aeterna Zentaris Inc., and expected to become a core product in the future. Approximately 37,000 adult males develop prostate cancer in Japan every year, a number that is expected to near 67,000 by the year 2015 with the aging of society. OZARELIX is a unique hormone therapy drug that counters symptoms by suppressing hormonal production, and is expected to be effective against prostate cancer and other hormone-dependent malignant tumors.

Nippon Kayaku, Aeterna Zentaris, and Spectrum (U.S.), a company that has been granted exclusive licenses in North America, Mexico, and India, are cooperating as partners in the pursuit of early sales of OZARELIX.



early application for national health care approval was confirmed. Subsequently, we applied for supplemental approval in June 2006 in order to meet the growing needs of patients and medical personnel.

Application for drug indication in Europe in the treatment of "Wegener's granulomatosis"

In Europe we have applied for sales approval of the immunosuppressant "SPANIDIN" (injectable) as an indication in the treatment of "Wegener's granulomatosis," an incurable autoimmune disease that causes inflammation of the lungs, liver, and blood vessels. In March 2001 we received orphan drug designation for SPANIDIN for use with the disease, and have proceeded with clinical development. With our application in December of last year, we expect to commence sales in Europe in 2008. More sufferers of the disease occur in Europe and the United States than in Asia, with approximately 1,200 patients in Japan, 20,000 in Europe, and 10,000 in the U.S.

Drug approval obtained for treatment of "malignant pleural mesothelioma" from asbestos particles

We obtained approval for the supplemental indication of the cancer drug "RANDA" (an injectable under the generic name "CISPLATIN," which is presently used to treat diseases such as cancer of the stomach) for the treatment of malignant pleural mesothelioma. This lung disease is thought to be caused by the inhalation of air-borne asbestos particles. In Japan the number of related deaths has been rising, reaching 833 in 2004, and previously no potent or effective drug has been developed to treat the disease. At the "First Discussion Conference for Problems in the Use of Unapproved Drugs" held in January 2005, a combined treatment of CISPLATIN and PEMETREXED was discussed, and the necessity of its

Supplemental indication requested of cancer drug "HYCAMTIN" for ovarian cancer



We applied for supplemental indication for the treatment of ovarian cancer "HYCAMTIN" introduced by the British company GlaxoSmithKline. HYCAMTIN, a drug typically that is effective in treating lung cancer, is a semi-synthetic derivative of camptothecin, which is extracted from a plant (*Camptotheca acuminata*) native to China. This drug has been

shown to suppress cancer cell proliferation by bonding strongly with enzymes involved in DNA synthesis in cells, hindering their actions. The number of ovarian cancer patients has been increasing in Japan, and is expected to reach 12,000 by 2015, a 20 percent increase over the current level. Ovarian cancer can often reoccur in a patient after the first round of treatment, so treatment outcomes can by no means be considered satisfactory. HYCAMTIN has already been approved as an ovarian cancer drug in approximately 80 countries, and is expected to receive approval in Japan as well in 2008.

Safety Systems Business

We will continue to provide appealing products to the rapidly growing global automotive safety products market, and work to increase our global market share.



Business Overview

We utilize a global tripartite system for the production and sales of automotive safety products.

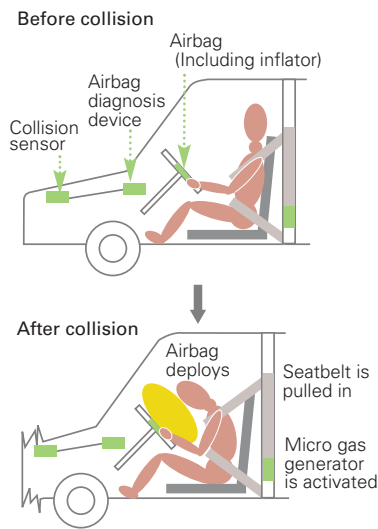
Nippon Kayaku utilizes a global tripartite system based in Japan (Himeji Plant), the United States (Lifesparc Inc., California), and the Czech Republic (Indet Safety Systems a.s., Vsetin) in order to produce and sell automotive safety products. The production of detonators at our Himeji Plant and explosives at our Asa Plant have given our company a long history and extensive range of technologies relating to igniters, detonators, and explosive combustion. We have adapted and applied these technologies to develop our own inflators (gas generators for inflating airbags), micro gas generators (used in the devices that automatically tighten seatbelts in the event of a collision), and the squibs (igniters) used in these products. Currently our inflators are produced in Japan, and our squibs and micro gas generators are produced in Japan, the U.S., and the Czech Republic, with these products destined for markets worldwide.

Market Trends and Overview of Operations for the Fiscal Year Ended May 31, 2007

Large growth in sales for Japan, the United States, and Europe

In Japan, there was a large increase in inflator sales, and income from sales of micro gas generators was also somewhat higher.

Mechanisms of Airbag and Seatbelt Pretensioner Operation



Airbag Inflator Mechanism

A airbag inflator is a device, incorporated in safety airbags, that generates gas to instantly inflate the bag when a vehicle collision occurs.

[Operating mechanism]

- (1) A sensor detects the collision, and an electrical signal is sent to the inflator.
- (2) The squib inside the inflator operates, igniting a gas-generating agent. The generated gas enters the airbag, instantly inflating it.



Micro Gas Generator Mechanism

The micro gas generator generates gas for the seatbelt pretensioner device, which winds up the seatbelt and instantly restrains the occupant's body when a vehicle collision occurs.

[Operating mechanism]

- (1) A sensor detects the collision, and an electrical signal is sent to the micro gas generator.
- (2) The squib inside the micro gas generator ignites the gas-generating agent. The generated gas pressure becomes the dynamic force that winds up the seatbelt.



Sales grew in the United States, however personnel costs, transport costs, and other expenses were higher, substantially reducing profits. We are now taking a variety of steps aimed at reducing production costs.

In Europe, profits increased as a result of higher sales.

Business Objectives and Strategies

We are focusing on improving service to Japanese automobile manufacturers engaged in global operations, and on developing new products that meet the needs of the changing times.

The automobile market is expected to continue growing rapidly worldwide, with market growth anticipated during the coming five years in China, Eastern Europe, and North America, followed by India, Russia, and Brazil. In addition, much attention has been focused on Japanese automotive parts manufacturers for their efforts to enter and expand in local markets as Japanese automobile manufacturers expand in markets worldwide.

Nippon Kayaku will focus on Japanese automobile and parts manufacturers, and at the same time also expand markets by providing service to automobile and parts manufacturers in Europe and America. Working to increase our share in the North American market and enhance our production capability and profits, our new plant in Mexico will begin operating in autumn of 2008. In Europe, we have purchased a business that produces micro gas generators with lead wires and have expanded our micro gas generator production system, in order to meet the needs of European automobile manufacturers, as these manufacturers utilize different designs than those of Japanese vehicles. To prepare for local production in China, where Japanese companies are making significant inroads, we established Kayaku Safety Systems (Huzhou) Co., Ltd. and are working towards a start of

inflator and micro gas generator production in mid 2008.

In order to deliver appealing new products to the market, we are also focusing on creating lead-free products and making other environmental improvements, and on developing semi-conductor bridge squibs, which are next-generation squibs that ignite using a smaller electrical current.

In the future, we will continue to establish an optimal globally oriented production and supply system, and develop new products through a distinctive fusion of Nippon Kayaku technologies, in order to expand our market share and increase our profit-earning capacity.

Topics

Purchase of lead wire-type MGG business, with aim of 50% global market share

Aiming to expand our micro gas generator (MGG) business, on December 1 we purchased the assets (production facilities, goodwill, etc.) of Austria's Hirschmann Automotive GmbH. The purchase was made through Indet Safety Systems a.s. (Czech Republic), a wholly owned subsidiary of Nippon Kayaku. The Nippon Kayaku Group produces pin-type micro gas generators in Japan, the Czech Republic, and the United States, and holds a near 30 percent of the global market share. This new purchase now makes it possible to produce lead wire-type micro gas generators as well, so the Group hopes to quickly achieve a 50 percent share of the global market in the overall seatbelt system business.

Construction of new plant in Mexico

In order to expand its automotive safety parts production base and boost cost competitiveness, Nippon Kayaku plans to start up a new plant in Mexico within the year, in addition to the plant in the United States. LifeSparc Inc., our California subsidiary that produces and sells squibs and micro gas generators, continues to operate at full capacity, so we enhanced facilities there at the start of 2007. However due to limits there for future expansion of production and improvement in cost competitiveness, we decided to establish a new production base in Mexico, a country that is part of the North American Free Trade Agreement (NAFTA) with expanding automobile production capability and competitive cost advantages. We plan to transfer the production of micro gas generators to the Mexico plant, as well as optimize our business structure in North America.

Notice of Organizational Change

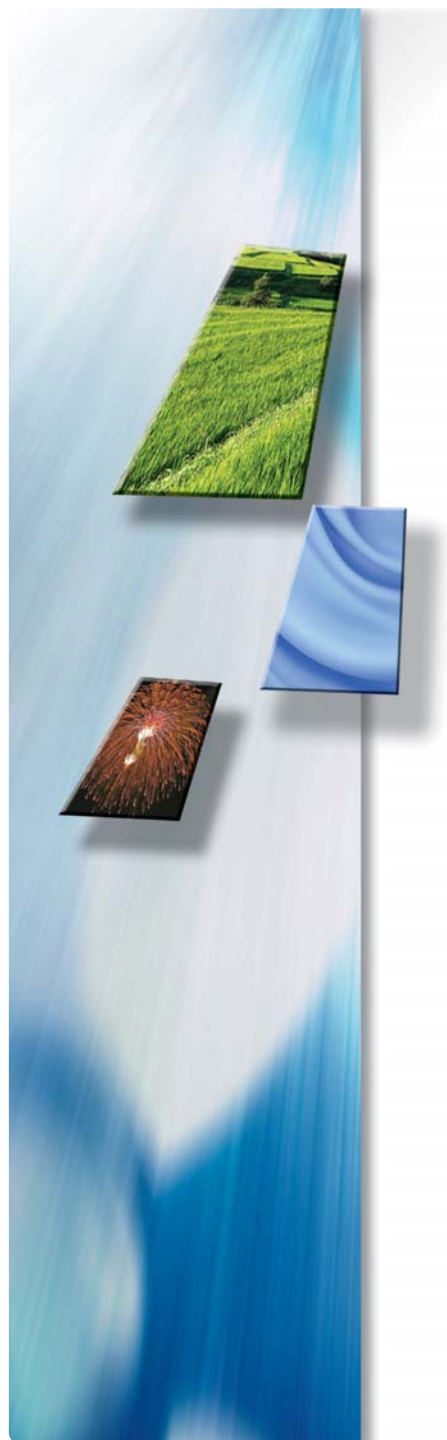
On Aug. 30, 2007, Nippon Kayaku established the Safety Systems Group. Previously this business was part of the Functional Chemicals Group, however with the expanding global market for automotive safety systems, we have established a new business group and are expanding our operations in this important area. Financial information for this group will be reported beginning from the year ending May 2008.



Yoshiyuki Ikeda
Member of the Board
Managing Director
Director of Safety Systems
Group

Fine Chemicals Business

Three years into our reforms, we have established our profit base and will dedicate ourselves to increasing sales and profits.



Agrochemicals Business

Both sales and profits for insecticides, fungicides, and other elements of our agrochemicals business increased during the year ended May 31, 2007, and we will continue to carry out further structural reforms.

Nippon Kayaku manufactures and sells agricultural insecticides, fungicides, herbicides, soil fumigants, and insecticides for such common pests as mosquitoes, flies, and cockroaches. Agricultural insecticides and soil fumigants occupy a large percentage of our sales. This business area produced both higher sales and profits for the year ended May 31, 2007, however our structural reforms are not yet complete, and we intend to further streamline our operations during the next three years, and take other steps such as purchasing newly developed chemicals when the opportunities arise.

During the year ended May 31, 2007, we released a new product, Safrotin® MC, which is an effective commercial insecticide for cockroaches. This chemical has been approved for use not only in Japan, but in more than 20 countries worldwide, and growth in overseas sales is expected as well. We have also succeeded in developing an original microbial pesticide, a product that is especially important now because it matches recent trends toward reducing or eliminating the use of agrochemicals.

Major Products

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

Color Chemicals Business

We are relocating our production and sales base for dyes for clothing and paper pulp to China, the largest market in the world.

In addition to the manufacture and sales of textile dyes and dyes for paper pulp, our color chemicals business has become involved in the new field of car seat dyes. Nippon Kayaku dyes are characterized by their high quality, including high fastness, bright colors, and few dyeing failures. For both textile dyes and dyes for paper pulp, we control the largest market share of any Japanese manufacturer.

However in recent years as production of clothing in particular has shifted to China, our share of the Japanese market has been declining by 3 – 4% each year. On the other hand, we are experiencing annual growth of 40 – 50% in the China market, and so our overall sales have been increasing.

Under these changing market conditions, our China production and sales companies Wuxi Advanced Kayaku Chemical Co., Ltd. and Zhao Yuan Advanced Kayaku Chemical Co., Ltd. are continuing to boost production and increase sales year after year. In the year ended May 31, 2007, we continued to expand our sales and technical service centers, and in June 2007 we completed construction of a new plant at Wuxi Advanced Kayaku Chemical Co., Ltd. With an eye toward selling made-in-China products in both the Chinese and global markets, we are planning to construct a dye business center in Shanghai during the fiscal year ending May 31, 2008.

■ Major Products

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

Explosives Business

We are integrating our industrial explosives business in order to streamline it, and are working for active expansion in the promising new business area of industrial nano-size diamonds.

The Nippon Kayaku explosives business is involved with the industrial explosives and detonators that are used in tunnel and dam construction, as well as the black powder and fuses used in fireworks and other products. Our industrial explosives business has been affected by a reduction in public works projects, and while sales have been declining by 6% annually, we have nonetheless succeeded in securing profits through cost reductions.

In order to streamline our industrial explosives business, during the year ended May 31, 2007 we began laying the groundwork for the integration of our explosives business with that of Asahi Kasei Chemicals Corporation, and we are planning to establish a new company in January 2008. This integration of our businesses will improve the efficiency of production, sales, and distribution, making it possible to increase profits.

Based on our explosives business technologies, we have

also succeeded in developing technology for the production of industrial nano-size diamonds, an emerging business field. We are actively working to commercialize this technology as a promising new Nippon Kayaku business.

■ Major Products

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

Topics

Sale of effective cockroach insecticide



Government approval for the commercial cockroach control insecticide "Safrotin® MC" was acquired in April 2007, and sales began in June. A feature of the insecticide is that it is effective against cockroaches that are

resistant to conventional agents, while being safe for humans. In addition to Japan, sales will extend to Southeast Asia, the Middle and Near East, and other overseas destinations, with the aim of reaching annual sales of 300 million yen within three years.

In-house development of environmentally friendly microbial pesticide



In March 2007, pesticide registration was acquired for "Hasumon Tenkei," an insecticide that kills *Spodoptera litura* (common cutworm), an insect that is harmful to such leafy plants as strawberries, soybean, and lettuce. In contrast to conventional chemosynthetic pesticides, this microbial pesticide controls the larvae of common cutworms through lethal infection. Since it has no harmful effect on plants, beneficial organisms in the soil, or insects that are the natural enemies of cutworms, it is also useful in the production of specially cultivated agricultural products. Test marketing centered on strawberry and soybean cultivation will be conducted this year, with sales expected to be expanded to such crops as early-summer lettuce starting next year.

WAC acquires ISO9001 certification

Wuxi Advanced Kayaku Chemical Co., Ltd. (China), a subsidiary of Nippon Kayaku that manufactures and sells dyes, acquired ISO9001 certification in April 2007 and has since commenced activities aimed at acquiring ISO14001 certification as well. The company is striving to deliver products that will provide an even higher degree of customer satisfaction in the expanding Chinese market, while becoming a business that is respected and appreciated by the community at large.

Yoshiaki Fukushima

Member of the Board
Managing Director
Director of Fine Chemicals
Group



1. Basic Concept of Corporate Governance

Nippon Kayaku understands that strengthening check functions in order to ensure management transparency and disclosing information to our shareholders and investors in a timely and fair manner are important issues for the purpose of ensuring sustainable business operations. Based on this understanding, we have selected a corporate governance system that is based on decision-making by the board of directors and on an auditor system as the most effective system in terms of exercising management functions.

2. Status of Programs Related to Corporate Governance

Nippon Kayaku has introduced an executive director system to ensure our ability to react quickly to changes in the business environment and carry out flexible operations. We have also clearly separated our management decision-making and supervision functions from our operational functions, strengthening each of them to ensure correct decision-making and rapid operations.

Board of directors (convenes monthly)

In order to rapidly carry out management decision-making, we reduced the number of directors to no more than 10, and are working to further strengthen our supervision functions so that all decisions regarding important issues in our operations are made based on the rules and policies of the board of directors, in accordance with laws and the articles of incorporation.

Management conference (convenes weekly)

This conference discusses and receives reports concerning important items related to management and operations. After full discussion by the management conference members, these items are decided by the company president, who is the conference chairman.

Executive directors committee (convenes quarterly)

This committee is chaired by the company president, and is composed of the executive directors (up to 25) who are in charge of company operations, and who are appointed by the board of directors. It reports on the status of operations that are entrusted to it by the board of directors and president, as well as on other necessary items.

Management strategy conference (convenes biannually)

This conference communicates the Nippon Kayaku Group business policies and business strategies decided by the board of directors, as well as other important items related to general management, to management personnel, and ensures that this information is known throughout the company.

Board of auditors (convenes monthly)

This board is composed of five auditors, three of whom are from outside the company. Based on the rules and policies of the board of auditors, it monitors and supervises the duties of the directors from an independent perspective.

In addition, we have established rules and policies for managerial authority, and have clarified the company business organization, business duties, and the authority and responsibilities of management and supervisory positions. We have constructed a system of responsibility, and are working to carry out systematic and efficient business operations.

3. Status of the Internal Administration System and Risk Management System

Based on the understanding that construction of a system to ensure fair and appropriate operations is an important matter, a basic policy concerning the construction of the system described below was decided at the board of directors meeting which was convened on May 30, 2006.

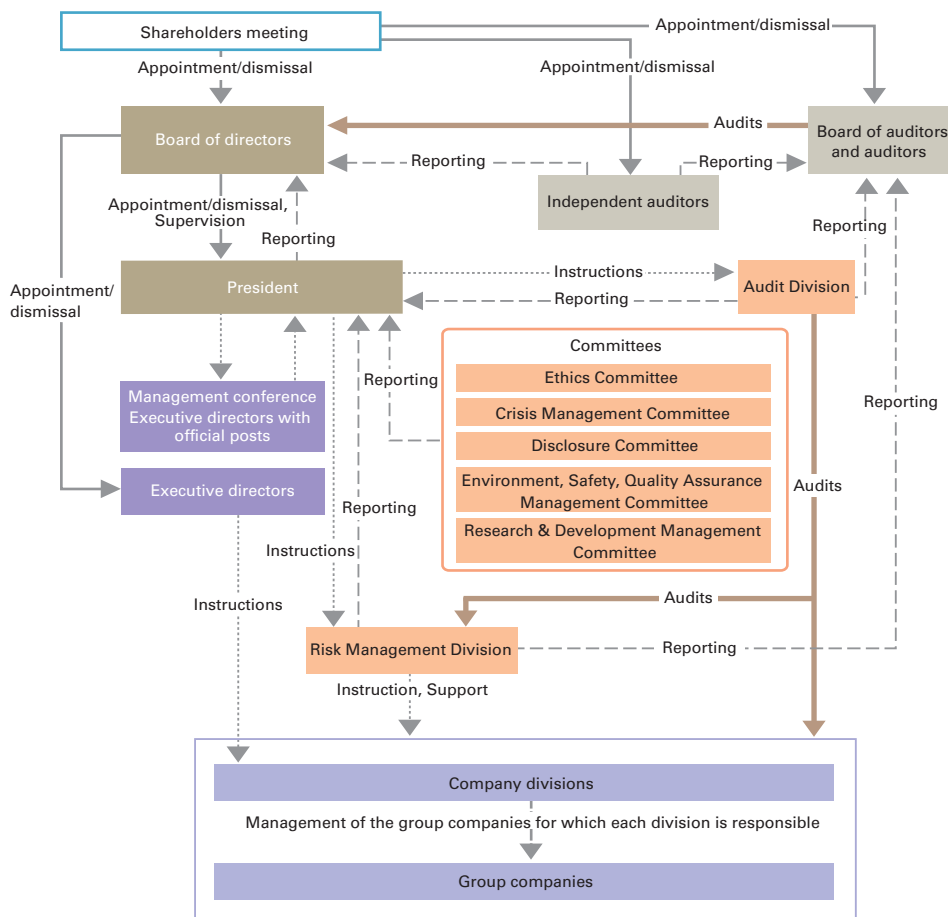
As a result of this decision, Nippon Kayaku is constructing the actual system, through steps which include establishing Action Charter and Action Standards, establishing a division in charge of compliance, establishing the Crisis Management Committee, formulating operating rules and policies for the Nippon Kayaku Group, and establishing a division for managing subsidiary companies in each group business segment.

- (1) A system for ensuring that the official duties of directors and employees are carried out in conformance with laws and the articles of incorporation
- (2) A system concerning the storage and management of information related to the directors' conduct of official duties
- (3) Rules and a system related to managing the risk of loss
- (4) A system for ensuring that the official duties of directors are carried out efficiently

- (5) A system for ensuring fair and appropriate operations within the Nippon Kayaku Group
- (6) Items concerning the employees in cases when an auditor requests the placement of employees to assist the auditor in his/her official duties, and items related to the independence of these employees from the directors

- (7) A system by which directors and employees report to auditors, and a system concerning other reports made to auditors
- (8) Other systems for ensuring that audits conducted by auditors are carried out effectively

[Schematic of the Internal Administration System]



Programs for Society, the Environment, and Safety

* The programs below were conducted during the fiscal year ended May 2006 (June 2005 – May 2006). For programs in the fiscal year ended May 2007, please refer to the Environmental & Safety / Sustainability Report 2007, which we expect to issue in December 2007.

Basic Approach to Sustainability

The Nippon Kayaku Group aims to fulfill its corporate social responsibilities and contribute to the creation of a sustainable society by becoming a corporate group that continually contributes to humanity through products and technologies that protect life and health and support a rich cultural lifestyle. Based on the concept of Responsible Care,* we are actively promoting business operations that are friendly to the environment, safety, and health, while engaging in social activities that make the best use of our business strengths.

* Responsible Care is the commitment by companies that manufacture or handle chemical substances to improving environmental, health, and safety measures in all processes involving chemical substances, from development, production, sales, and consumption to final waste disposal. Since its inception in Canada in 1985, Responsible Care has spread throughout the world and is currently practiced in 40 countries.

Social Activities

Asunaro House for Caregivers

Ten years ago, as a part of programs that commemorated Nippon Kayaku's 80th Anniversary, we envisioned a special lodging facility for caregivers accompanying children being treated for intractable diseases such as cancer, or who were to undergo bone marrow transplants at a local medical center. This facility, called the "Asunaro House," opened in Saitama City in Saitama Prefecture in 1998, and has now been operating for nine years. In addition to its 10 private accommodations, there are also a shared kitchen, cafeteria, discussion corner, and children's playroom to facilitate communication and mutual support among the caregivers. The number of families using this facility has continued to grow since it opened, and the facility was used 264 times during 2006.



Early Detection of Breast Cancer

While Nippon Kayaku already provides effective anti-cancer drugs and holds specialized study meetings for medical staff, we are also putting our efforts into awareness activities for citizens in general. In addition to actively participating in the Pink Ribbon campaign for breast cancer awareness in 2006 we also became a sponsor of the "Breast Cancer Info Navi" website, which promotes to a wide audience the importance of the early detection, early diagnosis, and early treatment of breast cancer.



Breast Cancer Info Navi:
http://www.nyugan-infonavi.jp/n_navi/

Environmental Activities

Environmental Management System

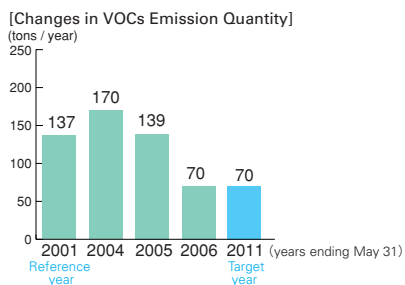
The Nippon Kayaku Group is working to carry out Responsible Care activities more efficiently, and also to continually raise the level of its environmental activities. For these purposes, we have acquired ISO14001 certification, the global standard for environmental management systems. All six Nippon Kayaku plants acquired this important certification by 2001. In addition, ISO14001 has also been obtained by the group companies Polatechno Co., Ltd., Indet Safety Systems a.s., Kayaku Chemical (Wuxi) Co., Ltd., and Wuxi Polatechno Optics Co., Ltd. (WPLC).

Environmental Master Plan Objectives and Progress

In the Environmental Master Plan, Nippon Kayaku has set three special mid-term objective items for the fiscal year ending May 2011, namely chemical substances, waste products, and prevention of global warming, and we are carrying out programs aimed at achieving them. We already achieved these objectives in the annual plan for the fiscal year ended May 2006, however this was due in part to the decrease in production activities caused by sluggish product demand in and after the fiscal year ended May 2001. Therefore we are working to carry out continued improvements.

• Reduction of Chemical Emissions

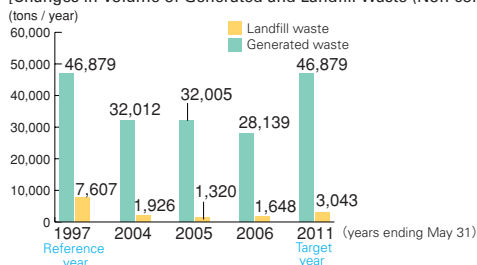
In the fiscal year ended May 2006, we successfully achieved the objective for the fiscal year ending May 2011 of "reducing the amount of VOC (volatile organic carbon) emissions to the atmosphere by 50% from the level of the fiscal year ended May 2001, to 70 tons or less." For the fiscal year ending May 2007, we have set VOC reduction objectives for each plant, and are making emission reduction plans.



• **Reduction of Waste Products**

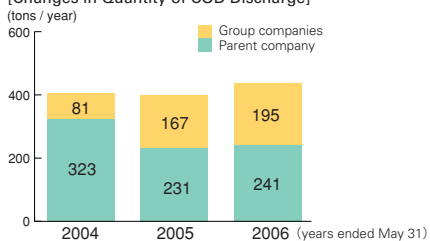
In the fiscal year ended May 2006, we successfully achieved the objective for the fiscal year ending May 2011 of “holding the amount of waste products generated to the same level as the fiscal year ended May 1997.” In the fiscal year ending May 2007, we are promoting recycling of waste materials and taking other steps to reduce waste.

[Changes in Volume of Generated and Landfill Waste (Non-consolidated)]



At the Tokyo Plant and Fukuyama Plant, which together manufacture color chemicals, the manufacturing process produces wastewater with a potentially high environmental impact (expressed as COD, or chemical oxygen demand). In order to reduce the damaging effects of this wastewater, it is treated by an active sludge treatment system and a decolorizing system that utilizes activated carbon and microorganisms to break down waste. Meanwhile, we are also researching more effective decolorization approaches.

[Changes in Quantity of COD Discharge]



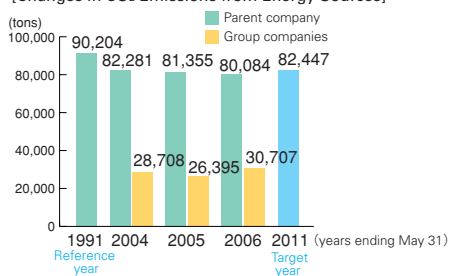
In June 2006, Nippon Kayaku became the first company in the Japan dye industry to begin offering a service for the collection and reuse of small-volume liquid dye containers (20 kg). This has helped to reduce the container disposal costs of our customers and also promotes the effective utilization of resources.

• **Prevention of Global Warming**

In the fiscal year ended May 2006, we have effectively achieved the objective for the fiscal year ending May 2011 of “reducing CO₂ emissions resulting from energy use by 8.6% from the level of May 1991.” However, with the recovery of product demand and the growing size of our business, an increase in CO₂ emissions is expected in the future. As a result, we are seeking to put in place further measures to save energy. During the fiscal

year ending May 2007, among other activities, we are changing the boiler fuel at the Fukuyama Plant to city-supplied gas.

[Changes in CO₂ Emissions from Energy Sources]

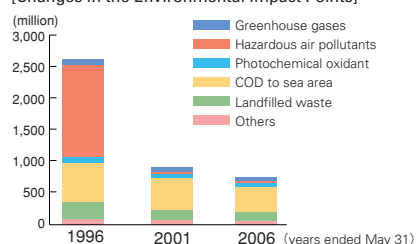


Changes in Environmental Impact Points

As an index to comprehensively assess the results of Nippon Kayaku environmental activities, we have calculated our environmental impact points using JEPIX.* Using this, when a comparison is made between the fiscal year ended May 1996 (when our Responsible Care activities first began), and the fiscal years ended May 2001 and May 2006, we see that the reduction of hazardous air pollutants – a top priority of our Responsible Care activities – contributed the greatest part to reducing the environmental impact of our business activities as a whole. We can also see that the second greatest contribution was a reduction in waste materials, for which we are carrying out activities under the Environmental Master Plan. By linking this sort of self evaluation to our future activities, we expect to further improve the effectiveness of our environmental programs.

*Japan Environmental Policy Index, which is a method for determining a manufacturer’s total burden on the environment. This method enables the environmental impact of business activities to be represented as a total by multiplying the eco-factor (environmental impact factor) for each substance by the amount of emissions of that substance, and totaling the results.

[Changes in the Environmental Impact Points]

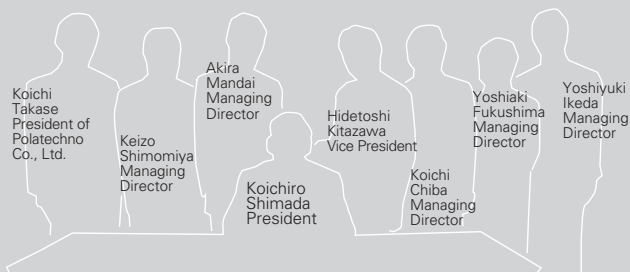


Environmental Accounting

In the fiscal year ended May 2006, Nippon Kayaku installed exhaust gas treatment systems, wastewater treatment systems, energy-saving boilers, and a container recycling system. The total environmental protection cost for these efforts was 2.2136 billion yen, and the environmental protection effects were 81.61 million yen.

Board of Directors/Auditors

As of October 1, 2007



Board of Directors

Koichiro Shimada
Member of the Board
President
Representative Director

Hidetoshi Kitazawa
Member of the Board
Vice President
Representative Director
Director of Strategic Corporate Planning Group
Director of Research & Development Group

Koichi Chiba
Member of the Board
Managing Director
Director of Administration Group

Yoshiaki Fukushima
Member of the Board
Managing Director
Director of Fine Chemicals Group

Akira Mandai
Member of the Board
Managing Director
Director of Pharmaceuticals Group

Yoshiyuki Ikeda
Member of the Board
Managing Director,
Director of Safety Systems Group

Keizo Shimomiya
Member of the Board
Managing Director
Director of Functional Chemicals Group

Koichi Takase
Member of the Board
President, Representative Director
of Polatechno Co., Ltd.

Auditors

Yukihisa Asakawa
Standing Auditor

Tadashi Fujii
Standing Auditor

Shoichi Saito
Auditor

Yo Ota
Auditor

Yasuharu Takamatsu
Auditor

Consolidated Five-Year Summary

Nippon Kayaku Co., Ltd. and Consolidated Subsidiaries
Years Ended May 31

	2007	2006	2005	2004	2003
Results for the year (millions of yen)					
Net sales	¥148,124	¥140,026	¥134,205	¥128,016	¥123,431
Cost of sales	93,537	87,074	86,062	81,621	79,002
Selling, general and administrative expenses	41,050	39,731	37,976	36,297	34,730
Operating income	13,536	13,219	10,166	10,097	9,697
Income before income taxes and minority interests	13,608	18,629	10,404	8,941	7,643
Net income	6,610	9,641	5,315	3,926	2,780
Amounts per share (yen)					
Net income	¥ 36.37	¥ 52.92	¥ 28.87	¥ 21.22	¥ 14.92
Cash dividend applicable to the year	20.00	20.00	11.70	11.00	11.00
Shareholders' equity	646.78	634.51	570.31	550.12	527.93
Year-end financial position (millions of yen)					
Current assets	¥102,661	¥108,644	¥ 92,716	¥ 93,651	¥ 99,223
Current liabilities	40,316	41,619	35,509	39,389	42,065
Working capital	62,345	67,025	57,207	54,262	57,158
Property, plant and equipment	69,783	62,754	57,533	57,069	58,009
Total assets	207,081	205,308	181,364	179,823	179,117
Total shareholders' equity *1	130,233	127,030	103,810	100,207	96,204
Year-end statistics					
Number of shares outstanding (thousands)	182,503	182,503	182,503	182,503	182,503
Number of round-lot shareholders	17,378	18,268	18,770	19,756	20,367
Number of employees	4,423	4,300	4,049	3,934	3,679
Financial ratios					
Current ratio (times)	2.5	2.6	2.6	2.4	2.4
Equity ratio (%)	56.7	56.2	57.2	55.7	53.7
ROE (%)	5.7	8.8	5.2	4.0	2.9
ROA (%)	3.2	5.0	2.9	2.2	1.6
Sales by business segment *2 (millions of yen)					
Functional chemicals business	¥ 78,925	¥ 73,133	¥ 64,574	¥ 56,405	
Functional materials	14,713	16,407	15,448	15,942	
Electronic materials	42,220	40,476	36,181	30,410	
Catalysts	5,008	2,661	2,574	2,096	
Safety systems	16,982	13,587	10,370	7,955	
Pharmaceuticals business	41,700	39,774	39,660	41,122	
Fine chemicals business	24,538	24,028	26,843	27,053	
Agrochemicals	8,740	8,246	11,333	11,150	
Color chemicals	9,869	9,608	9,269	9,617	
Explosives	5,927	6,173	6,241	6,286	
Other businesses	2,960	3,089	3,126	3,434	

*1 Shareholders' equity for years ended May 31, 2003, 2004, and 2005 do not include minority interests.

*2 Business segments have changed from June 1, 2004. Sales by business segment for 2004 are reclassified to the current business segments.

Management's Discussion and Analysis of Results of Operations and Financial Condition

Results of Operations

Business Overview

Despite high raw material costs due to the soaring price of oil, Japan's economy during the fiscal year ended May 31, 2007 on the whole remained on a recovery course, as evidenced by an active increase in capital investment backed by strong corporate performance, and by improvements in the hiring and personal income environments.

The chemical products industry, centering on digital home electronics and other IT-related fields, was generally headed toward expansion. But conditions remained difficult due to the effects of rising raw material costs caused by continuing high oil prices, and also due to falling product prices and inventory adjustments.

In the pharmaceuticals industry, in addition to the lowering of drug prices in April of last year, trends toward increased use of generic drugs and other steps aimed at controlling the cost of medicines became even stronger. At the same time, global competition in the research, development, and sale of new drugs intensified as a fight for survival among companies unfolded.

In the midst of such conditions, the Nippon Kayaku Group is aiming to raise its corporate value and become a company capable of sustained growth. For this purpose, we have invested business resources in key fields, worked to strengthen overseas operations and cut costs, and taken steps to improve profits.

As a result, and due to growth in our functional chemicals business and pharmaceutical business, the fiscal year ended May 31, 2007 produced more revenue than the previous fiscal year. Also, the profit was bigger than the previous fiscal year thanks to factors such as increased sales in the pharmaceuticals business.

Net sales

In the fiscal year ended May 31, 2007, net sales reached 148.124 billion yen, an increase of 8.097 billion yen (5.8%) from the previous fiscal year. Net sales for the entire Group were 143% of the net sales for the parent company alone.

Cost of Sales; Selling, General and Administrative Expenses

In the fiscal year ended May 31, 2007, the cost of sales was 93.537 billion yen, an increase of 6.462 billion yen (7.4%) from the previous fiscal year. It was up 0.9 percentage points from the previous fiscal year to 63.1% as a percentage with respect to net sales. Selling, general and administrative expenses in the fiscal year ended May 31, 2007 were 41.05 billion yen, an increase of 1.319 billion yen (3.3%) from the previous fiscal year.

Operating Income

In the fiscal year ended May 31, 2007, operating income was 13.536 billion yen, an increase of 316 million yen from the previous fiscal year (2.4%). It was up 0.3 percentage points from the previous fiscal year to 9.1% as a percentage with respect to net sales.

Operating Performance by Business Segment

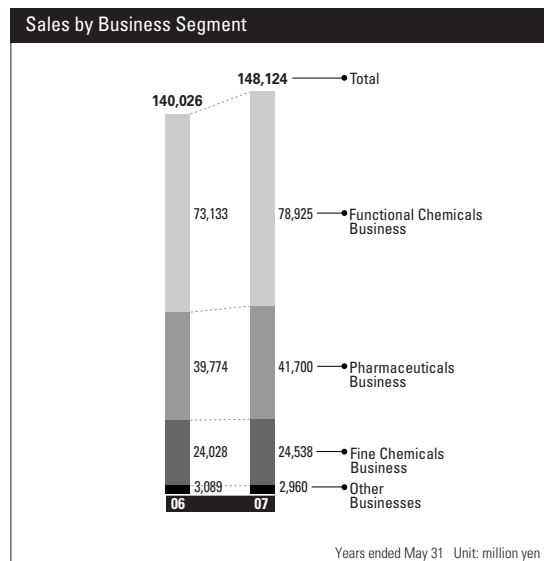
[Functional Chemicals Business]

In the fiscal year ended May 31, 2007, sales for the functional chemicals business reached 78.925 billion yen, an increase of 5.792 billion yen (7.9%) from the previous fiscal year.

In the functional materials business, sales of special epoxy resins for semiconductor encapsulation were higher than the previous fiscal year, however sales of UV-curing resins were lower. Due in part to the transfer of our polymer flocculent business, performance for the functional chemicals business as a whole was below the level of the previous fiscal year.

In the electronic materials business, sales of colors for inkjet printers were up from the previous fiscal year, while sales of resins for optical discs were down. In the area of optical films, sales of films for plasma displays were lower than the previous fiscal year, however Polatechno's polarizing film business was strong and exceeded the level of the previous fiscal year. Overall, sales in the electronic materials business were up from the previous fiscal year.

In the catalysts business, sales of catalysts for acrylic



acid and methacrylic acid manufacturing went smoothly, surpassing sales from the previous fiscal year.

In the safety systems business, sales of airbag inflators and micro gas generators for seatbelt pretensioners were both strong, and were up from the previous fiscal year.

Due to factors such as falling product prices and rising costs, overall operating income for the functional chemicals business was 8.307 billion yen, a decrease of 1.869 billion yen (18.4%) from the previous fiscal year.

[Pharmaceuticals Business]

In the fiscal year ended May 31, 2007, sales for the pharmaceuticals business amounted to 41.7 billion yen, an increase of 1.925 billion yen (4.8%) from the previous fiscal year.

Among pharmaceutical products for the Japanese domestic market, our new product "PACLITAXEL Inj. NK" (anti-cancer drug) made a large contribution to sales. In addition, sales of "EPIRUBICIN Inj. Merck" (anti-cancer drug), "CARBOMERCK" (anti-cancer drug), "IA-CALL" (arterial injection anti-cancer drug), "IMMUCYST" (anti-cancer drug), as well as introduced-product "CALSED" (anti-cancer drug) all were strong, and exceeded the levels of the previous fiscal year. On the other hand, due to the effects of competitor products and other issues, sales of "FARESTON Tab." (anti-cancer drug), "RANDA Inj." (anti-cancer drug) and "MILLISROL Inj." (vasodilator) were down from the previous fiscal year. Overall, sales of pharmaceuticals for the Japanese domestic market were

up from the previous fiscal year.

In the area of exports, sales of BLEO (anti-cancer drug) and ETOPOSIDE (anti-cancer drug) were higher than the previous fiscal year, while sales of active pharmaceutical ingredients were lower. Overall, exports were down from the previous fiscal year.

Sales of active pharmaceutical ingredients to the Japanese domestic market were higher than the previous fiscal year, thanks to strong sales of active pharmaceutical ingredients for generic pharmaceuticals.

In the area of diagnostic agents, sales of "LANAZYME ST-439 Plates" (breast cancer diagnostic agent) and "LANA 1,5AG" (diabetes diagnostic agent) were down from the previous fiscal year.

Overall operating income for the pharmaceuticals business was 7.475 billion yen, an increase of 1.975 billion yen (35.9%) from the previous fiscal year.

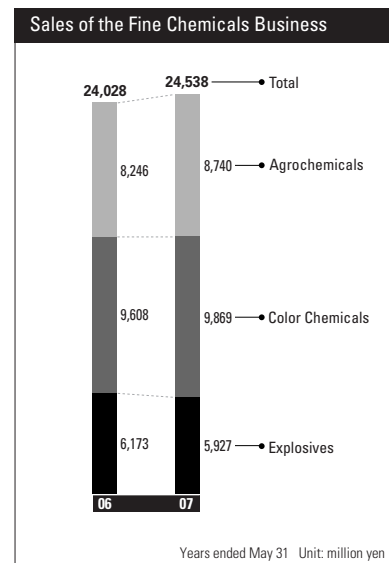
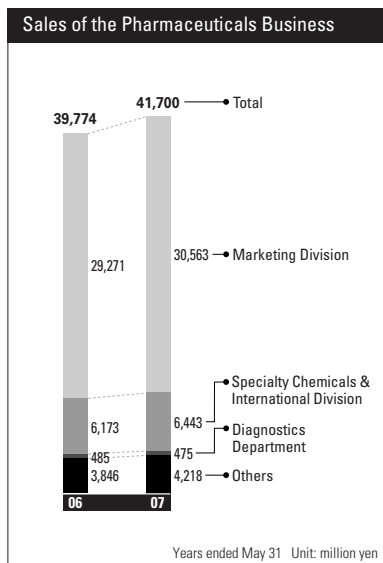
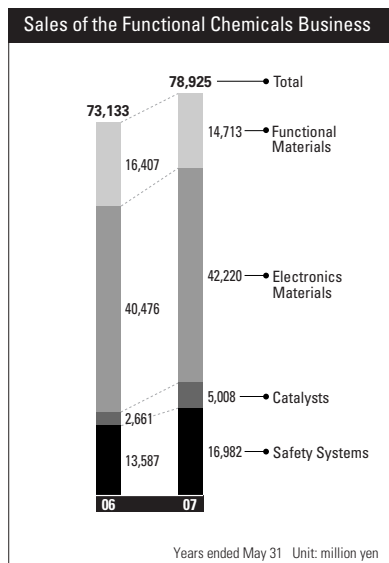
[Fine Chemicals Business]

In the fiscal year ended May 31, 2007, sales for the fine chemicals business amounted to 24.538 billion yen, an increase of 509 million yen (2.1%) from the previous fiscal year.

In the agrochemicals business, both domestic sales and exports were strong, and exceeded the levels of the previous fiscal year.

In the color chemicals business, sales from our overseas subsidiaries were strong, and were up from the previous fiscal year.

In the explosives business, sales were down from the



previous fiscal year, due to the effects of declining demand from civil engineering and stonecrushing applications.

Overall operating income for the fine chemicals business was 1.84 billion yen, a decrease of 44 million yen (2.3%) from the previous fiscal year.

[Other Businesses]

In the fiscal year ended May 31, 2007, sales from other businesses amounted to 2.96 billion yen, a decrease of 128 million yen (4.2%) from the previous fiscal year.

Operating income was 1.592 billion yen, an increase of 66 million yen (4.3%) from the previous fiscal year.

Other Income and Expenses

In the fiscal year ended May 31, 2007, interest and dividends received amounted to 361 million yen, while interest paid was 450 million yen. Other expenses (net) amounted to 161 million yen, an increase of 5.246 billion yen (97.0%) from the previous fiscal year.

Income before Income Taxes and Minority Interests

From the aforementioned results and due to absence of last year's profits from the sale of a former company housing site, income before income taxes and minority interests in the fiscal year ended May 31, 2007 was 13.608 billion yen, a decrease of 5.02 billion yen (26.9%) from the previous fiscal year.

Corporate Tax

In the fiscal year ended May 31, 2007, corporate tax was

5.503 billion yen, an increase of 1.866 billion yen (25.3%) from the previous fiscal year.

Minority Interests

In the fiscal year ended May 31, 2007, minority interests amounted to 1.494 billion yen, a decrease of 122 million yen (7.6%) from the previous fiscal year.

Net Income

In the fiscal year ended May 31, 2007, net income was 6.61 billion yen, a decrease of 3.03 billion yen (31.4%) from the previous fiscal year. It was down 2.4 percentage points from the previous fiscal year to 4.5% as a percentage with respect to sales. In the fiscal year ended May 31, 2007, net income for the entire Group was 152% of the net income for the parent company alone. Net income per share was 36.37 yen.

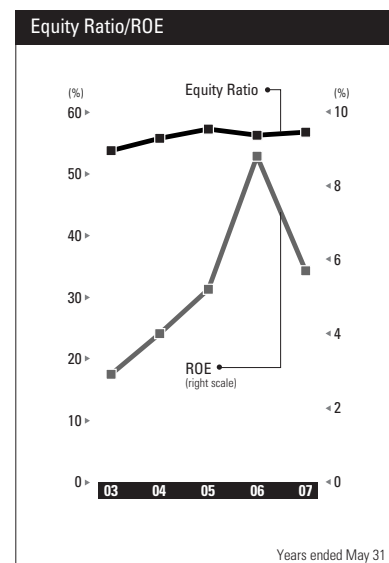
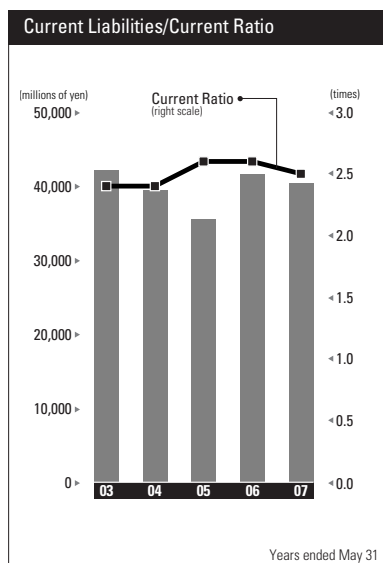
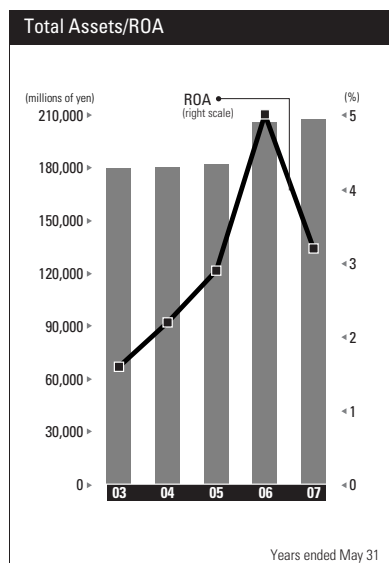
Financial Condition

Total Assets

As of the end of May 2007, total assets were 207.081 billion yen, an increase of 1.772 billion yen (0.9%) from the end of the previous fiscal year.

Current Assets

As of the end of May 2007, the balance of cash and cash equivalents was 25.589 billion yen, an increase of 4.164 billion yen (19.4%) from the end of the previous fiscal year.



Time deposits were 109 million yen, an increase of 67 million yen (159.5%) from the end of the previous fiscal year. Trade receivables were 46.213 billion yen, an increase of 585 million yen (1.3%) from the end of the previous fiscal year. Inventories were 26.18 billion yen, a decrease of 469 million yen (1.8%) from the end of the previous fiscal year; and deferred tax assets were 2.422 billion yen, an increase of 254 million yen (11.7%) from the end of the previous fiscal year. Other current assets were 2.216 billion yen, a decrease of 5.087 billion yen (69.6%) from the end of the previous fiscal year. As a result, total current assets were 102.661 billion yen, a decrease of 5.983 billion yen (5.5%) from the end of the previous fiscal year.

Property, Plant and Equipment; Investments and Other Assets

As of the end of May 2007, the value of property, plant, and equipment was 69.783 billion yen, an increase of 7.028 billion yen (11.2%) from the end of the previous fiscal year. Accumulated depreciation was 118.857 billion yen. The total value of investments and other assets was 34.636 billion yen, an increase of 727 million yen (2.1%) from the end of the previous fiscal year.

Liabilities

As of the end of May 2007, current liabilities were 40.316 billion yen, a decrease of 1.302 billion yen (3.1%) from the end of the previous fiscal year. Fixed liabilities were 36.531 billion yen, a decrease of 128 million yen (0.3%) from the previous fiscal year.

Net Assets

As of the end of May 2007, net assets were 130.233 billion yen, an increase of 3.203 billion yen (2.5%) from the previous fiscal year.

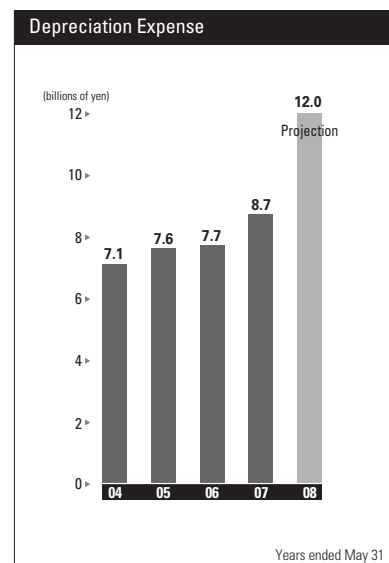
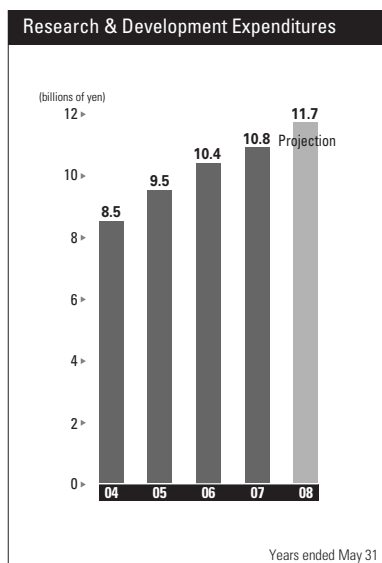
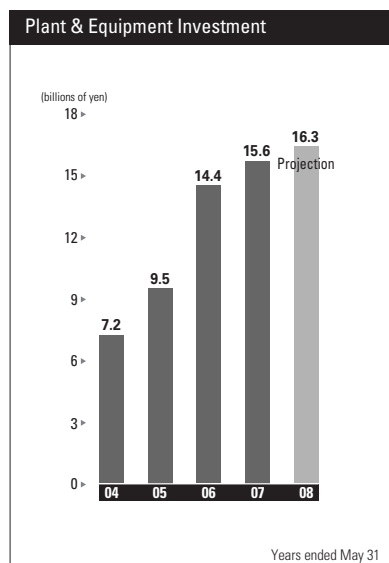
Cash Flow

Cash flow from operating activities increased by 8.409 billion yen from the previous fiscal year to 20.201 billion yen. This increase was primarily due to a reduction in inventory assets.

Cash flow from investing activities showed an expenditure of 17.882 billion yen, an increase in expenditures of 10.78 billion yen from the previous fiscal year. This decrease in cash flow was primarily due to a decrease in revenue from the sale of tangible fixed assets and to an increase in expenditures for the acquisition of tangible fixed assets.

Cash flow from financing activities increased by 2.742 billion yen over the previous year, to record an income of 1.559 billion yen. This increase was primarily due to an increase in income from long-term loans.

As a result, the balance of cash and cash equivalents at the end of the year increased by 4.164 billion yen from the previous fiscal year, reaching 25.589 billion yen.



Business Risk

In order to ensure sustainable business operations, the Nippon Kayaku Group analyzes a broad range of risks associated with our business, and works to prevent and disperse them. The following are possible risks which could have a major effect on our group's operating results, financial position, or image in society.

** The following have been identified as risks to the Nippon Kayaku Group at the end of this consolidated fiscal year. These do not cover events that go beyond our predictions, and are not a comprehensive list of all risks facing our group.*

1. Changes in the Business Environment

(1) Overall Business

The Nippon Kayaku Group is working to maximize its corporate value by creating a fusion of the technologies it possesses. For this purpose, we have established business strategies, development strategies, and other plans, and are managing our business in a way that is adapted to changes in the business environment. However while the functional chemicals business is a growth field that constitutes a large proportion of our sales and operating income, it is also a business that is susceptible to the effects of economic fluctuations. Domestic and international economic fluctuations, and changes in the business environment such as sluggish demand and intensifying competition, as well as the resulting changes to our business configuration, may have a major effect on the operating results and financial position of the Nippon Kayaku Group.

(2) Functional Chemicals Business

The functional chemicals business is focused on information and communications products, which have a short cycle of technological innovation. It is critical that development of new products and creation of the production system be carried out rapidly. An inability to provide new products that satisfy market needs in a timely manner, or lagging behind the radical technological innovations of other companies, represent large risks.

(3) Pharmaceuticals Business

Policies by the governments of Japan and other countries to reduce health care expenditures represent a risk to the pharmaceuticals business. In Japan, the health care insurance system has been overhauled, drug prices have been revised, and the use of generic drugs is being promoted. In Europe and America, there is downward pressure on prices under policies by vari-

ous national governments aimed at reducing pharmaceutical prices. In the active ingredients business, it is possible that business related to food products and food additives may be affected by recent problems involving the safety of food and other products.

(4) Fine Chemicals Business

In the fine chemicals business, the agrochemicals business is affected greatly by crop growing conditions, which are subject to climate changes and other phenomena, as well as by the occurrence of harmful insects. It is also affected by tightening governmental regulations related to food safety and environmental effects.

2. Rising Interest Rates

When determining the methods for procuring the funds necessary for operations, and the amounts required, the Nippon Kayaku Group considers its financial position as well as the monetary environment. Rising interest rates result in higher interest costs and may interfere with the procurement of funds.

3. Exchange Rate Changes

In order to minimize the risk to our overseas business and export-related transactions caused by sudden changes in the exchange rates, the Nippon Kayaku Group takes a number of steps, such as maintaining a balance of transactions denominated in foreign currencies. However it is still possible that there may be profits or losses on the foreign exchange.

Moreover, the operating results for overseas consolidated subsidiaries are converted to yen in order to create the consolidated financial statements, and are therefore affected by exchange rate changes.

4. Retirement Benefits

Based on mathematically calculated retirement benefit obligations and forecasts of pension plan assets, the Nippon Kayaku Group calculates its employee retirement benefit expenses and obligations. For this reason, the actual retirement benefits are affected by factors such as changes in the retirement bonus and pension system, changes to the discount rate used in the mathematical calculation, changes in the current value of the pension assets, and changes in the operating environment.

5. Valuation of Assets

Because the Nippon Kayaku Group owns securities and other items that have a current price, an event such as a large-scale drop in the stock market could result in loss for these financial instruments. In addition, fixed assets

may also be affected when the measured recoverable value ends up less than the book value, as that difference is recognized as a fixed asset loss.

6. Changes in Laws or Regulations

The business activities of the Nippon Kayaku Group are conducted in accordance with the laws and regulations of Japan and all overseas countries where we operate. Future changes in laws, regulations, or policies may restrict our business activities or increase costs.

7. Overseas Business

The Nippon Kayaku Group is working to expand its overseas business activities, however this business may be affected by changes to laws, regulations, or policies in overseas countries, or by events such as terrorism, wars, or other social disruptions.

8. Lawsuits

As the Nippon Kayaku Group conducts business in a wide variety of areas, there is the possibility that it could become the target of lawsuits, legal contests, or other legal actions.

9. Violation of Intellectual Property Rights

While the Nippon Kayaku Group carefully controls its patents and other intellectual property, it may not be possible to fully prevent violation by third parties. On the other hand, there is also the possibility that some of the Group's products or technologies may in the future be viewed as violating the intellectual property rights of another company.

10. Research and Development

The Nippon Kayaku Group considers research and development to be the engine that drives our business growth, and is actively engaged in R&D activities. In particular for pharmaceuticals, agrochemicals, and other products requiring R&D over extended periods of time, there may be cases of significant delays in product development, and also instances in which an R&D theme is abandoned without being commercialized. In addition, in the functional chemicals business, there is the possibility of a radical technological innovation by another company that will render us unable to develop and provide products that satisfy customer needs in a timely manner.

11. Procurement of Raw Materials

In order to obtain stable procurement of raw materials, the Nippon Kayaku Group disperses risk by securing multiple suppliers and other means. However events such as

sudden price changes or an interruption in supply of raw materials are possible.

12. Product Quality

The Nippon Kayaku Group has established control standards that are based on ISO9001 and other international standards, and manufactures products in accordance with them. Moreover, through measures such as the purchase of product liability insurance, we have created a risk prevention system for use in the unlikely event that a liability problem occurs. However, there is no guarantee that this system will be able to fully cover any settlement costs. In addition, there is the possibility for pharmaceuticals and agrochemicals that unpredictable side effects or other problems will be discovered after the product is marketed.

13. Accidents and Disasters

In order to prevent accidents involving manufacturing equipment, distribution, or other areas of our operations, and to prevent damage from natural disasters, the Nippon Kayaku Group has implemented safety measures that are in conformance with Group standards; however these cannot guarantee that accidents and natural disasters will not occur. There is the possibility of high expenditures and damage to the Group reputation in the event that an accident or other occurrence results in physical damage or injury at a plant or in the surrounding area, or in the event that our actions interfere with a customer's production and the customer demands compensation.

Consolidated Balance Sheets

Nippon Kayaku Co., Ltd. and Consolidated Subsidiaries
As of May 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2007	2006	2007
Assets			
Current assets:			
Cash and cash equivalents	¥ 25,589	¥ 21,424	\$ 210,280
Time deposits	109	42	895
Marketable securities (Note 5)	—	5,497	—
Trade receivables	46,213	45,627	379,760
Less allowance for doubtful receivables	(69)	(69)	(567)
Inventories (Note 4)	26,180	26,649	215,136
Deferred income taxes (Note 8)	2,422	2,167	19,903
Other current assets	2,216	7,304	18,210
Total current assets	102,661	108,644	843,627
Property, plant and equipment (Notes 3, 6 and 7):	188,640	177,224	1,550,168
Less accumulated depreciation	(118,857)	(114,470)	(976,719)
Property, plant and equipment, net	69,783	62,754	573,448
Investments and other assets:			
Investment securities (Notes 5 and 7)	24,375	22,017	200,304
Goodwill	2,042	2,867	16,780
Deferred income taxes (Note 8)	294	252	2,415
Other assets	7,924	8,771	65,116
Total investments and other assets	34,636	33,909	284,624
Total assets	¥207,081	¥205,308	\$1,701,709

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2007	2006	2007
Liabilities and shareholders' equity			
Current liabilities:			
Short-term bank loans (Note 7)	¥ 2,112	¥ 1,923	\$ 17,355
Current portion of long-term debt (Note 7)	4,987	2,944	40,981
Payables:			
Trade	15,671	16,580	128,778
Unconsolidated subsidiaries and affiliates	165	301	1,355
Construction	3,529	5,895	28,999
Other	3,362	6,622	27,627
Accrued expenses	5,129	4,948	42,148
Accrued income taxes (Note 8)	4,548	1,276	37,373
Other current liabilities	808	1,125	6,639
Total current liabilities	40,316	41,619	331,300
Non-current liabilities:			
Long-term debt, less current portion (Note 7)	12,033	7,175	98,882
Retirement benefits (Note 10)	3,980	8,086	32,706
Other non-current liabilities	15,101	15,345	124,094
Deferred income taxes (Note 8)	5,414	6,050	44,490
Total non-current liabilities	36,531	36,659	300,197
Total liabilities	76,847	78,278	631,498
Contingent liabilities (Note 12)			
Shareholders' equity (Notes 13 and 17):			
Common stock:			
Authorized – 700,000,000 shares			
Issued – 182,503,570 shares	14,932	14,932	122,705
Additional paid-in capital	17,269	17,264	141,909
Retained earnings	79,481	77,201	653,143
Less treasury stock, at cost	(514)	(398)	(4,223)
Total shareholders' equity	111,168	109,000	913,534
Valuation and translation adjustments:			
Unrealized holding gains on other securities	5,068	5,216	41,646
Translation adjustments	1,276	1,158	10,485
Total valuation and translation adjustments	6,345	6,375	52,140
Minority interests	12,719	11,653	104,519
Total net assets	130,233	127,030	1,070,202
Total liabilities and shareholders' equity	¥207,081	¥205,308	\$1,701,709

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

Nippon Kayaku Co., Ltd. and Consolidated Subsidiaries
Years Ended May 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2007	2006	2007
Net sales	¥148,124	¥140,026	\$1,217,224
Cost of sales	93,537	87,074	768,649
Gross profit	54,587	52,951	448,574
Selling, general and administrative expenses	41,050	39,731	337,332
Operating income	13,536	13,219	111,233
Other income (expenses):			
Interest and dividend income	361	430	2,966
Interest expense	(450)	(430)	(3,697)
Other, net	161	5,408	1,323
	72	5,409	591
Income before income taxes and minority interests	13,608	18,629	111,825
Income taxes (Note 8):			
Current	6,330	3,622	52,017
Deferred	(826)	3,748	(6,787)
Minority interests	1,494	1,616	12,277
Net income (Note 13)	¥ 6,610	¥ 9,641	\$ 54,318

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Net Assets

Nippon Kayaku Co., Ltd. and Consolidated Subsidiaries
As of May 31, 2007 and 2006

	Millions of yen									
	Shareholders' equity					Valuation and translation adjustments			Minority interests	Total net assets
	Common stock	Additional paid-in capital	Retained earnings	Less treasury stock, at cost	Total shareholders' equity	Unrealized holding gains on other securities	Translation adjustments	Total valuation and translation adjustments		
Balance as of May 31, 2005	¥14,932	¥17,260	¥68,109	¥(294)	¥100,007	¥3,231	¥ 571	¥3,803	¥ 6,805	¥110,616
Cash dividends paid			(2,128)		(2,128)					(2,128)
Bonuses to directors and corporate auditors			(65)		(65)					(65)
Net income			9,641		9,641					9,641
Purchases of treasury stock				(111)	(111)					(111)
Disposition of treasury stock		4		7	11					11
Decrease due to merger of consolidated subsidiaries			(60)		(60)					(60)
Increase resulting from newly consolidated subsidiaries			80		80					80
Equity in earnings of subsidiaries			1,624		1,624					1,624
Net change in items other than shareholders' equity						1,985	586	2,572	4,847	7,420
Total movements during the year	–	4	9,092	(103)	8,993	1,985	586	2,572	4,847	16,413
Balance as of May 31, 2006	14,932	17,264	77,201	(398)	109,000	5,216	1,158	6,375	11,653	127,030
Cash dividends paid			(4,453)		(4,453)					(4,453)
Bonuses to directors and corporate auditors			(18)		(18)					(18)
Net income			6,610		6,610					6,610
Purchases of treasury stock				(123)	(123)					(123)
Disposition of treasury stock		4		7	12					12
Increase resulting from newly consolidated subsidiaries			140		140					140
Net change in items other than shareholders' equity						(148)	118	(29)	1,065	1,035
Total movements during the year	–	4	2,279	(116)	2,167	(148)	118	(29)	1,065	3,203
Balance as of May 31, 2007	¥14,932	¥17,269	¥79,481	¥(514)	¥111,168	¥5,068	¥1,276	¥6,345	¥12,719	¥130,233

	Thousands of U.S. dollars									
	Shareholders' equity					Valuation and translation adjustments			Minority interests	Total net assets
	Common stock	Additional paid-in capital	Retained earnings	Less treasury stock, at cost	Total shareholders' equity	Unrealized holding gains on other securities	Translation adjustments	Total valuation and translation adjustments		
Balance as of May 31, 2006	\$122,705	\$141,868	\$634,407	\$(3,270)	\$895,718	\$42,863	\$ 9,515	\$52,387	\$ 95,759	\$1,043,881
Cash dividends paid			(36,592)		(36,592)					(36,592)
Bonuses to directors and corporate auditors			(147)		(147)					(147)
Net income			54,318		54,318					54,318
Purchases of treasury stock				(1,010)	(1,010)					(1,010)
Disposition of treasury stock		32		57	89					89
Increase resulting from newly consolidated subsidiaries			1,150		1,150					1,150
Net change in items other than shareholders' equity						(1,216)	969	(238)	8,751	8,505
Total movements during the year	–	32	18,727	(953)	17,807	(1,216)	969	(238)	8,751	26,320
Balance as of May 31, 2007	\$122,705	\$141,909	\$653,143	\$(4,223)	\$913,534	\$41,646	\$10,485	\$52,140	\$104,519	\$1,070,202

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Nippon Kayaku Co., Ltd. and Consolidated Subsidiaries
Years Ended May 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2007	2006	2007
Cash flows from operating activities			
Income before income taxes and minority interests	¥13,608	¥18,629	\$111,825
Adjustments to reconcile income before income taxes and minority interests to net cash provided by operating activities:			
Depreciation and amortization	8,730	7,708	71,739
Loss on impairment of fixed assets	819	192	6,730
Changes in reserves	1,255	(53)	10,313
Interest and dividend income	(361)	(430)	(2,966)
Interest expense	450	430	3,697
Equity in earnings of affiliates	(142)	(444)	(1,166)
Loss (gain) on disposal of property, plant and equipment, net	831	(4,939)	6,828
Loss (gain) on sales of investment securities, net	(191)	(7)	(1,569)
Changes in operating assets and liabilities:			
Notes and accounts receivable – trade	(355)	1,613	(2,917)
Inventories	681	(2,349)	5,596
Notes and accounts payable – trade	(1,244)	(758)	(10,222)
Payables – other	(757)	(138)	(6,220)
Other	(380)	(3,602)	(3,122)
Subtotal	22,944	15,848	188,544
Interest and dividends received	638	832	5,242
Interest paid	(542)	(354)	(4,453)
Income taxes paid	(2,839)	(4,535)	(23,329)
Net cash provided by operating activities	20,201	11,791	166,003
Cash flows from investing activities			
Purchases of time deposits, net	(46)	(2)	(378)
Purchase of marketable securities, net	5,497	(5,497)	45,172
Purchase of property, plant and equipment	(17,219)	(8,782)	(141,498)
Proceeds from sales of property, plant and equipment	307	8,099	2,522
Acquisition of goodwill and other intangible assets	(185)	(848)	(1,520)
Proceeds from sales (purchases) of investment securities, net	(3,406)	170	(27,989)
Purchase of investment securities of consolidated subsidiaries	–	(9)	–
Removal loss of property, plant and equipment	(2,223)	–	(18,267)
Other	(606)	(230)	(4,979)
Net cash used in investing activities	(17,882)	(7,102)	(146,947)
Cash flows from financing activities			
Net change in short-term debt	61	(538)	501
Proceeds from long-term debt	10,000	945	82,176
Repayment of long-term debt	(3,232)	(3,392)	(26,559)
Repayment of construction cooperation fund	(234)	(234)	(1,922)
Cash dividends paid	(4,434)	(2,119)	(36,436)
Increase due to issuance of additional shares by a consolidated subsidiary to third parties	–	4,524	–
Other	(600)	(368)	(4,930)
Net cash provided by (used in) financing activities	1,559	(1,182)	12,811
Effect of exchange rate changes on cash and cash equivalents	166	211	1,364
Increase in cash and cash equivalents	4,044	3,718	33,231
Cash and cash equivalents at beginning of year	21,424	17,191	176,053
Increase due to inclusion in consolidation	119	504	977
Increase due to merger by a subsidiary	–	11	–
Cash and cash equivalents at end of year	¥25,589	¥21,424	\$210,280

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Nippon Kayaku Co., Ltd. and Consolidated Subsidiaries
May 31, 2007 and 2006

Note 1

Basis of Consolidated Financial Statements

a. Basis of Preparation

The books and records of Nippon Kayaku Co., Ltd. (the "Company") and its consolidated domestic subsidiaries are maintained in the manner and form required or permitted under the Corporate Law of Japan and Japanese accounting practices. The books and records of overseas consolidated subsidiaries are maintained in conformity with the accounting principles and relevant legal requirements of their countries of domicile.

The accompanying consolidated financial statements of the Company and consolidated subsidiaries are prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and are compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan.

In addition, the notes to the consolidated financial statements include information which is not required under accounting principles generally accepted in Japan but is presented herein as additional information.

As permitted by the Securities and Exchange Law of Japan, amounts of less than one million yen have been omitted. As a result, the totals shown in the accompanying consolidated financial statements (both in yen and in dollars) do not necessarily agree with the sums of the individual amounts.

Certain amounts previously reported have been reclassified to conform to the current year's presentation.

b. Basis of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its significant subsidiaries controlled directly or indirectly by the Company (the "Companies"). Investment in companies over which the Company exercises significant influence in terms of their operating and financial policies have been included in the consolidated financial statements on an equity method of accounting.

All significant intercompany balances and transactions have been eliminated in consolidation.

Investments in unconsolidated subsidiaries and affiliates not accounted for by the equity method are generally stated at cost.

The differences at the dates of acquisition between the cost and underlying net equity of the consolidated subsidiaries and companies accounted for by the equity method are being amortized by the straight-line method over a period of five years. However, the goodwill generated in the United States consolidated subsidiary is no longer amortized by the United States accounting standard, and the impairment testing is made annually.

c. Foreign Currency Translation

The revenue and expense accounts of the foreign subsidiaries are translated at the average exchange rates prevailing during the year.

The accounts of foreign consolidated subsidiaries, except for the components of shareholders' equity, are translated into yen at the rates of exchange in effect at the balance sheet date. The components of shareholders' equity are translated at their historical exchange rates. Translation differences arising from the translation of the financial statements of the foreign consolidated subsidiaries are presented as translation adjustments.

Monetary assets and liabilities denominated in foreign currencies of the Company and its domestic consolidated subsidiaries are translated into yen at the current rates except for those hedged by forward foreign exchange contracts, which are translated at the contracted rates.

Gains and losses arising from exchange differences are credited or charged to income in the year incurred.

d. Cash Equivalents

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Note 1

Basis of Consolidated Financial Statements
(continued)

e. Securities

Securities are classified into three categories: trading, held-to-maturity or other securities. Trading securities are carried at fair value and held-to-maturity securities are carried at amortized cost. Marketable securities classified as other securities are carried at fair value with changes in unrealized holding gain or loss, net of the applicable income taxes, included directly in shareholders' equity. Non-marketable securities classified as other securities are carried at cost. Cost of securities sold is determined by the moving average method.

f. Inventories

Inventories are stated at cost determined principally by the average method.

g. Property, Plant and Equipment

Property, plant and equipment is stated at cost except that the cost of certain assets has been reduced by certain capital gains in accordance with the Corporation Tax Law of Japan.

Depreciation is mainly computed by the declining-balance method, except that the straight-line method is applied to the buildings which were acquired after April 1, 1998 based on the estimated useful lives of the respective assets. Moreover, the method of depreciation based on the revised Corporation Tax Law is applied for acquisitions after April 1, 2007.

h. Leases

Finance lease transactions are primarily accounted for as operating leases except that lease agreements which stipulate transfer of ownership of the leased assets to the lessee are accounted for as finance leases.

i. Retirement Benefits

The lump-sum payment plans and the tax-qualified pension plans were integrated into the defined benefit pension plan on June 1, 2006.

Domestic consolidated subsidiaries have defined benefit plans, i.e., welfare pension fund plans, tax-qualified pension plans and lump-sum payment plans, covering substantially all employees who are entitled to lump-sum or annuity payments, the amounts of which are determined by reference to their basic rates of pay, length of service, and the conditions under which termination occurs. Certain foreign subsidiaries have defined contribution plans.

Accrued employees' retirement benefits are provided mainly at an amount calculated based on the retirement benefit obligation and the fair value of the pension plan assets at the balance sheet dates, as adjusted for unrecognized actuarial gain or loss, and unrecognized past service cost. The retirement benefit obligation is attributed to each period by the straight-line method over the estimated years of service of the eligible employees. Actuarial gain and loss are amortized in the year following the year in which the gain or loss is recognized primarily by the straight-line method over periods of 10 years which are shorter than the average remaining years of service of the eligible employees. Past service cost is amortized primarily by the straight-line method over periods of 10 years which are shorter than the average remaining years of service of the eligible employees.

j. Derivative Financial Instruments

The Company has entered into derivative transactions in order to manage certain risks arising from adverse fluctuations in foreign currency exchange rates. Derivatives are carried at fair value with changes in unrealized gains or losses charged or credited to operations. Receivables and payables hedged by qualified derivatives are translated at the corresponding foreign exchange contract rates.

Note 2

U.S. Dollar Amounts

The translation of yen amounts into U.S. dollar amounts is included solely for the convenience of readers outside Japan. The rate of ¥121.69 = U.S.\$1, the approximate rate of exchange on May 31, 2007, has been used. The inclusion of such amounts is not intended to imply that the yen amounts have been or could be readily converted, realized or settled in U.S. dollars at that or any other rate.

Note 3

Accounting Changes

The method of depreciation of fixed assets "Property, plant and equipment" acquired after April 1, 2007 has been changed to the method of depreciation based on the revised Corporation Tax Law of Japan in 2007 fiscal year. The effect of the change to the 2007 profit and loss was immaterial.

Note 4

Inventories

Inventories at May 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Merchandise	¥ 3,583	¥ 3,595	\$ 29,443
Finished products	9,874	10,452	81,140
Semi-finished products and work in process	6,771	6,230	55,641
Raw materials and supplies	5,951	6,370	48,902
	¥26,180	¥26,649	\$215,136

Note 5

Marketable and Investment Securities

Information regarding marketable securities classified as other securities as of May 31, 2007 and 2006 were as follows:

Marketable other securities

	May 31, 2007					
	Millions of yen			Thousands of U.S. dollars		
	Acquisition cost	Carrying value	Unrealized gain (loss)	Acquisition cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their acquisition cost:						
Stock	¥5,801	¥14,460	¥8,658	\$47,670	\$118,826	\$71,147
Debt securities	—	—	—	—	—	—
Other	1,905	1,908	3	15,654	15,679	24
Subtotal	7,707	16,369	8,661	63,333	134,513	71,172
Securities whose acquisition cost exceeds their carrying value:						
Stock	1,023	870	(152)	8,406	7,149	(1,249)
Debt securities	—	—	—	—	—	—
Other	1,059	1,055	(3)	8,702	8,669	(24)
Subtotal	2,082	1,926	(156)	17,109	15,827	(1,281)
Total	¥9,790	¥18,295	¥8,505	\$80,450	\$150,341	\$69,890

	May 31, 2006		
	Millions of yen		
	Acquisition cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their acquisition cost:			
Stock	¥2,867	¥11,555	¥8,688
Debt securities	—	—	—
Other	1,803	1,804	0
Subtotal	4,670	13,359	8,688
Securities whose acquisition cost exceeds their carrying value:			
Stock	1,070	1,051	(18)
Debt securities	—	—	—
Other	1,459	1,449	(9)
Subtotal	2,530	2,501	(28)
Total	¥7,200	¥15,861	¥8,660

Sales of securities classified as other securities amounted to ¥539 million (\$4,429 thousand) as of May 31, 2007 with the aggregate gain of ¥191 million (\$1,569 thousand) and the aggregate loss of ¥0 million (\$0 thousand) for the year ended May 31, 2007.

Note 6**Depreciation**

Depreciation of property, plant and equipment were ¥7,888 million (\$64,820 thousand) and ¥6,756 million for the years ended May 31, 2007 and 2006, respectively.

Note 7**Short-Term Bank Loans and Long-Term Debt**

Short-term bank loans are unsecured and are generally represented by 60-day notes. The weighted average interest rates for the years ended May 31, 2007 and 2006 were approximately 3.41% and 3.17%, respectively.

The interest rates applicable to the long-term borrowings (except for current portion) at May 31, 2007 and 2006 average approximately 1.98% and 2.61%, respectively.

Long-term debt at May 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Collateralized loans from banks, insurance companies, government agencies and other financial institutions, due through 2015	¥ 1,616	¥ 1,806	\$ 13,279
Loans without collateral	15,405	8,314	126,592
	17,021	10,120	139,871
Less current portion	(4,987)	(2,944)	(40,981)
	¥12,033	¥ 7,175	\$ 98,882

The aggregate annual maturities of long-term debt subsequent to May 31, 2007 are as follows:

	Millions of yen	Thousands of U.S. dollars
Year ending May 31, 2008	¥ 4,987	\$ 40,981
2009	4,170	34,267
2010	2,878	23,650
2011 and thereafter	4,985	40,964
	¥17,021	\$139,871

Assets pledged as collateral for long-term debt, other non-current liabilities and payables-trade at May 31, 2007 are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Investment securities	¥ 201	\$ 1,651
Property, plant and equipment, at net book value	10,249	84,222
	¥10,450	\$85,873

Note 8**Income Taxes**

The Company and its domestic consolidated subsidiaries are subject to a number of taxes based on income which, in the aggregate, resulted in statutory tax rate of 40.69% in 2007 and 2006. Income taxes of the foreign consolidated subsidiaries are based generally on the tax rates applicable in their countries of incorporation.

There was no significant difference between the normal effective statutory income tax rate and the effective income tax rate reflected in the accompanying consolidated statements of income for the year ended May 31, 2007 and 2006.

The significant components of deferred tax assets and liabilities as of May 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Deferred tax assets:			
Accrued retirement benefits	¥ 2,288	¥ 2,294	\$ 18,801
Accrued bonuses	1,255	1,352	10,313
Accrued enterprise tax	483	178	3,969
Allowance for sales rebate	167	141	1,372
Tax loss carried forward	2,822	1,971	23,190
Other	1,452	1,200	11,931
Total deferred tax assets	8,469	7,140	69,594
Valuation allowance	(3,075)	(2,169)	(25,269)
	5,393	4,971	44,317
Deferred tax liabilities:			
Adjustment of acquisition costs of fixed assets	(3,178)	(2,505)	(26,115)
Special reserve for adjustment of acquisition costs of fixed assets	–	(1,006)	–
Unrealized holding gains on other securities	(3,461)	(3,572)	(28,441)
Adjustments on book value relating to land of consolidated subsidiaries	(706)	(706)	(5,801)
Goodwill and other intangible assets	(382)	(420)	(3,139)
Other	(364)	(392)	(2,991)
Total deferred tax liabilities	(8,092)	(8,602)	(66,496)
Net deferred tax assets (liabilities)	¥(2,698)	¥(3,630)	\$(22,171)

Note 9**Stock Options**

Information relating to fiscal year ended May 31, 2007 (from June 1, 2006 to May 31, 2007) are as follows:

(1) Overview, volume and changes

[1] Overview

Company Name	MOXTEK Inc.
Date of resolution	February 10, 2004
Persons granted	2 directors of the Company, 12 executives of the Company, 2 others
Number of stock options granted by class of stock (NOTE)	Common stock 100,000
Date of grant	February 10, 2004
Vesting conditions	Continuous service from the date of grant (February 10, 2004) to the right fixation day (February 10, 2004), or, not exceeding 30 days after termination.
Service period	No service period is specified
Exercise period	From February 10, 2004 to February 9, 2009

Note: The given common stock is a common stock without the right to vote.

Note: The number of options is described after being translated into the number of shares.

Note 9

Stock Options
(continued)

(1) Overview, volume and changes (continued)

[1] Overview (continued)

Company Name	MOXTEK Inc.
Date of resolution	March 10, 2005
Persons granted	5 executives of the Company, 2 others
Number of stock options granted by class of stock (NOTE)	Common stock 31,000
Date of grant	March 10, 2005
Vesting conditions	Continuous service from the date of grant (March 10, 2005) to the right fixation day (March 10, 2005), or, not exceeding 30 days after termination.
Service period	No service period is specified
Exercise period	From March 10, 2005 to March 9, 2010

Company Name	MOXTEK Inc.
Date of resolution	February 2, 2006
Persons granted	4 executives of the Company, 1 others
Number of stock options granted by class of stock (NOTE)	Common stock 10,000 shares
Date of grant	February 2, 2006
Vesting conditions	Continuous service from the date of grant (February 2, 2006) to the right fixation day (February 2, 2006), or, not exceeding 30 days after termination.
Service period	No service period is specified
Exercise period	From February 2, 2006 to February 1, 2011

Company Name	MOXTEK Inc.
Date of resolution	March 30, 2006
Persons granted	1 director of the Company
Number of stock options granted by class of stock (NOTE)	Common stock 10,000 shares
Date of grant	March 30, 2006
Vesting conditions	Continuous service from the date of grant (March 30, 2006) to the right fixation day (March 30, 2006), or, not exceeding 30 days after termination.
Service period	No service period is specified
Exercise period	From March 30, 2006 to March 29, 2011

Company Name	MOXTEK Inc.
Date of resolution	January 31, 2007
Persons granted	2 directors of the Company
Number of stock options granted by class of stock (NOTE)	Common stock 20,000 shares
Date of grant	January 31, 2007
Vesting conditions	Continuous service from the date of grant (January 31, 2007) to the right fixation day (January 31, 2007), or, not exceeding 30 days after termination.
Service period	No service period is specified
Exercise period	From January 31, 2007 to January 31, 2012

Company Name	MOXTEK Inc.
Date of resolution	February 14, 2007
Persons granted	9 directors of the Company, 10 executives of the Company, 8 others
Number of stock options granted by class of stock (NOTE)	Common stock 80,000 shares
Date of grant	February 14, 2007
Vesting conditions	Continuous service from the date of grant (February 14, 2007) to the right fixation day (February 14, 2007), or, not exceeding 30 days after termination.
Service period	No service period is specified
Exercise period	From February 14, 2007 to February 14, 2012

Note: The given common stock is a common stock without the right to vote.

Note: The number of options is described after being translated into the number of shares.

[2] Volume and changes of stock options

a. Number of stock options

Company Name	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.
Date of resolution	February 10, 2004	March 10, 2005	February 2, 2006	March 30, 2006	January 31, 2007	February 14, 2007
Prior to vesting						
Beginning of period	–	–	–	–	–	–
Granted	–	–	–	–	–	–
Forfeited	–	–	–	–	–	–
Vested	–	–	–	–	–	–
Unvested	–	–	–	–	–	–
After vesting						
Beginning of period	63,050	24,250	10,000	10,000	–	–
Vested	–	–	–	–	20,000	80,000
Exercised	46,700	6,750	–	–	–	–
Forfeited	–	–	–	–	–	–
Outstanding	16,350	17,500	10,000	10,000	20,000	80,000

b. Unit price information

(In U.S. dollar)

Company Name	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.	MOXTEK Inc.
Date of resolution	February 10, 2004	March 10, 2005	February 2, 2006	March 30, 2006	January 31, 2007	February 14, 2007
Exercise price	4.66	8.70	17.16	17.16	25.13	25.13
Average stock market price at exercise	–	–	–	–	–	–
Fair value unit price at grant date	–	–	–	–	–	–

(2) Estimate method of fair value unit price

A fair evaluation unit price is calculated by origin value about the incentive stock option because a consolidated subsidiary concerned is a non public enterprise.

[1] Method of evaluating the stock that become bases of value calculation: DCF method etc.

[2] Amount of total of origin value at the end of the fiscal year: – yen

[3] Amount of total of origin value on the right of incentive stock option to which right was exercised at the end of the fiscal year: Not applicable

Note 10

Retirement Benefit Plans

The following table sets forth the funded and accrued status of the plans, and the amounts recognized in the consolidated balance sheets as of May 31, 2007 and 2006 for the Company's and the consolidated subsidiaries' defined benefit plans:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Retirement benefit obligation	¥(25,380)	¥(25,579)	\$(208,562)
Plan assets at fair value	25,992	24,700	213,591
Unfunded retirement benefit obligation	611	(878)	5,020
Unrecognized actuarial gain or loss	(2,282)	(331)	(18,752)
Unrecognized past service cost	(1,910)	(1,351)	(15,695)
Net retirement benefit obligation	(3,581)	(2,561)	(29,427)
Prepaid pension cost	322	5,463	2,646
Accrued retirement benefits	¥ (3,904)	¥ (8,025)	\$ (32,081)

Note 10**Retirement Benefit Plans***(continued)*

The components of retirement benefit expenses for the year ended May 31, 2007 and 2006 are outlined as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Service cost	¥1,318	¥1,428	\$10,830
Interest cost	495	492	4,067
Expected return on plan assets	(336)	(187)	(2,761)
Amortization of actuarial gain or loss	204	662	1,676
Amortization of past service cost	(291)	(206)	(2,391)
Total	¥1,389	¥2,189	\$11,414

The assumptions used in accounting for the above plans were as follows:

	May 31,	
	2007	2006
Discount rates	2.0% – 2.1%	2.0% – 2.1%
Expected rates of return on plan assets	1.0% – 2.1%	1.0% – 2.1%
Period for amortization of prior service liability	10 years	10 years
Period for recognition of actuarial gain or loss	10 years	10 years

Accrued retirement benefits included ¥76 million (\$624 thousand) for directors and corporate auditors of the Company and its domestic consolidated subsidiaries at May 31, 2007.

Note 11**Research and Development Expenses**

Research and development expenses amounted to ¥10,897 million (\$89,547 thousand) and ¥10,419 million for the years ended May 31, 2007 and 2006, respectively.

Note 12**Contingent Liabilities**

Contingent liabilities of the companies at May 31, 2007 were as follows:

	Millions of yen	Thousands of U.S. dollars
	¥	\$
Notes receivable discounted	178	1,462
Guarantees of loans of employees	2,189	17,988
Guarantees of loans of non-consolidated subsidiary	300	2,465

Note 13**Amounts per Share**

	Yen		Thousands of U.S. dollars
	2007	2006	2007
For the year ended May 31:			
Net income:			
Primary	¥ 36.37	¥ 52.92	\$0.29
Diluted	36.11	—	0.29
Cash dividends	20.00	20.00	0.16
At May 31:			
Net assets	646.78	634.51	5.31

Note 14
Derivatives

- (1) The Companies utilize forward foreign exchange contracts solely in order to hedge against the risk of fluctuations in foreign currency exchange rates and to stabilize their future cash flows relating to debts denominated in foreign currencies relating to their operations.
- (2) The Companies have entered into derivative transactions solely in order to hedge against certain risks in compliance with their internal policies. The Companies have not and do not utilize derivatives for speculative trading purposes.
- (3) The Companies are exposed to the risk of credit loss in the event of nonperformance by the counterparties to these derivative transactions, but consider the risk of any such loss to be minimal because the Companies enter into derivative transactions only with financial institutions which have high credit ratings.
- (4) The Companies enter into, monitor and manage their derivative positions based on their own internal policies.

Note 15
Leases

Lease payments relating to finance lease transactions accounted for as operating leases amounted to ¥354 million (\$2,909 thousand) and ¥385 million for the years ended May 31, 2007 and 2006, respectively.

Future minimum lease payments (including the interest portion) subsequent to May 31, 2007 relating to finance lease transactions accounted for as operating leases are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Year ending May 31, 2008	¥263	\$2,161
2009 and thereafter	306	2,514
	¥570	\$4,684

Lease income relating to finance leases accounted for as operating leases amounted to ¥51 million (\$419 thousand) and ¥51 million for the years ended May 31, 2007 and 2006, respectively.

Note 16
Segment Information

The Companies operate principally in four industry segments: functional chemicals, pharmaceuticals, fine chemicals and other businesses. The functional business involves the production and sales of inflators, functional materials, catalysts and electric materials. The fine chemical business involves the production and sales of agro, color chemicals and explosives. Other businesses comprises real estate leasing business.

Industry segment information for the Companies as of or for the years ended May 31, 2007 and 2006 is summarized as follows:

	2007						
	Millions of yen						
	Functional chemicals business	Pharmaceuticals business	Fine chemicals business	Other businesses	Total	Eliminations	Consolidated
I. Sales and operating income:							
Sales to third parties	¥78,925	¥41,700	¥24,538	¥ 2,960	¥148,124	–	¥148,124
Intersegment	116	1	293	6	418	¥ (418)	–
Total	79,042	41,702	24,831	2,967	148,542	(418)	148,124
Operating expenses	70,734	34,227	22,990	1,374	129,326	5,261	134,588
Operating income	¥ 8,307	¥ 7,475	¥ 1,840	¥ 1,592	¥ 19,215	¥ (5,679)	¥ 13,536
II. Asset depreciation and capital expenditures:							
Total assets	¥89,852	¥40,075	¥27,067	¥16,550	¥173,545	¥33,535	¥207,081
Depreciation and amortization	4,575	1,818	1,149	608	8,152	577	8,730
Loss on impairment of fixed assets	819	–	–	–	819	–	819
Capital expenditures	11,883	1,213	1,417	101	14,615	422	15,038

Note 16

Segment Information
(continued)

	2007						
	Thousands of U.S. dollars						
	Functional chemicals business	Pharmaceuticals business	Fine chemicals business	Other businesses	Total	Eliminations	Consolidated
I. Sales and operating income:							
Sales to third parties	\$648,574	\$342,674	\$201,643	\$ 24,324	\$1,217,224	–	\$1,217,224
Intersegment	953	8	2,407	49	3,434	\$ (3,434)	–
Total	649,535	342,690	204,051	24,381	1,220,659	(3,434)	1,217,224
Operating expenses	581,263	281,263	188,922	11,290	1,062,749	43,232	1,105,990
Operating income	\$ 68,263	\$ 61,426	\$ 15,120	\$ 13,082	\$ 157,901	\$ (46,667)	\$ 111,233
II. Asset depreciation and capital expenditures:							
Total assets	\$738,367	\$329,320	\$222,425	\$136,001	\$1,426,123	\$275,577	\$1,701,709
Depreciation and amortization	37,595	14,939	9,442	4,996	66,989	4,741	71,739
Loss on impairment of fixed assets	6,730	–	–	–	6,730	–	6,730
Capital expenditures	97,649	9,967	11,644	829	120,100	3,467	123,576

	2006						
	Millions of yen						
	Functional chemicals business	Pharmaceuticals business	Fine chemicals business	Other businesses	Total	Eliminations	Consolidated
I. Sales and operating income:							
Sales to third parties	¥73,133	¥39,774	¥24,028	¥ 3,089	¥140,026	–	¥140,026
Intersegment	86	8	64	8	167	¥ (167)	–
Total	73,219	39,783	24,093	3,097	140,194	(167)	140,026
Operating expenses	63,042	34,283	22,208	1,571	121,106	5,700	126,806
Operating income	¥10,177	¥ 5,499	¥ 1,884	¥ 1,526	¥ 19,087	¥(5,867)	¥ 13,219
II. Asset depreciation and capital expenditures:							
Total assets	¥83,041	¥39,667	¥28,500	¥16,992	¥168,202	¥37,106	¥205,308
Depreciation and amortization	3,689	1,614	1,175	661	7,141	567	7,708
Loss on impairment of fixed assets	–	–	–	–	–	192	192
Capital expenditures	9,334	2,230	1,324	33	12,923	878	13,802

Overseas sales, which include export sales of the Company and its consolidated subsidiaries, totaled ¥50,168 million (\$412,260 thousand) and ¥42,280 million, or 33.8% and 30.2% of the consolidated net sales for the years ended May 31, 2007 and 2006, respectively.

Note 17

Subsequent Events

(1) The following appropriations of retained earnings of the Company were approved at a meeting of the shareholders held on August 30, 2007:

	Millions of yen	Thousands of U.S. dollars
2007 year-end cash dividends (¥10 = \$0.082 per share)	¥1,816	\$14,923

(2) The Company and Asahi Kasei Chemicals Corporation concluded the basic agreement that agreed to integration, and the reorganization of manufacturing, sales, and the research and development business that lay an industrial gunpowder business that each enterprise group was doing to the joint venture company by the cooperation of both investments dated June 5, 2007. The system of the product supply of stabler and the high quality is constructed, and the business base of industrial gunpowder that is indispensable Basic Industry material to the infrastructure maintenance of our country is strengthened by this integration in the industrial gunpowder industry that exists for the long-term and structurally in the severe environment because of the investment in public works reduction, etc. Details of the method of integration and reorganization, etc. are assumed to provide in the joint master agreement that is scheduled to be settled on, and to concluded in the future.

Report of Independent Auditors



■ Certified Public Accountants
Hibiya Kokusai Bldg.
2-2-3, Uchisaiwai-cho
Chiyoda-ku, Tokyo, Japan 100-0011
C.P.O. Box 1196, Tokyo, Japan 100-8641

■ Tel: 03 3503 1100
Fax: 03 3503 1197

Report of Independent Auditors

The Board of Directors
Nippon Kayaku Co., Ltd.

We have audited the accompanying consolidated balance sheets of Nippon Kayaku Co., Ltd. and consolidated subsidiaries as of May 31, 2007 and 2006, and the related consolidated statements of income, changes in net assets, and cash flows for the years then ended, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Nippon Kayaku Co., Ltd. and consolidated subsidiaries at May 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

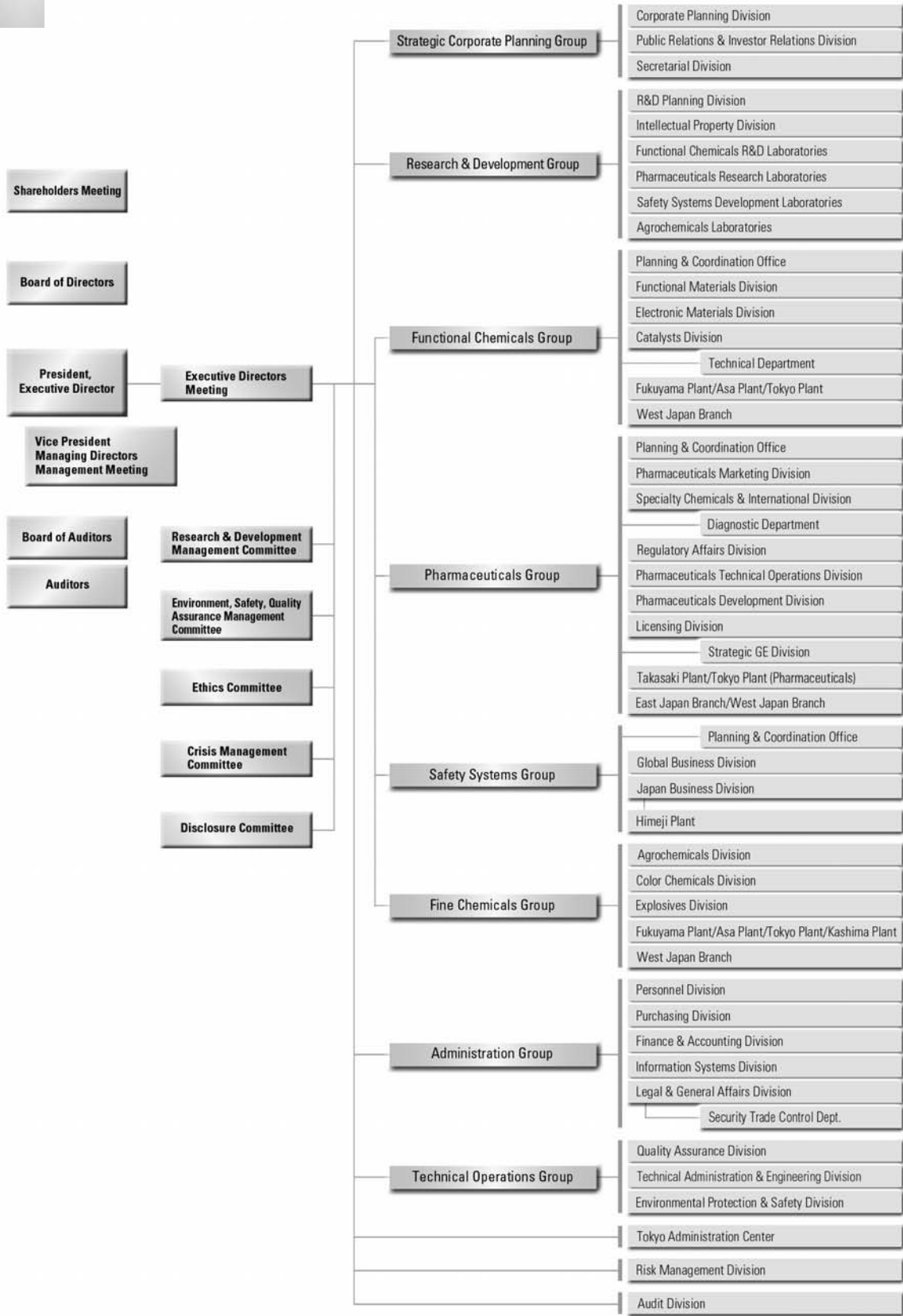
The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended May 31, 2007 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 2.

Ernst & Young Shin Nihon

August 30, 2007

Organization

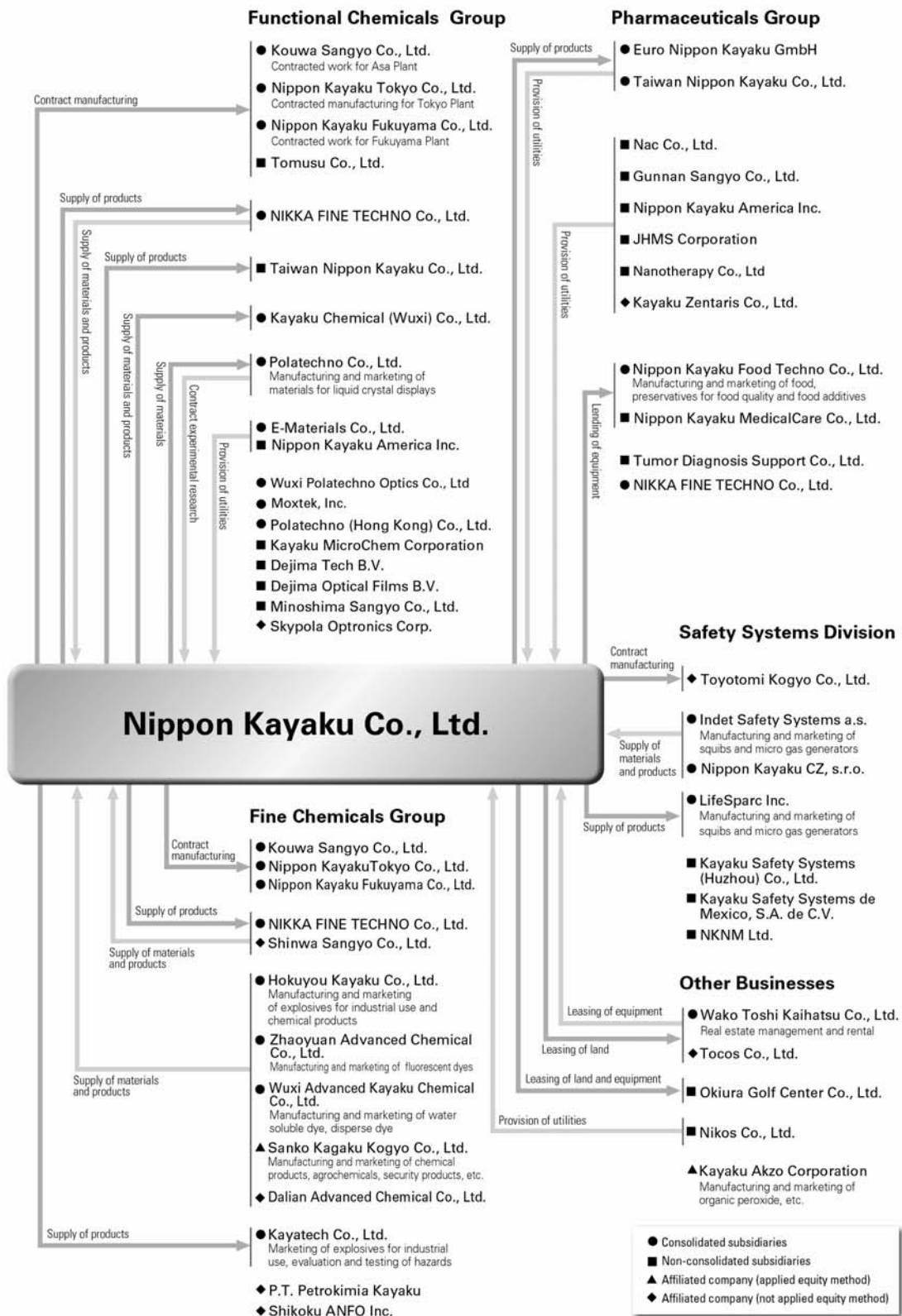
As of October 1, 2007



Group Companies

As of October 1, 2007

The Nippon Kayaku Group comprises Nippon Kayaku Co., Ltd., subsidiary companies, and affiliated companies. The outline of the placement of each company in the relevant business is as shown below.



Corporate Information

As of October 1, 2007

- **Business Name** Nippon Kayaku Co., Ltd.
- **Representative** Koichiro Shimada, President
- **Foundation** June 5, 1916
- **Head Office Address** Tokyo Fujimi Bldg., 11-2, Fujimi 1-chome, Chiyoda-ku, Tokyo 102-8172, Japan
- **Number of Employees** 1,933 (non-consolidated), 4,423 (consolidated) (as of May 31, 2007)
- **Banks of Accounts** Bank of Tokyo-Mitsubishi UFJ, Mizuho Bank, Joyo Bank

■ Business Area

Functional Chemicals

- Functional Materials Division** Epoxy resins, Epoxy resin curers, Combustion retardants for synthetic resins, UV-curing type resins, Polyimide/polyamide resins
- Electronic Materials Division** Optical functional films, Optical disk materials, Optical materials, Functional colors, Colors for inkjet printers, LCD projector components
- Catalysts Division** Catalysts for the production of acrylic acid and methacrylic acid, Plant licensing business

Pharmaceuticals

Anti-cancer agents, Neurological agents, Circulatory system agents, Digestive system agents, Metabolic agents, Antibiotics, Anti-inflammatory analgesic agents, Pharmaceutical API and intermediates, Food and food additives, Preservatives for food quality, Veterinary pharmaceuticals, Animal feedstuffs and feedstuff additives, Diagnostics

Safety Systems

Airbag inflators, Micro gas generators for seatbelt pretensioners, Squibs

Fine Chemicals

- Agrochemicals Division** Insecticides, Herbicides, Fungicides, Acaricide, Public hygiene insecticides, Biological pesticides, Soil disinfectant, Animal repellents
- Color Chemicals Division** Disperse dyes, Cationic dyes, Acidic dyes, Reactive dyes, Direct dyes, Sulphur dyes, Fluorescent dyes, Functional chemicals for textiles and paper, Special dyes for non-textile applications
- Explosives Division** Industrial explosives, Black powder, Electric detonators, Non-electric detonators, Concrete crushers, Hazard evaluation test, Pyrotechnics

Others

Real estate leasing

- **Head Office** Tokyo Fujimi Bldg., 11-2, Fujimi 1-chome, Chiyoda-ku, Tokyo 102-8172, Japan
- **East Japan Branch (Tokyo Office)** Tokyo Fujimi Bldg., 11-2, Fujimi 1-chome, Chiyoda-ku, Tokyo 102-8172, Japan
- Sapporo Office** Hiroyasu Bldg., 1-13-73, Minami 7-jyo Nishi, Chuo-ku, Sapporo-shi, Hokkaido 064-0807, Japan
- Nagoya Office** Taiko Creacion Bldg., 19-11, Kikui 2-chome, Nishi-ku, Nagoya-shi, Aichi 451-0044, Japan
- **West Japan Branch (Osaka Office)** Midouji Honmachi Bldg., 5-7, honmachi 3-chome, Chuo-ku, Osaka-shi, Osaka 541-0053, Japan
- Fukuoka Office** Nishitetsugion Bldg., 1-1, Gokushomachi, Hakata-ku, Fukuoka-shi, Fukuoka 812-0037, Japan
- **Tokyo Administration Center** 31-12, Shimo 3-chome, Kita-ku, Tokyo 115-8588, Japan
- **Laboratories**
 - Functional Chemicals R&D Laboratories** 31-12, Shimo 3-chome, Kita-ku, Tokyo 115-8588, Japan
 - Pharmaceuticals Research Laboratories** 31-12, Shimo 3-chome, Kita-ku, Tokyo 115-8588, Japan
 - Safety Systems Development Laboratories** 3903-39, Toyotomi, Toyotomicho, Himeji-shi, Hyogo 679-2123, Japan
 - Agrochemicals Laboratories** 6, Sunayama, Kamisu-shi, Ibaraki 314-0255, Japan
- **Plants**
 - Fukuyama Plant** 126, Minookicho, Fukuyama-shi, Hiroshima 721-8567, Japan
 - Asa Plant** 2300, Sanyoonoda-shi, Yamaguchi 757-8686, Japan
 - Tokyo Plant** 23-1, Shinden 1-chome, Adachi-ku, Tokyo 123-0865, Japan
 - Takasaki Plant** 239, Iwahanamachi, Takasaki-shi, Gunma 370-1208, Japan
 - Himeji Plant** 3903-39, Toyotomi, Toyotomicho, Himeji-shi, Hyogo 679-2123, Japan
 - Kashima Plant** 6, Sunayama, Kamisu-shi, Ibaraki 314-0255, Japan

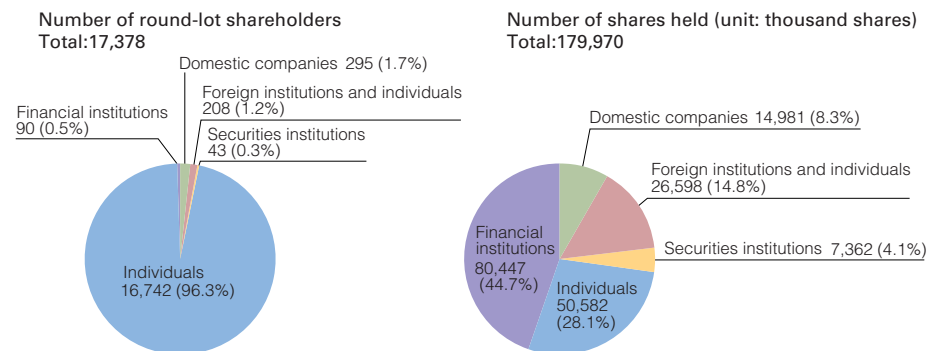
Investor Information

As of May 31, 2007

- Fiscal year June 1 to May 31
- Ordinary general meeting of shareholders Normally held in August in Tokyo.
- Record date Ordinary general meeting of shareholders: May 31
Year-end dividend: May 31
Interim dividend: November 30
- Stock exchange listing Tokyo stock exchanges
- Number of common stock Authorized: 700,000,000
Issued: 182,503,570
- Paid-in capital ¥14,932,922,842
- Number of shareholders 23,955
- Major shareholders

Shareholders	Number of shares held (unit: thousand)	Shareholding ratio
The Master Trust Bank of Japan, Ltd. (Trust account)	16,119	8.83
Japan Trustee Services Bank, Ltd. (Trust account)	10,878	5.96
Mizuho Bank, Ltd.	8,318	4.55
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	5,788	3.17
Meiji Yasuda Life Insurance Company	5,102	2.79
The Joyo Bank, Ltd.	5,089	2.78
Kayavestor Club	4,663	2.55
Nippon Life Insurance Company	3,274	1.79
Trust & Custody Services Bank Ltd. (Securities investment trust account)	3,118	1.70
Employees' stock holding	2,442	1.33

■ Breakdown of shareholders



- Transfer agent for common stock The Chuo Mitsui Trust and Banking Company, Limited
33-1, Shiba 3-chome, Minato-ku, Tokyo 105-8574, Japan

- Investor information Nippon Kayaku Co., Ltd
Public Relations & Investor Relations Division
Tokyo Fujimi Bldg., 11-2, Fujimi 1-chome, Chiyoda-ku,
Tokyo 102-8172 Japan
Phone: +81-3-3237-5046
Email: kouho@nipponkayaku.co.jp
URL: <http://www.nipponkayaku.co.jp/english/index.html>



Our company logo

This logo symbolizes Nippon Kayaku's company policies.
The space at the center represents the cosmos, world and expanses of the Earth.
The two soaring ellipses represent creativity and courage and the
two circles are the confidence between Nippon Kayaku, which
aspires to extraterrestrial space, and the public.

 **NIPPON KAYAKU CO.,LTD.**

Head Office: Tokyo Fujimi Bldg., 11-2, Fujimi 1-chome, Chiyoda-ku, Tokyo 102-8172, Japan
<http://www.nipponkayaku.co.jp/>