MANAGING OUR GROWTH, IN EVERY ASPECTS

Annual Report 2007

Year ended March 31, 2007

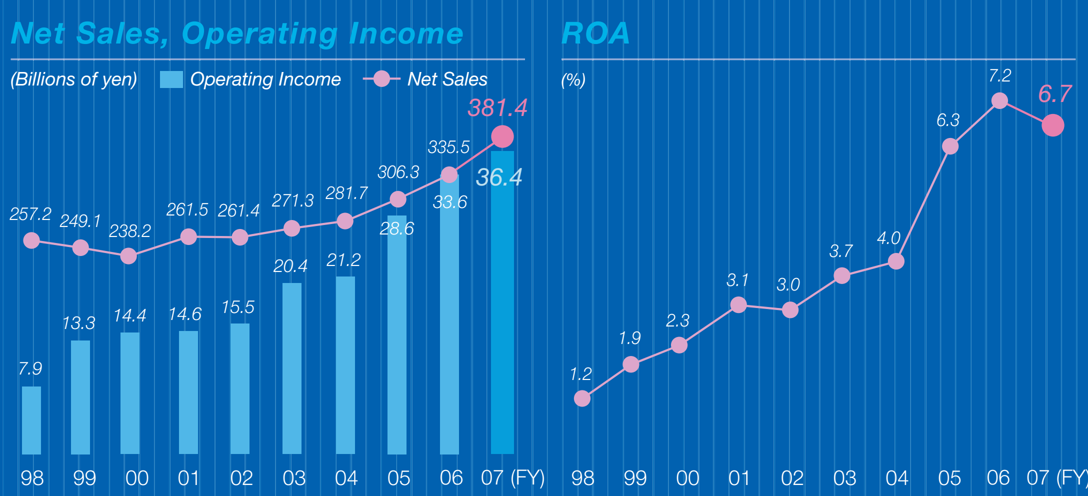
DAICEL CHEMICAL INDUSTRIES, LTD.

Previous Medium-Term Business Plan Targets

Targets Met One Year Ahead of Schedule

Daicel succeeded in achieving the three targets of its previous medium-term business plan one year ahead of their fiscal 2007 target date. The goals were net sales of ¥300 billion, operating income of ¥30 billion, and ROA (ratio of recurring profit to total assets) of 6.0%.

The engineering plastics and automobile airbag inflator businesses were the main factors behind this accomplishment. We also benefited from significant growth in sales of triacetyl cellulose (TAC), used in the manufacture of films for LCDs. In summary, we attribute our success to our focus on two of Japan's most dynamic sectors: automobiles and flat-panel displays.



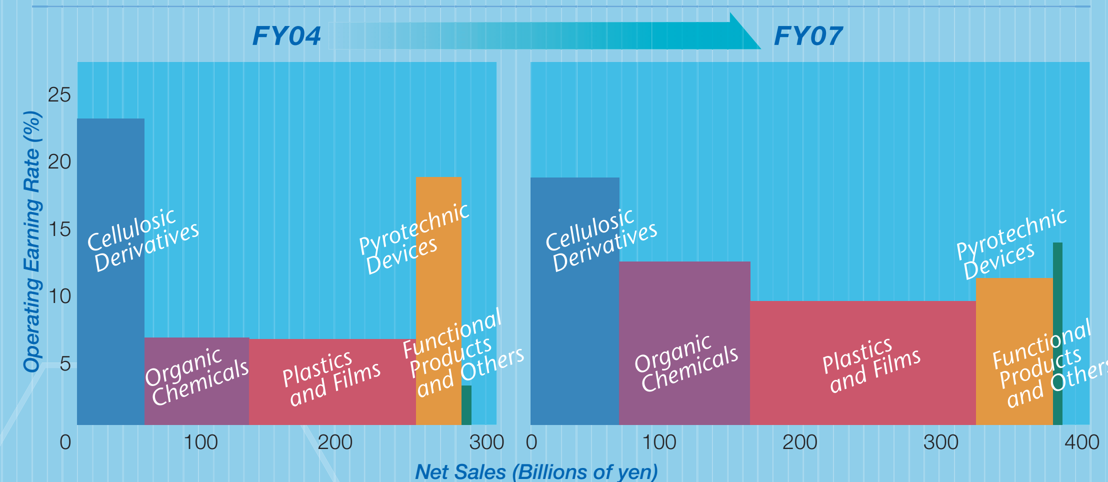
In the following sections, we describe in detail the changes Daicel made during the period of its medium-term plan from three perspectives: business portfolio, production innovation, and global business development.

Aspect 1: Business Portfolio

During the period covered by the plan, Daicel's well-balanced and robust business portfolio, centering on four segments, contributed to sturdy growth in earnings. Two of the segments are organic chemicals and plastics and films, both of which are expanding stably. There is also the pyrotechnic devices sector, which has rapidly grown into a core of our operations, as well as the cellulosic derivatives business, which has evolved into a key growth driver business owing to growth in LCD film applications.

Driven largely by expanding demand for automotive applications, the markets for engineering plastics (plastics and films segment) and airbag inflators (pyrotechnic devices segment) are experiencing considerable growth.

Changes in the Business Portfolio



Achievements of the Plan

- Steady growth in the inflators business
- Transformation of the cellulosic derivatives business from a core business to a key growth driver business

Future Challenges

- Development of new businesses

Aspect 2: Production Innovation

Guided by the previous medium-term business plan, the Company pursued production innovation activities in its chemical plants. In addition to enabling fewer workers to be required, these initiatives helped stabilize our operations and deliver significant cost reductions.

Daicel's initiatives have been highly acclaimed, as illustrated by their mention in the fiscal 2006 Monozukuri* White Paper issued by the Ministry of Economy, Trade and Industry. The Company has launched the Intellectual and Integrated Production System Consulting Business in collaboration with Yokogawa Electric Corporation to publicize these effective methods and enhance the competitiveness of Japan's manufacturing industries.

*Monozukuri: "design and manufacturing"

Achievements of the Plan

- Significant cost reductions across the Company
- Fewer workers required as a result of integration
- Reduction of operator loads to approximately one-seventh (compared with fiscal 2001)

Future Challenges

- Maintenance, entrenchment and enhancement of production innovation
- Promotion of production innovation at the new Ohtake facility
- Promotion of production innovation at the Harima assembly facility
- Promotion of production innovation at Polyplastics Co., Ltd.

Aspect 3: Global Development

During the period of the plan, Daicel responded to market and customer needs by rapidly advancing its operations on a global basis in those businesses that will aid in achieving sustained improvements in its competitive edge worldwide. In the airbag inflator business, we have a five-pronged global production system encompassing Japan, the United States, Thailand, Poland, and China. At the regional level, we established a centralized base for operations in China in 2004, and expanded and built new manufacturing and sales facilities for each of our cellulosic derivatives, plastics, and inflator businesses. During the period of the new medium-term plan, we will concentrate on reinforcing our business foundation through initiatives such as recruiting and training human resources at our overseas operations.

Achievements of the Plan

- Completion of a five-pronged global production system for airbag inflators
- Establishment of a centralized management company in China
- Establishment of polyacetal resin and inflator production facilities in China
- Production facilities for cellulose acetate and acetic acid anhydride under construction in China
- Establishment of chiral column business facilities in China and India

Future Challenges

- Reinforcement of global management

New Medium-Term Business Plan (FY2008 - FY2010)

Performance Targets for the New Medium-Term Business Plan

Daicel has set the following targets for its new medium-term business plan, taking into account achievements of the previous plan and issues that require ongoing attention.

1. Net sales of ¥450 billion, operating income of ¥55 billion, and ROA of more than 9%

2. Further selection and focus of operations
   – Reinforcement of core businesses through selection and focus, including consideration of M&A opportunities

3. Development and exploration of new businesses
   – Creation of a next-generation business pillar by developing both the content and scale of our product range for the electronic materials market
   – Exploration of promising themes for business beyond 2010

The Daicel Group will continue to focus on strengthening its business infrastructure to ensure sustainable growth beyond 2010. Measures include expansion and entrenchment of production and business process innovation activities, global reinforcement of group management, environmentally safe operations, and risk management and internal control measures.

Net Sales
450
Billion

Operating Income
55
Billion

ROA
9
%

Initiatives by Business Segment (FY2008-FY2010)

In the period of the new medium-term business plan we aim for further growth based on the two pillars of strengthening current core operations through further selection and focus and unearthing and developing new businesses.

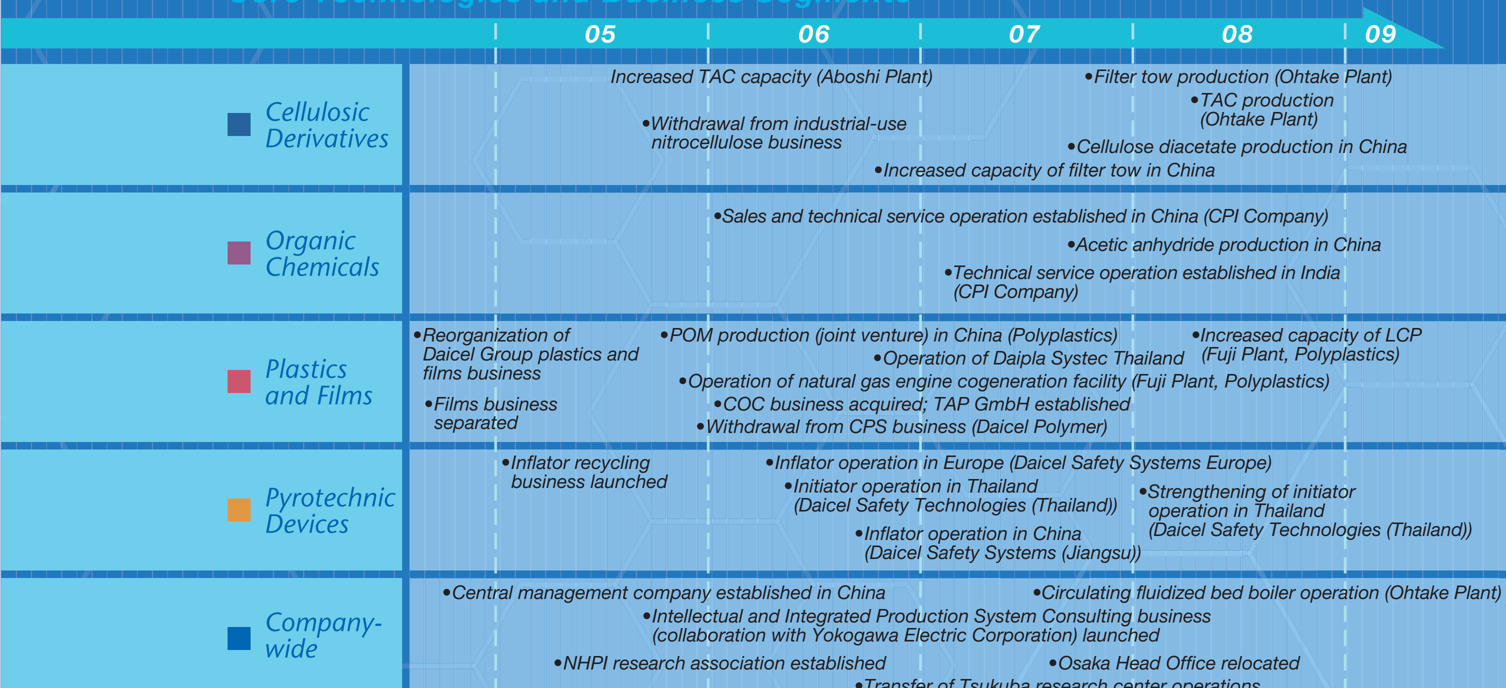
In the Cellulosic Derivatives segment we will continue our concentration on the key earnings driver businesses of TAC and filter tow. In the TAC business the most important issue is smoothly progressing planned capital expenditure. Following on from the Aboshi Plant, we are working to start production at a new facility at the Ohtake Plant in April 2008. Through this we will build a stronger production structure that enables us to meet the higher volumes demanded by key customers.

In the Organic Chemicals segment we are working to increase cost competitiveness and increase production of acetic acid derivatives to meet expanding demand in Asia. In the chiral pharmaceutical ingredients business we will further develop the foundation of our strength, centering on chromatographic separation of optical isomers.

In the Plastics and Films segment we are working to maintain and strengthen our position as the leading company in the Asia Pacific region for engineering plastics, at Polyplastics Group. In other resin compounds and processes businesses we will continue selection and focus with an eye on profitability.

In the Pyrotechnic Devices segment we will continue to strengthen the business foundation of car airbag inflators in each region on the five pronged global production system established as part of the previous medium-term business plan.

Core Technologies and Business Segments

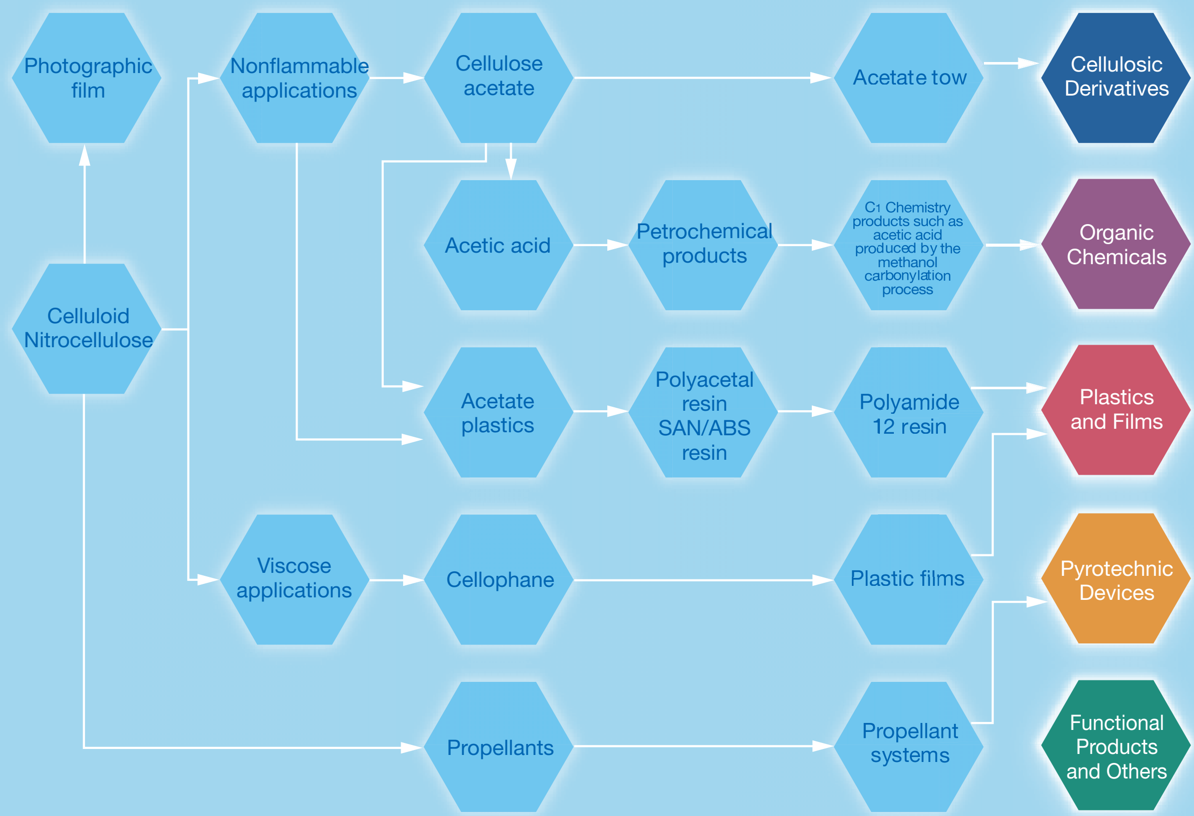


Profile

Daicel Chemical Industries Ltd. was founded in 1919 as Dainippon Celluloid Company Limited, created through the merger of eight celluloid producers. Deploying its original celluloid-related technological expertise, the Company has expanded into the fields of cellulose chemistry, organic synthesis chemistry, polymer chemistry, and pyrotechnic chemistry.

Today, Daicel's extensive business lineup includes cellulose acetates made from pulp and other natural fibers, cigarette filter tow, water-soluble polymers and other cellulosic derivatives, organic compounds (centering on acetic acid and acetic acid derivatives), organic fine chemical products, engineering plastics (such as polyacetal and polybutylene terephthalate resins), acrylonitrile styrene and acrylonitrile butadiene styrene resins, resin compounds derived from engineering plastic alloys, various plastic products, defense-related items (such as propellants and aircrew emergency-escape systems), and automobile airbag inflators.

Business Development Flowchart



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CAUTION WITH RESPECT TO FORWARD-LOOKING STATEMENTS

This annual report contains forward-looking statements about the future plans, strategies, beliefs and performance of the Daicel Group as a whole and its individual consolidated companies. These forward-looking statements are not historical facts. They are expectations, estimates, forecasts and projections based on information currently available to the Daicel Group and are subject to a number of risks, uncertainties and assumptions, which, without limitation, include economic trends, fluctuations in foreign currency exchange rates, fluctuations in the price of raw materials, competition in markets where the Company is active, personal consumption, market demand, the tax system and other legislation. As such, actual results may differ materially from those projected and the Daicel Group cannot guarantee that these forward-looking statements are accurate or will be achieved.

Message from the President

Daisuke Ogawa
President and CEO

Year in Review

In fiscal 2007, ended March 31, 2007, Japan's economy continued its mild recovery supported by strong capital investment, steady consumer spending, solid domestic demand, and healthy exports. In the chemical industry, however, despite firm demand for products overall, there was continued pressure on earnings stemming from high raw material and fuel prices.

Under these circumstances, the Daicel Group continued to adjust its selling prices and reduce costs. At the same time, we improved productivity through production and business process innovation activities, and proactively invested in growth businesses.

As a result, consolidated net sales rose 13.7%, to ¥381.4 billion, while operating income increased 8.4%, to ¥36.4 billion, and net income jumped 22.6%, to ¥17.4 billion. All of these figures were record highs for the second year in a row. Of particular note is the Group's operating income, an important performance indicator, which increased for the ninth consecutive year.

In the year under review, total assets reached ¥547.4 billion, up ¥64.0 billion year-on-year. Contributing factors included an increase in property, plant, and equipment owing to investment in a new cellulosic derivatives facility at the Ohtake Plant, as well as an increase in inventories aimed at addressing the rise in raw material and fuel prices.

Summary of the Previous Medium-Term Business Plan

Targets Met One Year ahead of Schedule, Higher Asset Efficiency

In the previous fiscal year, we achieved three key targets set for the year under review: net sales of ¥300 billion, operating income of ¥30 billion, and ROA (the ratio of recurring profit to total assets) of 6%. In fiscal 2007, we continued to build on those achievements.

The Company's engineering plastics business and the automobile airbag inflator business were the main drivers of this success. Moreover, during the period the cellulose acetate business evolved into a key growth driver business.

The sharp rise in demand for triacetyl cellulose (TAC), which is used in the manufacture of liquid crystal display films, transformed the business from one that generated stable cash flows through the utilization of existing facilities into a business with huge growth potential thanks to proactive capital investment. We attribute our growth in both businesses to our focus on two of Japan's strongest sectors – automobiles and flat-panel displays.

We also reduced costs and implemented a selection and focus strategy in line with our emphasis on profitability. As a result, the operating income margin rose from 7.5% in fiscal 2004 to 9.5% in fiscal 2007, and ROA rose from 4.0% to 6.7% over the same period.

Development of New Businesses Prioritized in New Medium-Term Business Plan

Unfortunately, there was one target of the business plan that we were unable to meet–"30% contribution to operating income by focus*1, entry-point*2, and new businesses." In the final year of the plan, however, this ratio reached only 20%.

Nevertheless, we achieved pleasing results in several areas. For example, the inflator business generated sales of around ¥40.0 billion, growing into one of Daicel's mainstay business pillars. Meanwhile, our corporate R&D initiatives led to the commercial production of semiconductor resist polymers, which were transferred to the Organic Chemical Products Company, aimed at the electronic materials market–another sign of promising times ahead. However, we were not satisfied with our progress in developing next-generation growth businesses.

In order to sustain growth beyond 2010, Daicel has made the development and exploration of new businesses the most important challenge of its new medium-term business plan.

*1 Focus business: Business for which high market growth is expected. Examples include intermediate pharmaceuticals and inflators for automobile air bags.

*2 Entry-point business: Business that leverages Daicel's business and technological strengths to develop markets in which growth is expected, and functions as an entry point into focus business areas. As example is organic fine chemicals.

New Medium-Term Business Plan

In April 2007, Daicel embarked on its new medium-term business plan, covering the three-year period to March 2010. Accordingly, we have now entered the final phase of

Financial Highlights

Daicel Chemical Industries, Ltd. and Consolidated Subsidiaries

Years ended March 31	Millions of yen			Thousands of U.S. dollars*2
	2007	2006	2005	2007
Net sales	¥ 381,423	¥ 335,520	¥ 306,335	$ 3,232,398
Operating income	36,399	33,570	28,553	308,466
Income before income taxes and minority interests	33,185	29,386	22,380	281,229
Net income	17,438	14,221	10,844	147,780
Total assets	547,432	483,469	413,493	4,639,254
Total equity*1	242,409	197,780	171,225	2,054,313

Amounts per common share: *3	Yen			U.S. dollars*2
Net income	¥ 48.19	¥ 39.16	¥ 29.82	$ 0.41
Cash dividends applicable to the year	8.00	8.00	8.00	0.07

* 1. From FY2007, Shareholders' Equity is being shown as Total Equity.
* 2. The U.S. dollar amounts in this report are translated from Japanese yen, for convenience only, at the rate of ¥118=$1, the approximate exchange rate at March 31, 2007.
* 3. The computations of net income per share of common stock are based on the weighted average number of shares outstanding.

our second long-term business plan, a 10-year program that was formulated in 1999. The next three years will be an extremely vital time for bolstering the Company's foundation for growth beyond 2010.

Daicel has formulated the following targets for the new plan, taking into account the achievements of the plan just ended and issues for 2010 and thereafter.

(1) Targets of ¥450 billion for consolidated net sales, ¥55 billion for operating income, and 9% or more for ROA

We will seek to raise asset efficiency even higher, targeting ROA of 10% (as stated in the Second Long-Term Business Plan). To this end, we will dispose of redundant assets including unnecessary securities, constrict total assets, and work together as a Group to reduce our working capital requirements.

(2) Further business selection and focus

We will reinforce core businesses through selection and focus, with due consideration to M&A opportunities.

(3) Explore and nurture new businesses

We will nurture our businesses related to functional chemicals, materials, and components for the electronic materials market into a next-generation pillar. We will also explore promising business themes with a view to 2010 and beyond.

An additional target of the current medium-term business plan in addition to the three mentioned above is the reinforcement of Daicel's business infrastructure.

The period of the previous medium-term business plan, when we expanded overseas and businesses grew sharply, was a huge turning point for the Group as it positioned itself for a significant leap forward. In addition to establishing a global five-basis production and sales structure for the automobile air bag inflator business, we launched a polyacetal business in Nantong, China, set up chiral operations in China and India, built a cellulose acetate business in China, and established Daicel Chemical (China) Investment Co., Ltd. With respect to the development of human resources however, we were unable to keep pace with these advances in many areas.

Daicel plans to further bolster the business infrastructure of the entire Group, including overseas affiliates. Our aim is to ensure sustainable growth and progress beyond 2010 and transform ourselves into a top-quality corporate group. To this end, we will focus on the following activities.

(A) Production and Business Process Innovation

We will maintain, entrench and enhance production innovation while reducing the number of workers required at the Arai and Ohtake Plants. We will also introduce production innovation to the new facility within the Ohtake Plant and implement similar measures at the Harima Plant, an assembly facility. In addition, we will also introduce production innovation at Group company Polyplastics Co., Ltd.

(B) Reinforcement of Global Group Management

We will increase support for Group management by forming a global corporate team centering on the Corporate Department. We will also ensure that the Daicel Group Conduct Policy, formulated in July 2006, penetrates every corner of the Group. In addition, we will boost corporate social responsibility (CSR) activities, starting with each company's formulation of their own code of conduct and Groupwide observance of corporate ethics.

(C) Environmental Management and Responsible Care

As measures to prevent global warming, we have reduced greenhouse gas emissions by switching from the use of conventional heavy oil to natural gas at the Aboshi and Arai Plants, and introduced a natural gas engine cogeneration system at Polyplastics Co., Ltd. We are also operating a circulating fluidized bed boiler that uses recycled tires as fuel at the Ohtake Plant.

(D) Risk Management and Internal Control

It has become more important than ever to make decisions based on careful assessment of risks overseas when proceeding with global business expansion.

The Company is building and strengthening a truly effective internal control system in accordance with the basic guidelines for creating such a system, approved by the

Board of Directors in May 2006. Measures include establishing a Groupwide risk management system, centering on the Risk Management Committee, and setting up an internal control system to ensure the reliability of financial reporting.

Through these activities, the Daicel Group intends to establish a business infrastructure for sustained growth through 2010 and beyond.

Outlook

For fiscal 2008, Daicel is forecasting consolidated net sales of ¥415.0 billion and operating income of ¥36.5 billion, marking the tenth consecutive period of increased operating income.

These forecasts are based on estimates of increased sales volumes underpinned by firm demand for cellulose acetate used in LCD films, as well as for engineering plastics and automobile airbag inflators. We believe that adjustments to selling prices to reflect surging raw material and fuel prices, together with cost-reduction efforts through production and business process innovation, will help us attain these targets.

The above forecasts have been calculated taking into account an anticipated ¥3.0 billion increase in depreciation expenses stemming from changes to the depreciation system.

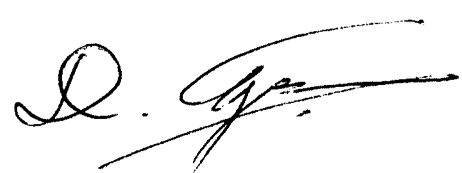
In Conclusion

Basic Policy on Profit Distribution and Dividends for the Period

Daicel's basic policy on the distribution of profits emphasizes a comprehensive and long-term balance between consistent and appropriate dividends to shareholders and reinforcing internal reserves to further solidify the Company's revenue base. To this end, we take account of earnings in each fiscal year and business development prospects viewed from a general and long-term perspective.

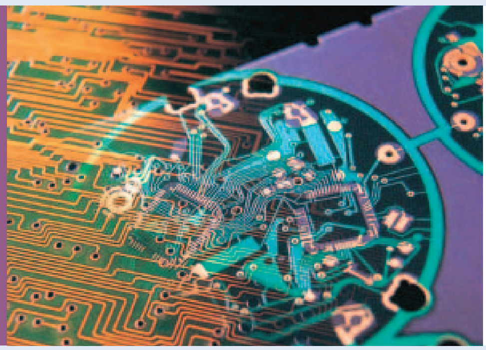
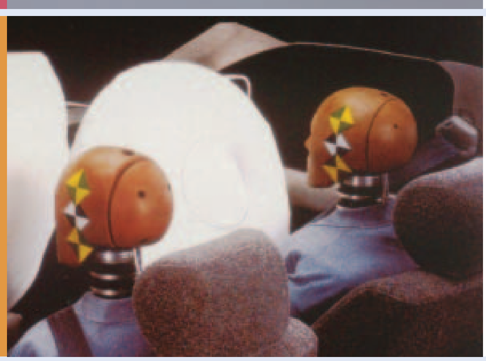
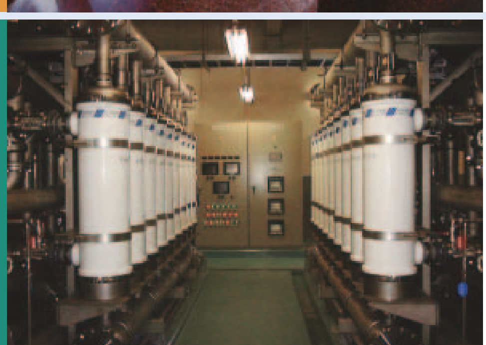
Recognizing that the Company has entered a new growth stage, we are planning and implementing active capital investments to enhance corporate value over the medium to long term. Because we reinforced the Company's internal reserves to fund this high level of capital investment, we held annual dividends at ¥8.00 per share, unchanged from the previous year.

By achieving the targets of our new medium-term business plan and delivering sustained growth, we will meet the expectations of all shareholders and other investors. I look forward to your continued understanding and support.



Daisuke Ogawa
President and CEO

At a Glance

Business Segment		Sales	Operating Income
Cellulosic Derivatives		16.6%	26.0%
Organic Chemicals		24.6%	25.3%
Plastic and Films		42.4%	33.1%
Pyrotechic Devices		14.6%	13.5%
Functional Products and Others		1.8%	2.1%

Major Products	Uses	Market Position
Cellulose acetate	LCD films, acetate fibers, photographic films, plastics	• Overwhelming market share in the manufacture and sale of triacetyl cellulose (TAC) used in film for LCDs. • Stable supplier of acetate tow for cigarette filters to a number of leading cigarette manufacturers.
Acetate tow	Cigarette filters	
Carboxymethyl cellulose (CMC) and other water-soluble polymers (WSP)	Foods, pharmaceuticals, cosmetics, adhesives, textiles, mud stabilizers, thickeners	
Acetate plastics	Frames for glasses, other products	
Celluloid		
Acetic acid	Cellulose acetate, vinyl acetate	• Acetic acid is a mainstay product, and Daicel is a leading manufacturer of this product in Asia. • Sales of peracetic acid to expand due to withdrawal of a competitor. • World's largest manufacturer of chiral columns used for the separation of optical isomers.
	Auxiliary dyeing agents, pharmaceuticals	
	Agricultural chemicals, pure terephthalic acid (PTA)	
Solvents		
Chiral HPLC columns	Separation of optical isomers	
Other organic and inorganic industrial-use chemicals		
Polyacetal resin	Electric and electronic appliance parts, automobile parts Communications appliance parts, household goods, sundry goods	• Polyplastics holds the top share in Asia for POM, PBT, and LCP, and ranks second for PPS.
Polybutylene terephthalate (PBT) resin		
SAN/ABS resins and alloys		
Polystyrene sheets and plastic products		
Moisture-proof packaging films	Packaging for foods, drugs, textiles	
Inflators	Automobile air bag systems	• Market share for car airbag inflators has increased annually, and today Daicel is the top manufacturer of inflators in Japan and third globally.
Aircrew emergency-escape systems	Fighters, trainers, helicopters	
Rocket motors	Missiles	
Propellants		
Sepatation membrane modules	Water treatment	

Cellulosic Derivatives

Operations

	Millions of yen				
	2007	2006	2005	2004	2003
Sales to outside customers	¥ 63,501	¥55,899	¥50,132	¥48,180	¥49,136
Intersegment sales	2,355	2,222	1,942	1,785	1,900
Total sales	65,856	58,121	52,074	49,965	51,036
Total cost and expenses	54,226	47,290	42,409	39,139	39,275
Operating income	¥ 11,630	¥10,831	¥ 9,665	¥10,826	¥11,761
Total assets	¥118,803	¥86,828	¥57,894	¥55,103	¥55,087
Depreciation	4,549	4,131	4,127	4,254	4,245
Capital investments	32,267	30,154	4,398	4,440	2,247

Overview

The Cellulosic Derivatives segment produces a wide range of cellulosic derivatives that draw on the manufacturing technologies of the celluloid business on which Daicel was founded. Today, our lineup includes cellulose acetate, which accounts for the largest sales in the segment and whose many applications include liquid crystal display (LCD) and photographic films, cigarette filters, and acetate fibers.

Daicel's strengths lie in its overwhelming market share in the manufacture and sale of triacetyl cellulose (TAC) used in film for LCDs, as well as in the production of acetic acid, cellulose acetate, and acetate tow.

The Company also makes water-soluble polymers (WSP); carboxymethyl cellulose (CMC) for use in the civil engineering, oil drilling, and fish feed; and hydroxyethyl cellulose (HEC) for use in paint products, polymerization, and cosmetics.

Performance

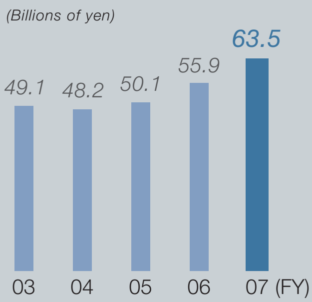
In fiscal 2007, sales to outside customers amounted to ¥63.5 billion, up 13.6% compared with the previous year. Operating income rose 7.4%, to ¥11.6 billion.

Sales of cellulose acetate increased owing to stronger demand for its use in LCD film applications, as well as our revision of sales prices to reflect rises in the prices of raw materials and fuel.

Despite a gradual decline in demand for cigarettes in Japan, we reported an increase in sales of acetate tow for cigarette filters. Strong exports to the overseas production bases of leading cigarette makers, as well as sales price revisions and exchange rate fluctuations, contributed to overall sales growth.

Sales of WSP also rose on the back of higher sales in Japan for use in medical and cosmetic applications and stronger overseas demand for use in oil drilling and electronic materials applications.

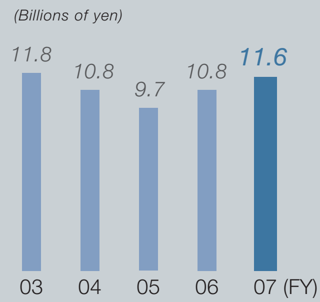
Sales to Outside Customers



Main Reasons for Increased Sales:

- Acetate tow cellulose (+¥5.4 billion): Increase in sales for use in film for LCDs
- Acetate tow for cigarette filters (+¥2.1 billion): Increase in exports

Operating Income



Main Reason for Increase in Operating Income:

- Higher sales of cellulose acetate for LCD applications

Strategies for Future Growth

Triacetyl Cellulose (TAC)

Demand for LCDs continues to increase as screen sizes become larger and sales volumes grow. Accordingly, sales of TAC, which is used in the manufacture of film for LCDs, have been very strong, helping drive the Company's growth during the period covered by its new medium-term business plan. We are establishing a new TAC manufacturing facility at the Ohtake Plant to meet the requirements of a major customer planning to increase production. The facility is scheduled to commence operations in April 2008.

Acetate tow for Cigarette Filters

Worldwide demand for acetate tow used in cigarette filters has been increasing at a rate of between 1 and 2% a year. This is primarily attributable to a trend toward longer filters resulting from increased consumption of low-tar cigarettes on health grounds.

Daicel is a medium-to-long term supplier to a number of leading cigarette manufacturers, including the JT Group, BAT, and Philip Morris. To boost market share and strengthen relationships with our customers, we are engaged in supply chain management and joint research and development with our major customers and raw materials suppliers. Meanwhile, the Sakai Plant will be relocated due to construction of an expressway. We are using this opportunity to upgrade acetate tow production capacity at the Ohtake Plant. The expanded facility is scheduled to come on-stream in October 2007.

Organic Chemicals

Operations

	Millions of yen				
	2007	2006	2005	2004	2003
Sales to outside customers	¥ 93,839	¥84,435	¥79,087	¥74,916	¥72,170
Intersegment sales	14,126	10,989	11,083	9,816	8,236
Total sales	107,965	95,424	90,170	84,732	80,406
Total cost and expenses	96,641	85,947	83,310	79,930	73,692
Operating income	¥ 11,324	¥ 9,477	¥ 6,860	¥ 4,802	¥ 6,714
Total assets	¥ 93,690	¥82,909	¥82,321	¥84,530	¥86,161
Depreciation	5,881	6,426	7,062	7,861	8,014
Impairment loss on fixed assets	—	895	—	—	—
Capital investments	5,499	5,461	5,209	4,585	5,593

Overview

The Organic Chemicals segment consists of three main business categories: (1) organic chemical products, primarily acetic acid and its derivates, (2) organic-designed products, primarily peracetic acid derivatives, and (3) chiral pharmaceutical ingredients, such as chiral chemicals and pharmaceutical intermediates.

Acetic acid is one of Daicel's mainstay products, and the Company is a leading manufacturer of this product in Asia. The withdrawal of other company from the peracetic acid business has presented an opportunity for Daicel to expand the business. We are also the world's largest manufacturer of chiral columns used for the separation of optical isomers.

Performance

In fiscal 2007, sales to outside customers in this segment totaled ¥93.8 billion, up 11.1% over the previous year*. Operating income climbed 19.5%, to ¥11.3 billion.

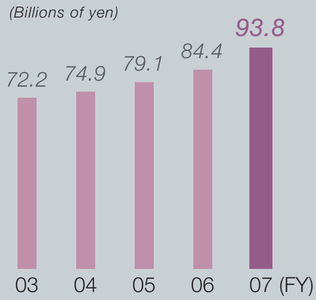
Sales of acetic acid, a core Daicel product, rose on the back of firm demand and higher sales prices attributable to soaring prices for methanol, the main raw material of acetic acid. We also generated increased sales of general-use products such as acetic acid derivatives and solvents. Here, too, revenue was boosted by strong domestic demand coupled with sales price increases brought about by higher raw material prices.

Fine chemical product sales increased owing to our focus on high-performance chemicals for electronics materials, as well as higher sales prices.

Sales of pharmaceutical intermediates grew thanks to strong sales of some products. We also reported higher sales in the chiral chromatograhic business. This was due to strong demand for chiral chromatograhic columns and bulk chiral stationary phases used for drug development purposes, and an increase in sales prices.

* From the year under review, some functional products from the Functional Products and Others segment have been reclassified to the Organic Chemicals segment.

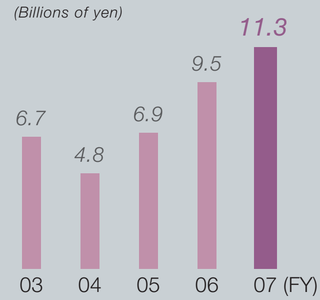
Sales to Outside Customers



Main Reasons for Increased Sales:

- Acetic acid (+¥3.8 billion): Increase in production volume owing to strong demand
- General-use products such as acetic acid derivatives, organic-designed products (+¥4.6 billion): Increases in both sales prices and volumes; Reclassification of semiconductor resist materials to this segment
- Chiral pharmaceutical ingredients business (+¥1.0 billion): Strong sales in the chiral chromatography business.

Operating Income



Main Reason for Increase in Operating Income:

- Improved profitability accompanying higher sales volume

Strategies for Future Growth

Acetic Acid and Acetic Acid Derivatives

We constantly examine the viability of expanding production of acetic acid, including at overseas locations, although at present we do not have specific plans in this area. We also make ongoing improvements to the production technology side of this core product, and succeeded in increasing production and reducing costs under our previous medium-term business plan.

With the construction of a new production facility at Ningbo Da-An Chemical Industries Co., Ltd., in China, we have increased output of acetic anhydride by 30,000 tons annually. We have also raised production capacity of ethylamine and acetate esters at the Ohtake Plant. With respect to ethylamine, we will take advantage of liberalization in the industrial alcohol market to switch to bioethanol as a raw material.

Organic-Designed Products

The withdrawal of other companies from the peracetic acid derivatives business has resulted in a tight supply-and-demand situation for lactone and epoxy-based products. Daicel intends to increase earnings by setting appropriate prices for its offerings and concentrating on high-value-added products used in electronic materials.

We will continue developing and supplying organic-designed products for the high-growth electronic materials market with the aim of making our lineup of offerings a future mainstay of the Company's business.

Chiral Pharmaceutical Ingredients

In response to advances in the worldwide development of chiral pharmaceuticals, we are reinforcing and expanding our activities in this area by taking full advantage of the Group's strengths in the chromatographic separation of optical isomers.

In early 2006, we set up sales operations for chiral columns in China and are currently establishing a technical service center and research center in Shanghai. We also opened a technical service center in Hyderabad, India, in February 2007. We now have five centers spread around the world —— Japan, United States, France, China, and India.

In Japan, we are increasing production capacity at the Arai Plant by re-locating a processing room and constructing a new manufacturing facility for stationary phases compatible with all solvents.

Plastics and Films

Operations

	Millions of yen				
	2007	2006	2005	2004	2003
Sales to outside customers	¥161,881	¥142,556	¥133,390	¥119,299	¥114,877
Intersegment sales	29	37	49	46	51
Total sales	161,910	142,593	133,439	119,345	114,928
Total cost and expenses	147,135	129,421	120,430	111,796	108,872
Operating income	¥ 14,775	¥ 13,172	¥ 13,009	¥ 7,549	¥ 6,056
Total assets	¥159,234	¥149,738	¥135,949	¥128,172	¥137,186
Depreciation	7,473	6,887	6,770	7,491	8,133
Impairment loss on fixed assets	66	15	—	—	—
Capital investments	4,677	6,960	10,583	5,615	5,576

Overview

This segment consists of several businesses, notably engineering plastics, including polyacetal (POM), polybutylene terephthalate (PBT), polyphenylene sulfide (PPS), and liquid crystal polymers (LCP); and the plastic compound business, centering on acrylonitrile styrene (AS) and acrylonitrile butadiene styrene (ABS). This segment also encompasses the Company's sheet business, molded vessels and shock-absorbing materials business, film business, and other plastic products business.

Polyplastics Co., Ltd., a Daicel subsidiary, is responsible for the engineering plastics business. As a leading manufacturer and marketer of engineering plastics, it holds the top share in Asia for POM, PBT, and LCP, and ranks in second place for PPS. Polyplastics supplies products for a wide range of applications, including those used in precision machinery, construction materials, and household consumer appliances, to the electronics and automobile industries, mainly in the Asia-Pacific region.

Daicel Polymer Ltd., also a subsidiary, manufactures and markets plastic compounds and polystyrene sheets. It meets increasingly sophisticated user needs and the needs of users expanding globally by focusing on supplying high performance products such as engineering plastic alloys and through its close-knit network of operations in Japan, Hong Kong, Shanghai, and Singapore.

Also, in January 2006, we acquired the cyclic olefin copolymer (COC) operations of Ticona Limited Liability Company, with the aim of developing new markets, primarily in the optical components sector.

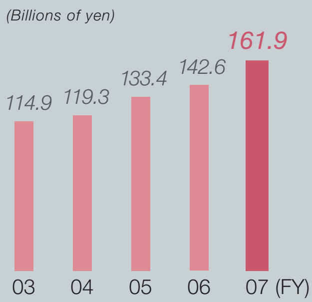
Performance

In fiscal 2007, sales to outside customers amounted to ¥161.9 billion, up 13.6% over the previous year. Operating income increased 12.2%, to ¥14.8 billion.

Sales of engineering plastics, such as polyacetal and PBT, increased thanks to strong demand from the Japanese automobile sector and electronic device markets in Japan and overseas.

The plastic compound business, centering on AS and ABS and engineering plastic alloys, also performed strongly owing to growth in sales of both general-use resins and high-performance engineering plastic alloys. Sales also benefited from the inclusion of long fiber reinforced thermoplastics in this segment from the year under review.

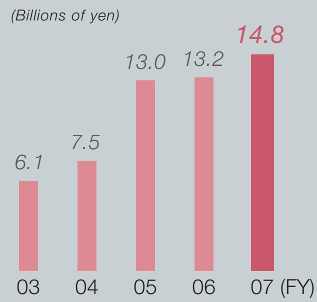
Sales to Outside Customers



Main Reasons for Increased Sales:

- Polyplastics (+¥14.5 billion): Increased sales of main products (POM, PBT, LCP, and PPS); substantial increase in POM sales due to full-scale operations at PTM Engineering Plastics (Nantong) Co., Ltd. (China)
- Recent inclusion of Topas Advanced Polymers: +¥1.7 billion
- Plastic compound business: +¥3.8 billion

Operating Income



Main Reason for Increase in Operating Income:

- Polyplastics : +¥0.8 billion
- Plastic compound business, etc: +¥0.9 billion

In the sheet business, we withdrew from some unprofitable product operations. However, we strove to expand sales and raise sales prices to reflect growing raw material costs, leading to an increase in category sales.

Harsh market conditions continued in the molded vessels and shock-absorbing materials business. In the year under review, sales in this business declined despite increased sales of high-value-added products and revisions to sales prices.

Sales in the film business remained mostly unchanged, despite efforts for higher sales of barrier films, a core product, and for expansion of our new coatings business.

In the other plastic products business, sales declined due to a fall in demand for some products in the construction materials sector, despite increased sales of pressure-resistant polyethylene pipes for the civil engineering sector.

Strategies for Future Growth

Amid growing demand for engineering plastics in the Asia-Pacific region, Polyplastics continues to implement measures aimed at strengthening its position as a leader in this field. In the plastic compound and other plastic products business, meanwhile, we have adopted an earnings-oriented strategy centering on specialization and the development of value-added products. In the COC business, Daicel, Polyplastics and our partners in Germany and the United States will continue working closely to open up new markets, especially in the optical components sector.

Polyacetal (POM)

Polyplastics is the world's leading manufacturer of polyacetal, one of its mainstay products. We make this product at the Fuji Plant in Japan and at facilities in Taiwan, Malaysia, and China, for an annual production capacity of 200,000 tons. In China, in addition to existing markets among Japanese, American, European manufacturers with local Chinese operations, we will develop new markets among Chinese manufacturers of automobiles and electrical and electronic products with the aid of a technical service center to be operated in Shanghai by the end of 2007.

Liquid Crystal Polymers (LCP)

To meet demand from the strong electronic device market, we will increase annual production capacity of liquid crystal polymers at the Fuji Plant by 3,000 tons, for a total of 8,200 tons, by April 2008. Over the next several years, we envisage further increases in capacity, to more than 10,000 tons.

Pyrotechnic Devices

Operations

	Millions of yen				
	2007	2006	2005	2004	2003
Sales to outside customers	¥55,496	¥44,090	¥36,605	¥32,541	¥28,409
Total sales	55,496	44,090	36,605	32,541	28,409
Total cost and expenses	49,449	37,473	30,063	26,573	24,126
Operating income	6,047	6,617	6,542	5,968	4,283
Total assets	¥59,965	¥52,786	¥39,730	¥32,418	¥28,891
Depreciation	¥ 4,393	¥ 3,434	¥ 3,069	¥ 3,000	¥ 3,056
Capital investments	4,227	12,678	4,449	5,559	1,723

Overview

This segment consists of two main businesses: the motor vehicle safety devices business, which handles inflators (gas generating devices) for automobile airbags; and the aerospace & defense business, made up mainly of aircrew emergency escape systems, gun propellants, and rocket motors.

Airbag systems are constantly changing as a result of technical advances. Daicel has earned high praise for its automobile airbag inflators, which are the most important component of these systems. Our market share has increased annually, and today we are the top manufacturer of inflators in Japan and rank number three in the world.

In the aerospace & defense business, we manufacture various kinds of gun propellants made from nitrocellulose, a raw material of celluloid, as well as composite propellants and rocket motors for missile applications. We also make pilot emergency-escape systems that use the power of propellants to safely eject pilots.

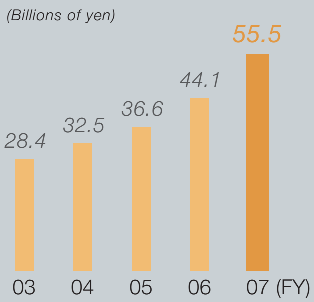
Performance

In fiscal 2007, sales to outside customers climbed 25.9%, to ¥55.5 billion. Operating income was down 8.6%, to ¥6.0 billion.

Sales of automobile airbag inflators grew substantially in Japan thanks to higher demand for side impact inflators and new design driver and passenger inflators accompanying an increase in vehicle production. Healthy sales in overseas markets also helped boost sales.

In the aerospace & defense business, sales increased thanks to a rise in the number of aircrew emergency-escape systems bought by Japan's Ministry of Defense. This was despite a fall in the volume of gun propellants and missile components procured by the Ministry of Defense.

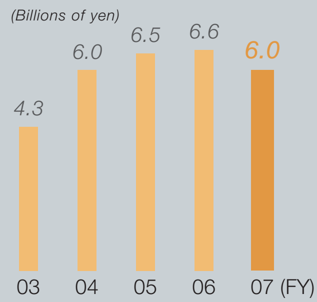
Sales to Outside Customers



Main Reasons for Increased Sales:

- Motor vehicle safety devices business: Increase in inflator sales volume (from 22.7 million to 33.1 million units)
- Aerospace & defence business: Growth in procurement of emergency escape systems

Operating Income



Main Reason for Decrease in Operating Income:

- Higher fixed costs in the motor vehicle safety devices business accompanying construction of overseas facilities; higher operating costs due to reinforcement of business infrastructure

Strategies for Future Growth

Automobile Airbag Inflators

Daicel's automobile airbag inflator business has grown steadily and now represents a new mainstay operation for the Company. This growth is attributable to an increase in the number of airbags fitted per vehicle as side impact and curtain airbags become standard features alongside driver and passenger airbags.

The Company's global production strategy calls for increasing the number of facilities to cover the main automobile manufacturing regions around the world. We commenced operations at our facility in Poland in spring 2006 and a new facility in China in the autumn of the same year. Added to our manufacturing bases in Japan, the United States, and Thailand, Daicel has completed a five pronged global production system for automobile airbag inflators. We are also working to strengthen cost competitiveness by increasing the ratio of major components, such as gas generating agents and initiators, manufactured in-house by overseas subsidiaries.

Utilizing our global production system, we will continue to maintain our position as the world's top supplier of airbag inflators to Japanese automobile manufacturers. We will also continue our proactive sales activities targeting South Korean automobile manufacturers, a market that is expected to grow.

By fiscal 2010, the final year of our medium-term business plan, we are targeting an annual sales volume of 58 million units (approximately 50% in overseas sales) and a 19% share of the world inflator market.

Aerospace & Defense Business

The market for aerospace & defense products continues to face a challenging operating environment stemming from cutbacks in Japan's defense budget. Nonetheless, we are pursuing a number of initiatives to achieve growth. We will respond to changes in the duties, structure, systems and equipment of Japan's Self-Defense Forces necessitated by today's world of peacekeeping activities, guerilla and terrorist countermeasures, and the tense situation involving North Korea. To this end, we will develop new products by applying our key strengths in pyrotechnics and assembly, and add new levels of value by expanding existing product areas into broader integrated systems.

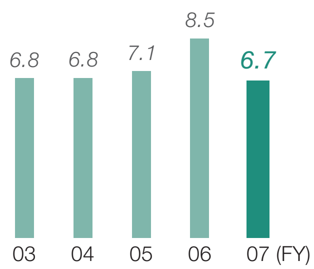
Functional Products and Others

Operations

	Millions of yen				
	2007	2006	2005	2004	2003
Sales to outside customers	¥ 6,706	¥ 8,540	¥ 7,121	¥ 6,804	¥ 6,750
Intersegment sales	11,876	10,267	10,082	9,293	8,671
Total sales	18,582	18,807	17,203	16,097	15,421
Total cost and expenses	17,657	17,490	16,723	15,831	15,337
Operating income	¥ 925	¥ 1,317	¥ 480	¥ 265	¥ 84
Total assets	¥ 9,704	¥10,908	¥10,323	¥ 8,372	¥ 4,902
Depreciation	327	290	348	406	426
Capital investments	224	340	190	392	213

Sales to Outside Customers

(Billions of yen)



Operating Income

(Billions of yen)

Performance

In fiscal 2007, sales in this segment amounted to ¥6.7 billion, down 21.5% over the previous year. Operating income fell 29.8%, to ¥925 million.

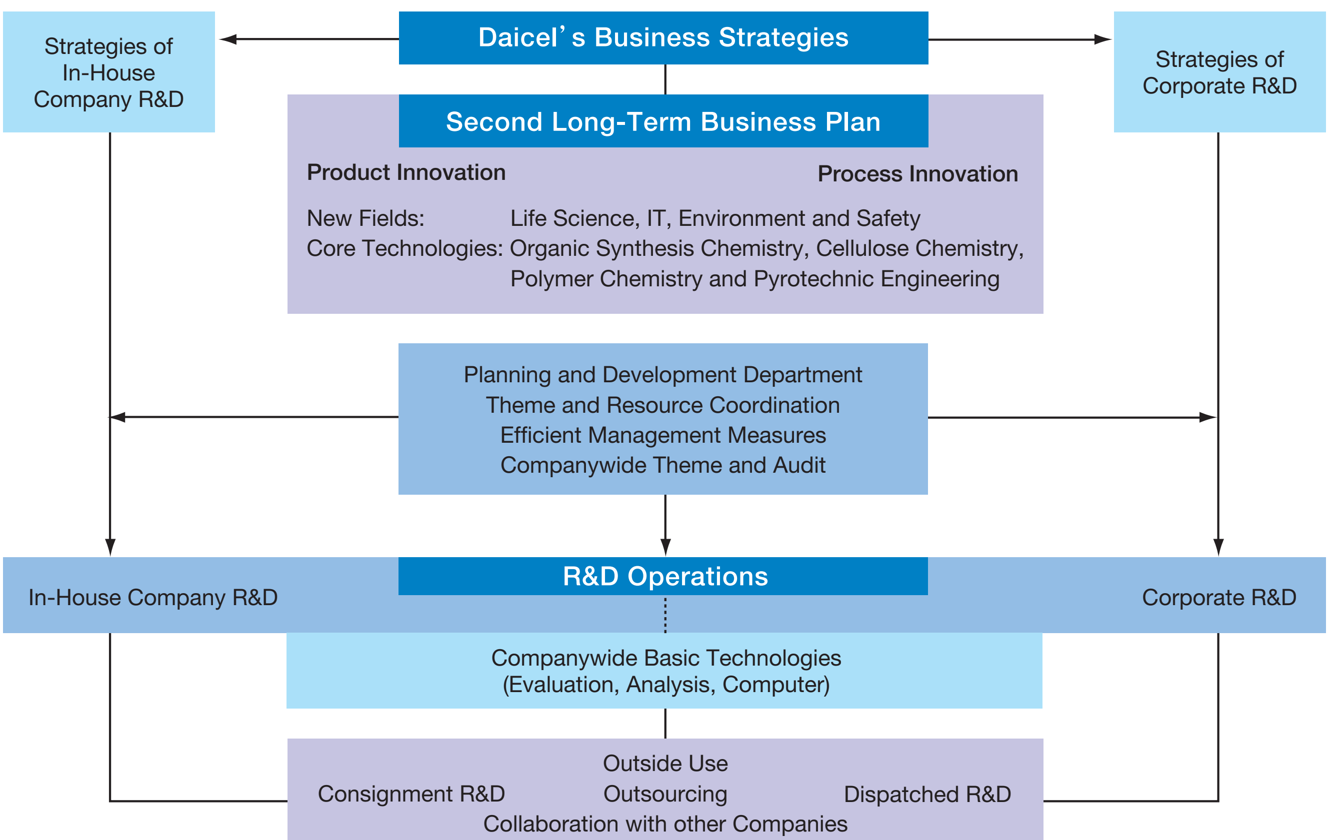
In the membrane systems business, which includes separation membrane modules and other products for water treatment, we posted increased sales to the medical sector and wastewater disposal sector. However, total sales declined due to a considerable decline in sales to water purification plants stemming from a downturn in public sector demand.

Also, sales of new functional materials decreased due to the reclassification of some functional products to the Organic Chemicals business segment from the year under review.

Importance of R&D in Group Operations

Given Japan's lack of natural resources, to achieve continued profitable growth chemical manufacturers must demonstrate their ability to seamlessly introduce creative, highly distinctive products, embodying proprietary technologies, into the market. The Daicel Group recognizes that research and development is a key factor in this ability. For this reason, we consider R&D to be one of our most important management priorities. Based on the core technologies it has amassed over the years in organic synthesis chemistry, cellulose chemistry, polymer chemistry, and pyrotechnic engineering, Daicel aims to create new levels of value for customers. Specifically, we seek to establish pioneering, world-first technologies; develop high-value-added, high-performance products; and focus on R&D connected to new business creation. By also developing technologies that lead to significant cost reductions, moreover, we will target R&D initiatives that contribute to enhanced profitability.

The Position of R&D



R&D Structure and Policies

Features of R&D under our In-House Company System

The Daicel Group's R&D system is based on two streams of R&D activities – those conducted by each in-house companies, and corporate R&D initiatives conducted by the Corporate Department. All entities involved have clear definitions of their respective responsibilities and functions. In-house companies are charged with developing their existing business domains and related R&D activities. Corporate R&D, meanwhile, focuses on the three following areas.

(1) Creation of new businesses: This includes R&D related to creating businesses in new domains outside the scope of current operations.

(2) Support for existing businesses: This includes research themes in the initial stage, themes in which in-house companies have no track record (thus making it more efficient to consign them to corporate R&D), and cases in which development by corporate R&D is deemed most appropriate, even if research is related to existing or peripheral businesses.

(3) Development and support of companywide basic technologies.

Overview of R&D Structure

In principle, the planning and development departments of each in-house company are responsible for in-house company R&D, while corporate R&D is undertaken by R&D Management. The Company has also established the Analysis Service Center to provide support for companywide R&D activities. The Center undertakes analysis and evaluation of properties and safety, as well as computer-based chemistry and environmental technology services.

In the fiscal year under review, consolidated R&D expenses amounted to ¥11.7 billion, the equivalent of 3.1% of net sales. Details of the objectives, main themes, and expenses for R&D undertaken by each of the business segments during the year under review are the following.

(1) Cellulosic Derivatives

Conducted mainly by Daicel Chemical Industries, activities by this segment included raising production capacity and quality of acetate cellulose, as well as strengthening production technologies and raising quality related to filter tow. R&D expenses in this business totaled ¥915 million.

(2) Organic Chemicals

R&D activities in this business are spearheaded by Daicel Chemical Industries. Initiatives during the year included research into improving acetic acid manufacturing technologies, development of new organic derivatives, development and commercialization of functional polymers, examination of industrialization for new pharmaceutical intermediates, development of columns for the separation of optical isomers, and development of separation processes for such columns. R&D expenses in this segment amounted to ¥2,590 million.

(3) Plastics and Films

Conducted mainly by Polyplastics Co., Ltd. and Daicel Polymer Ltd., activities in this segment included developing high-performance resins and polymer alloys, developing styrene products, enhancing the quality of engineering plastics, and developing production technologies for new films. This segment's R&D expenses totaled ¥3,541 million.

(4) Pyrotechnic Devices

R&D activities in this segment, conducted mainly by Daicel Chemical Industries, included research into the development of new gas generating agents and new inflators for car airbags. Segment R&D expenses totaled ¥1,699 million in the year under review.

(5) Functional Products and Others

During the year, Daicen Membrane-Systems Ltd. undertook development work on membrane separation systems, while Daicel Chemical Industries conducted research into digital image printing media. Total R&D expenses for other businesses amounted to ¥232 million.

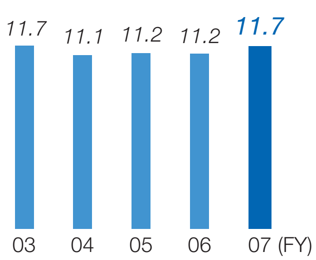
(6) Companywide R&D

Daicel Chemical Industries conducts research into new business creation and basic themes that cannot be allocated to individual businesses. During the year under review, these R&D expenses amounted to ¥2,738 million.

Daicel has been focusing on research into the development of N-hydroxyphthalimide (NHPI) catalyst air-oxidation technology in partnership with Professor Yasutaka Ishii of the Department of Chemistry, Faculty of Engineering, Kansai University. We are engaged in ongoing research as part of the Research Association for Ishii Oxidation Technology project. This project, sponsored by the Ministry of Economy, Trade and Industry, is aimed at developing environmentally friendly chemical processing technologies.

Research and Development Expenses

(Billions of yen)



NHPI Technology

NHPI catalyst air-oxidation technology enables revolutionary oxygen oxidation reactions that have four important advantages: (1) enable oxidation reactions at significantly lower temperatures and pressures than existing manufacturing methods, (2) reduce by-products, (3) lower energy costs during the manufacturing process, and (4) cut down greenhouse gas emissions.

Daicel has been advancing studies into commercial applications of NHPI technology in partnership with its discoverer, Professor Yasutaka Ishii of Kansai University. As a result, we have succeeded in the commercial production of resist polymers for argon fluoride (ArF) excimer lasers. As a member of the Research Association for Ishii Oxidation Technology, launched in 2005, we are conducting research into the commercial production of adipic acid and other bulk chemicals made using this new catalyst air-oxidation technology.

Production Innovation

Aboshi Plant Now a Next-Generation Chemical Plant

Since the 1990s, Daicel has undertaken production innovation activities with the aim of reinventing the concept of "monozukuri" (product manufacture), to take it beyond individual ideas for improvements. The Aboshi Plant, where these production innovation activities began, has evolved into a "next-generation chemical plant," where innovations to people and organization, production systems, and information systems have optimized all aspects of the facility's operations. We have achieved amazing results in making production more efficient. For example, we have raised production by reducing problems with equipment and facilities while generalizing operations. We have also reported a three-fold increase in productivity by requiring fewer workers, as well as significant reductions in both supervision requirements and energy loss, of which the latter has led to enhanced environmental protection.

During the period of the previous medium-term plan, we applied the experience and expertise acquired at the Aboshi Plant to enhance the operations of other plants, resulting in considerable cost reductions.

Over the three-year period of the new medium-term plan, which commenced in April 2007, we will endeavor to continue and enhance these production innovation activities. At the same time, we plan to introduce them at a new facility currently under construction at the Ohtake Plant, as well as at the Harima Plant assembly facility and Polyplastics Co., Ltd., a subsidiary.

Intellectual and Integrated Production System Consulting Business Launched

Daicel's fresh approach to innovation has earned it high praise and a number of industry awards, such as the Technology Award from the Society of Chemical Engineers, Japan and the Grand Prize at the Monozukuri Awards from the Society of Plant Engineers Japan. In order to share this approach with others and enhance the competitiveness of Japan's manufacturing industries, Daicel has launched an intellectual and integrated production system consulting business in collaboration with Yokogawa Electric Corporation.

Business Process Innovation

Applying the Results of Production Innovations to Business Processes

Daicel is currently expanding the generalization initiatives undertaken as part of its production innovation activities to reform not only its production, but also sales, purchasing, and logistics systems. In this way, we are undertaking business process innovation activities to achieve productivity gains by generalizing the business processes of the entire Group.

We have already initiated process generalization and systemization in our cellulose business (starting June 2005) and in the organic chemical products and CPI (chiral pharmaceutical ingredients) business (October 2006). These programs have already resulted in a huge reduction in clerical work. Business process innovation has also had the beneficial effects of raising efficiency and reinforcing internal control functions.

Starting in fiscal 2008, we plan to centralize the Group's information systems based on our successes in reforming and generalizing business processes.

Aboshi Plant

Basic Approach

Daicel's basic policy regarding the distribution of profits emphasizes a comprehensive and long-term balance between consistent and appropriate dividends to shareholders and reinforcing internal reserves to solidify the Company's revenue base. To this end, our policy takes account of profits for each fiscal year and business development prospects viewed from a long-term perspective. Retained earnings are allocated to establishing new businesses and expanding business activities. Investments required for ensuring a highly profitable structure are made, including that for strengthening existing businesses through research and development, building new and upgraded equipment and facilities, and programs to enhance efficiency.

Capital Investment

During the three-year period of the new medium-term business plan, which began in April 2007, we plan to allocate capital investments of around ¥120.0 billion for the construction of a new facility for manufacturing cellulose acetate for LCD film applications at the Ohtake Plant and other projects.

Investment Plan

Business Segments	Planned Investment under the New Medium-Term Business Plan	
	Total investment over three-year period (billions of yen)	Main Investment Projects
Cellulose Derivatives	37.5	Triacetyl cellulose (TAC) facility (Ohtake Plant)
Organic Chemicals	28.5	Increase production capacity for acetic acid derivatives, switch to new method for making ethylamine, increase production of peracetic acid derivative epoxy compounds, and increase chiral production capacity
Plastics and Films	22.5	Expand liquid crystal polymer (LCP) facility (Polyplastics' Fuji Plant)
Pyrotechnic Devices	26.0	Raise production capacity for inflators, bring manufacture of major inflator components in-house and strengthen them
Functional Product and Others, and Companywide	5.5	
Total	120.0	

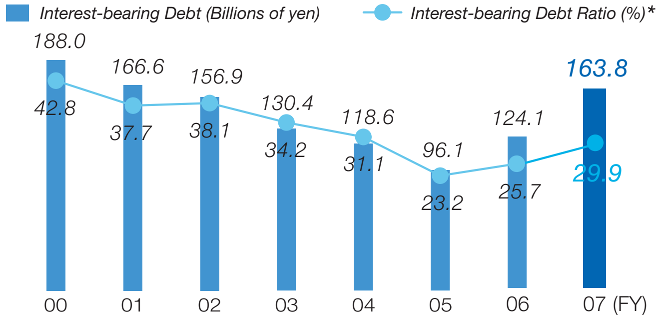
Reinforcing our Financial Foundation

The Daicel Group strives to enhance asset efficiency and maximize cash flows. We place high priority on ROA (the ratio of recurring profit to total assets) as an indicator of our success in achieving these aims. At the end of fiscal 2007, ROA was 6.6%, up from 4.0% in fiscal 2004.

Our current plan is to raise ROA to more than 9.0% by fiscal 2010. To achieve this goal, we will reduce total assets by disposing of redundant assets including unnecessary securities and reduce the required working capital of the entire Group. In these ways, we will continue improving asset efficiency.

In recent years, capital expenditures have been the main factor in the increase in interest-bearing debt. Under the new medium-term business plan, we intend to use operating cash flows to reduce interest-bearing debt to around ¥130.0 billion by the end of fiscal 2010.

Interest-bearing Debt and Debt Ratio



*Interest-bearing debt to total assets

Basic Approach

Since its inception, Daicel has endeavored to maintain environmentally safe operations and become a corporate group that can achieve sustainable growth. In accordance with our basic policy for Responsible Care established in 1995, we seek to ensure safety and health and protect the environment in whatever stage of its operations—from the development of products to their manufactures, distribution, use and disposal.

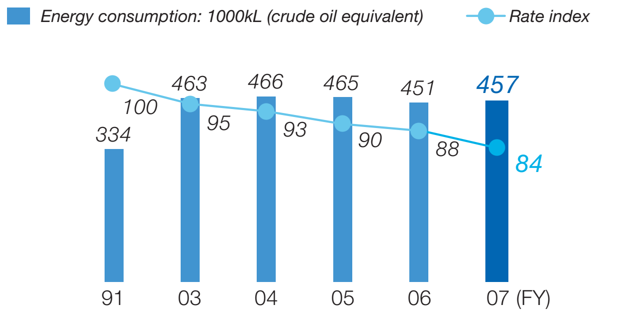
We view all aspects of responsible care—Environmental Preservation, Chemical and Product Safety, Occupational Health and Safety, Process Safety and Disaster Prevention, Distribution Safety, and Communication with the Community—as fundamental to continuous growth. Under the new medium-term business plan, as well, we give priority to responsible care and corporate ethics in all of our business activities. In this section, we introduce several initiatives in our environmental protection program devoted to prevention of global warming and energy conservation.

Prevention of Global Warming and Energy Conservation Efforts

Daicel has long been committed to reducing emissions of greenhouse gases through its energy conservation efforts. Under a voluntary initiative, we have been focusing on reducing our energy consumption rate index to the target level of 90 (relative to the fiscal 1991* level of 100) by the end of fiscal 2011. In fiscal 2007, we recorded an index of 84, which represents achievement of our target for the third consecutive year. In fiscal 2007, we also reduced our emissions of greenhouse gases to 1.29 million tons.

* This is the same as the target defined in the Chemical Industry Voluntary Environmental Preservation Action Plan proposed by the Japan Chemical Industry Association (JCIA).

Amounts and Rate Index of Energy Consumption



Other main initiatives related to prevention of global warming and energy conservation are outlined below.

- Since 2005, the Arai Plant, Aboshi Plant, and Hirohata Plant have substituted from using conventional heavy oil to natural gas and city gas, fuel that plays a huge part in preventing global warming. Polyplastics Co., Ltd., a Group company, has reduced greenhouse gas emissions through the introduction of a natural gas engine cogeneration system in 2005.

- The Ohtake Plant has constructed a circulating fluidized bed boiler that is powered by fuel made from used tires. The boiler began operating in July of 2007.

- Daicel Logistics Service Co., Ltd. is planning to shift from land transportation (trucks) to marine transportation (inland shipping) for the transportation of raw materials and products between Hanshin Port and Ohtake in Himeji. The company expects to start shipping entirely by boat in October 2007.

Corporate Governance

Basic Approach

Daicel recognizes corporate governance as an important aspect of business that can contribute to improved corporate value. As a publicly listed enterprise, Daicel is committed to carrying out its social mission and responsibilities. We believe in the need to strengthen our relationships with various stakeholders.

We ensure our maneuverability by clarifying the role-sharing of various organs, and we have implemented an agile management system capable of timely decision-making and execution. We can respond quickly to opinions from outside the Company and can apply them to our corporate operations. We intend to maintain sound company management by improving the transparency and fairness of management.

Timely Decision-Making and Execution

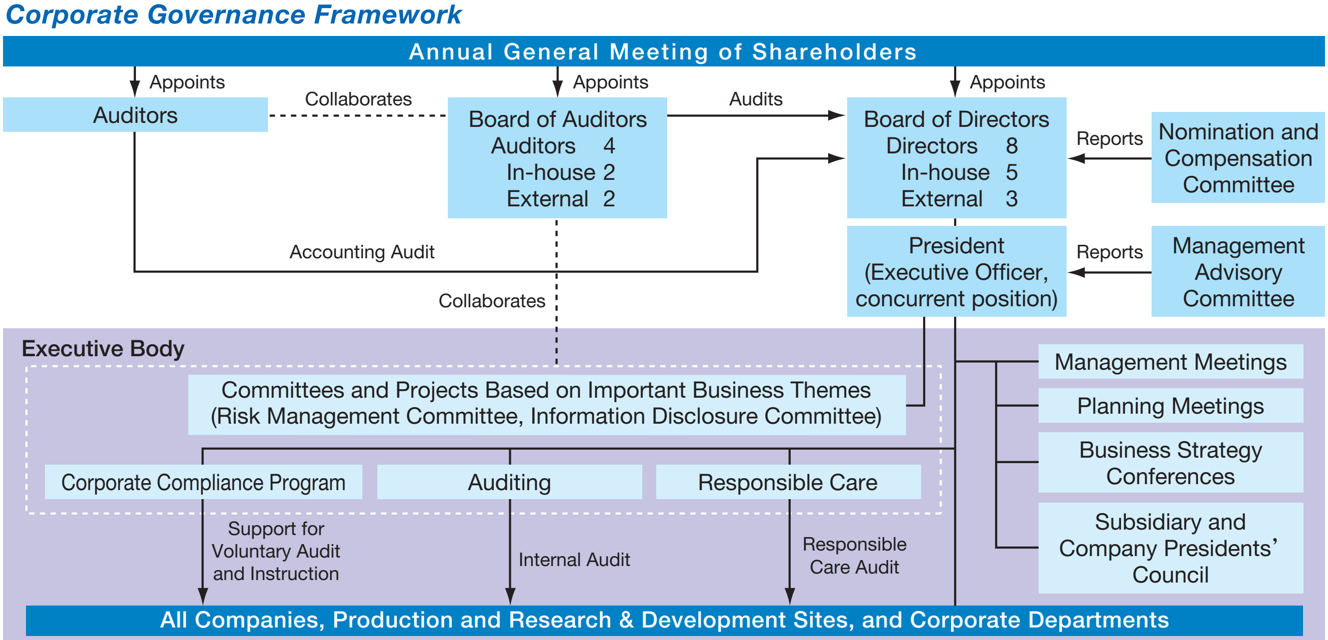
The Company has adopted an executive officer system to clearly separate the decision-making and supervisory functions from the business execution function. This system enables timely decision-making and responsive execution of duties.

The Company's Board of Directors comprises eight directors, three of whom are external directors. In principle, the Board of Directors meets once a month. At these meetings, the directors make decisions regarding important management items based on Board regulations, while also overseeing the operating and executive functions.

The president holds management meetings, which serve as a forum to deliberate and ratify the execution of fundamental policies concerning company management as determined by the Board of Directors. Management meetings are attended by the president, members of the Management Advisory Committee, full-time corporate auditors, and other executive officers designated by the president. Planning meetings, comprising the same membership as the management meetings, are held to discuss important proposals put forward by each operating division.

Business strategy conferences are held to discuss issues and problems concerning individual Group companies and business divisions. Daicel's management team receives reports from in-house company presidents and the presidents of major subsidiaries through the Subsidiary and Company President's Council so it can accurately ascertain the current

Corporate Governance Framework



Note: Executive Officers include heads of companies, heads of sites, and heads of corporate departments who administer corporate affairs.

state of each business. The Council provides support and resolves problems as necessary.

Enhancing the Quality of Decision-Making

Daicel elects three external directors as a means of ensuring the appropriateness of decision-making. At Board of Directors meetings, these external directors voice their valuable opinions from a fair and neutral standpoint supported by their extensive business knowledge and experience.

Monitoring and Auditing System

The Company's Board of Auditors consists of four auditors, two of whom are external auditors. One external auditor comes from another company, while the other is a lawyer.

In addition to the monitoring of business undertaken by the Board of Directors, auditors attend management meetings and other important meetings to oversee the business and affairs of the Company. The Board of Auditors also reports, deliberates, and decides on important auditing-related items.

The Nomination and Compensation Committee consists of the president and external directors. The function of this committee is to deliberate on matters raised by the chairman of the Board of Directors regarding personnel matters relating to the nomination and compensation of directors and executive officers.

The Management Advisory Committee, which reports to the president, was established in April 2002 to enable exhaustive deliberation on important matters, such as the formulation of Group strategies and corresponding business restructuring.

Collaboration between Auditors and Internal Auditing

At Daicel, Auditing performs the role of an internal auditing department. There is also the Corporate Compliance Program and Responsible Care, which audit matters related to compliance and responsible care activities, respectively. The auditors have the following collaborations with the Company's various internal auditing functions.

Collaboration with Auditing

The auditors receive a briefing three times a year on matters related to internal auditing.

Collaboration with Corporate Compliance Program

In addition to holding regular meetings with the Corporate Compliance Program four times a year, the auditors also participate in a top management review of corporate ethics and the training of corporate ethics for upper management.

Collaboration with Responsible Care

The auditors participate in the annual Daicel Group Responsible Care Convention, held for the purpose of enhancing activities and raising awareness of principles and policies related to responsible care.

Support for External Directors and Auditors

At Board of Directors' meetings, which are attended by auditors, external directors and auditors are briefed on the agenda items. When there is a particularly important decision to be made, the relevant director visits external directors and auditors beforehand to explain the contents of the proposal and provide information to ensure that an appropriate decision is taken at the meeting.

In the event that an external director or external auditor is absent from a Board of Directors' meeting, the member is sent the minutes of the meeting. In the case of important matters, a company official visits the external member at a later date to give a briefing on the meeting.

Addressing Risk Management

In April 2006, Daicel adopted a Risk Management Code that stipulates a company-wide risk management policy. In addition, a Risk Management Committee was formed to control and promote company-wide risk management. At present, under the instructions of the Risk Management Committee, and according to the Risk Management System Establishment Project launched during the same period, Daicel is considering a system for applying the PDCA cycle of risk management throughout all group companies. In November 2006, our company created its first inventory of risks, which comprehensively investigated and shed light on significant challenges in that area. In the future, we plan to assign priority levels to significant risks we have identified and implement appropriate countermeasures.

With regard to the initial response to the identification of significant risks, we will establish new regulations after reviewing the content of existing regulations and expanding the scope of possible plant accidents.

In our new medium-term business plan, we targeted the reinforcement of our foundation and identified two key initiatives: risk management and internal controls. We will improve these initiatives and link them to the creation of a foundation for our corporate social responsibility.

Corporate Ethics

Basic Approach

Daicel believes that compliance with the law and corporate ethics are fundamental to the existence of every business. Our aim is to earn the trust of society at large through the exemplary ethics and sound judgment displayed by each and every one of our employees or executives.

Compliance Framework

In July 2006, we formulated the “Daicel Group Basic Philosophy” and the “Daicel Group Conduct Policy.” Previously, each Group Company had their own conduct policy and codes of conduct. However, we formulated these standards to cover the entire Group in response to the growing need for the Group to act as one in fulfilling its social responsibilities. These standards serve as a basis for raising further awareness concerning ethical matters within the Group.

We established the Corporate Compliance Program in order to promote compliance activities. The Program provides employee training in compliance matters. It also receives feedback on annual action plans formulated by each division, and reports to the Board of Directors.

In the event that a Company employee or executive discovers an action that appears to be a violation of laws, regulations, or standards, that person reports the matter immediately to the Corporate Compliance Program. Based on that information, the Corporate Ethics Officer then investigates the matter, and takes the required action upon conferring with the president. In addition, we have an in-house and external Corporate Ethics Help Line to ensure that information is passed on promptly should an employee discover an act that appears to breach a law or regulation. This framework also ensures that the whistleblowers is not placed at any disadvantage as a result of his or her action.

President
Daisuke Ogawa *(Left)*
Director
Yasuo Umeno *(Right)*

Board of Directors and Corporate Auditors

PRESIDENT
Daisuke Ogawa

DIRECTORS
Yasuo Umeno
Tetsuji Yanami
Keiichiro Tsuji
Kazuo Yamaguchi
Shigetaka Komori
President of FUJIFILM Holdings Corporation
Akishige Okada
Advisor of Sumitomo Mitsui Banking Corporation
Yuichi Miura
Advisor of Tokuyama Corporation

CORPORATE AUDITORS
Mikio Kitagawa
Hideo Asanuma

AUDITORS
Hirokuni Imai
President of SEIWA REAL ESTATE CO., LTD.
Yoshikatsu Moriguchi
Lawyer

Executive Officers

CHIEF EXECUTIVE OFFICER
Daisuke Ogawa

SENIOR MANAGING EXECUTIVE OFFICER
Yasuo Umeno
General Manager of Corporate Support Center, Corporate Compliance Program, Business Process Innovation, President of Daicel Finance Ltd.

MANAGING EXECUTIVE OFFICERS
Tetsuji Yanami
General Manager of R&D Management, Intellectual Property Center, Analysis Service Center
Keiichiro Tsuji
General Manager of Himeji Production Sector, General Manager of Aboshi Plant, President of Kyodo Sakusan Co., Ltd.
Kazuo Yamaguchi
General Manager of Production Technology Management, Responsible Care
Tetsuzo Miyazaki
President of Aerospace & Defense Systems/Safety Systems Company
Kohji Shima
General Manager of Engineering Center, Deputy General Manager of Production Technology Management
Ichiro Katagiri
President of Cellulose Company
Shuzaburo Kumano
President of Organic Chemical Products Company
Masumi Fukuda
General Manager of Corporate Planning
Masayuki Mune
President of Daicel Polymer Ltd.

EXECUTIVE OFFICERS
Yoshiro Taniguchi
General Manager of Nagoya Sales Office, Executive Vice President of Aerospace & Defense Systems/Safety Systems Company, General Manager of Safety Systems Division and Safety Systems Overseas Business Division, Aerospace & Defense Systems/Safety Systems Company
Shinzo Uda
President of Ningbo Da-An Chemical Industries Co., Ltd.
Tetsuo Yoshioka
General Manager of Aerospace & Defense Systems Division, Aerospace & Defense Systems/Safety Systems Company
Mitsuharu Shimada
General Manager of Ohtake Plant
Hitoshi Oya
General Manager of Raw Material Purchasing Center
Yasunori Iwai
Executive Vice President of Aerospace & Defense Systems/Safty Systems Company
Yuji Iguchi
General Representative in China, Chairman of the Board of Daicel Chemical (China) Investment Co.,Ltd., Deputy General Manager of Corporate Planning
Misao Fudaba
Deputy General Manager of Corporate Support Center
Yoshimi Ogawa
Executive Vice President of Aerospace & Defense Systems/Safety Systems Company, General Manager of Harima Plant, Aerospace & Defense Systems/Safety Systems Company

	2007	2006	2005	2004
For the year:				
Net sales	**¥381,423**	¥335,520	¥306,335	¥281,740
Operating income	**36,399**	33,570	28,553	21,207
Income before income taxes and minority interests	**33,185**	29,386	22,380	8,055
Net income (loss)	**17,438**	14,221	10,844	5,166
Amounts per common share (yen):				
Net income (loss)	**¥ 48.19**	¥ 39.16	¥ 29.82	¥ 14.21
Cash dividends applicable to the year	**8.00**	8.00	8.00	6.00
Capital expenditures	**¥ 55,316**	¥ 59,018	¥ 25,377	¥ 20,991
Depreciation and amortization	**23,774**	22,484	22,490	24,514
Research and development expenses	**11,717**	11,221	11,219	11,085
At year-end:				
Total current assets	**¥206,670**	¥172,344	¥160,541	¥141,233
Total assets	**547,432**	483,469	413,493	381,485
Total current liabilities	**152,556**	133,420	102,779	105,093
Total long-term liabilities	**152,467**	121,159	110,875	88,684
Total equity*1	**242,409**	197,780	171,225	160,479
Ratios:				
Current ratio (%)	**135.5**	129.2	156.2	134.4
Shareholders' equity ratio (%)*2	**39.5**	40.9	41.4	42.1
Return on assets (%)	**3.4**	3.2	2.7	1.4
Return on equity (%)	**8.4**	7.7	6.5	3.3
Ratio of net income to net sales (%)	**4.6**	4.2	3.5	1.8
Assets turnover (times)	**0.7**	0.7	0.8	0.7
Tangible fixed assets turnover (times)	**1.8**	1.8	1.9	1.7
Other information:				
Price range of common stock (yen):				
High	**¥ 1,050**	¥ 1,017	¥ 597	¥ 501
Low	**739**	516	441	374
Exchange rate at year-end (yen per US$1)	**¥ 118.00**	¥ 117.00	¥ 107.00	¥ 106.00
Number of employees (at year-end)	**7,034**	6,248	5,819	5,604

*1: From FY 2007, Total Shareholders' Equity is being shown as Total Equity.
*2: Shareholders' Equity Ratio= Total Equity less Minority Interests/ Total Assets

Millions of yen, except per share amounts and other information

2003	2002	2001	2000	1999	1998	1997
¥271,342	¥261,358	¥261,520	¥238,240	¥249,111	¥257,177	¥260,884
20,410	15,483	14,627	14,369	13,294	7,891	16,140
6,864	6,841	10,066	8,396	6,469	5,968	12,891
2,029	3,635	3,381	3,125	1,401	(845)	3,141
¥ 5.50	¥ 9.86	¥ 9.03	¥ 8.48	¥ 3.77	¥ (2.26)	¥ 8.40
6.00	6.00	6.00	6.00	6.00	6.00	6.00
¥ 16,747	¥ 20,082	¥ 22,189	¥ 38,820	¥ 27,490	¥ 29,122	¥ 26,597
25,413	26,709	28,484	26,931	27,666	30,805	30,419
11,747	11,485	11,841	10,393	10,735	11,395	11,195
¥143,280	¥150,862	¥168,079	¥191,248	¥169,695	¥180,026	¥225,678
381,518	412,008	442,055	439,108	401,062	414,088	462,308
107,385	135,303	141,072	156,916	131,812	147,891	190,885
94,934	95,150	114,526	107,933	100,218	95,937	98,887
151,987	154,515	155,314	142,777	138,257	139,735	143,510
133.4	111.5	119.1	121.9	128.7	121.7	118.2
39.8	37.5	35.1	32.5	34.5	33.7	31.0
0.5	0.9	0.8	0.7	0.3	(0.2)	0.7
1.3	2.3	2.3	2.2	1.0	(0.6)	2.2
0.7	1.4	1.3	1.3	0.6	(0.3)	1.2
0.7	0.6	0.6	0.6	0.6	0.6	0.6
1.5	1.4	1.4	1.3	1.3	1.4	1.4
¥ 423	¥ 467	¥ 378	¥ 497	¥ 395	¥ 491	¥ 698
293	290	273	260	212	150	441
¥ 120.00	¥ 133.00	¥ 124.00	¥ 106.00	¥ 121.00	¥ 132.10	¥ 124.10
5,416	5,363	5,412	5,132			

Operating Results

Net Sales

In fiscal 2007, ended March 31, 2007, consolidated net sales amounted to ¥381.4 billion, up ¥45.9 billion or 13.7% from fiscal 2006. This was mainly due to an increase in sales volume and prices revisions made by the company to reflect escalating raw materials and fuel prices. The movement of the yen against the U.S. dollar during the year had a ¥5.7 billion positive impact on net sales.

Revenues were boosted by a number of factors. In the cellulosic derivatives segment, sales of cellulose acetate increased ¥5.4 billion year-on-year, due to greater sales volume for LCD film applications and price revisions. Similarly, sales of tow for cigarette filters grew ¥2.1 billion owing to increased sales volume to overseas customers, price revisions, and the yen's depreciation.

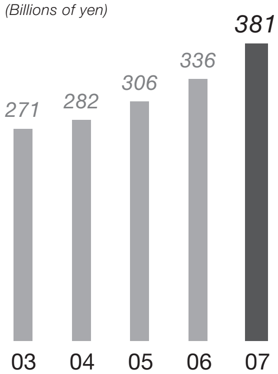
In the organic chemicals segment, sales of acetic acid rose ¥3.8 billion, brought about by upward revisions of sales prices to reflect increased prices of methanol, a main raw material, amid supply and demand pressures. Sales of acetic acid derivatives, solvents, and fine chemicals rose ¥4.6 billion, stemming primarily from increased sales volume and price revisions made to counter surging raw materials costs, as well as a shift of certain high-performance materials to this segment from the functional products and others segment in the year under review.

In the plastics and films segment, sales of engineering plastics, such as polyacetal (POM) and polybutylene terephthalate (PBT), jumped ¥14.5 billion year-on-year, buoyed by solid demand from the domestic automobile sector and Japanese and overseas electronic device markets. Sales of POM made a particularly strong contribution, benefiting from an increase in sales volume following commencement of full-scale operations of a new production facility in China in October 2005. In the plastic compounds, sheet, molded vessels and shock-absorbing materials, and films businesses, sales increased ¥3.5 billion due to such factors as price revisions.

In the pyrotechnic devices segment, sales of inflators for

Net Sales

(Billions of yen)



automobile air bag systems surged ¥10.7 billion, thanks to significant increases in volume, both in Japan and overseas, on the back for growing need for air bag installation worldwide.

By contrast, several factors had a negative impact on revenues. In the plastic products and films segment, reduced demand for certain construction material products in the molded plastic products business, which is classified in the other plastic products business, led to a ¥500 million decline in sales. In the functional products and others segment, the shift of certain functional products to the organic chemicals segment, as well as a decline in sales of membranes to filtration plants, had a ¥1.8 billion negative affect on net sales.

Gross Profit

Gross profit increased ¥5.1 billion, or 5.9%, to ¥91.9 billion, but gross profit to sales ratio declined 1.7 percentage points, to 24.1%. This was because increased sales volume and revisions of sales prices failed to fully offset the negative impact of escalating raw materials and fuel prices.

Selling, General and Administrative (SG&A) Expenses

SG&A expenses totaled ¥55.5 billion, an increase of ¥2.3 billion, or 4.3%, from the previous year. This stemmed mainly from a rise in direct sales costs accompanying the increase in sales volume, as well as higher personnel expenses due to expansion of operations. The ratio of SG&A expenses to consolidated net sales improved 1.2 percentage points, to 14.6%.

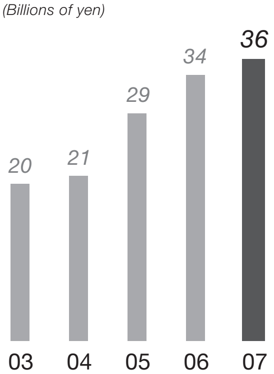
Operating Income

Operating income grew ¥2.8 billion, or 8.4%, to ¥36.4 billion. The ratio of operating income to net sales edged down 0.5 percentage point, to 9.5%. The movement of the yen against the U.S. dollar during the year had a ¥1.5 billion positive impact on operating income.

Several factors had a positive effect on operating income. The cellulosic derivatives segment boosted income by ¥0.8 billion mainly owing to increased sales volume of cellulose acetate. The organic chemicals segment posted a ¥1.8 billion rise thanks to higher sales volume. The plastics and

Operating Income

(Billions of yen)



films segment reported ¥1.6 billion growth in operating income thanks to increased sales volumes of engineering plastics and plastic compounds.

By contrast, the pyrotechnic devices segment posted a ¥0.6 billion decline in operating income, due to increased fixed costs stemming from the establishment of an overseas facility to make inflators for automobile air bags, as well as higher costs associated with reinforcement of that business's foundation.

Other Income (Expenses)

Other expenses, net, totaled ¥3.2 billion, an improvement of ¥1 billion year-on-year. The primary factors for the improvement included a ¥1 billion fall in impairment losses on fixed assets and the non-recurrence of one-time charges of ¥1.2 billion related to employee's retirement benefit, while negative factors included a ¥1 billion increase in interest expenses.

Income before Taxes and Minority Interest

Income before taxes and minority interest grew ¥3.8 billion, or 12.9%, to ¥33.2 billion.

Income Taxes

The effective tax rate after application of tax-effect accounting decreased 3.0 percentage points, to 36.2%.

Minority Interest

Minority interest rose ¥0.1 billion, or 3.1%, to ¥3.7 billion.

Net Income

Net income increased ¥3.2 billion, or 22.6%, to ¥17.4 billion.

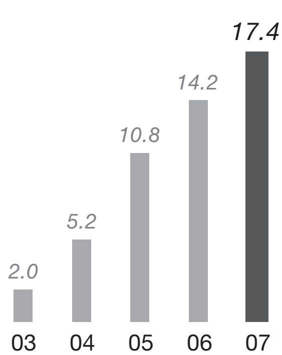
Per Share Information

Net income per share reached ¥48.19, up from ¥39.16 a year earlier.

In the year under review, the Company declared an interim dividend of ¥4.00 and the year-end dividend of ¥4.00, for total annual dividends of ¥8.00 per share.

Net Income

(Billions of yen)



Financial Position

Assets

As of March 31, 2007, total assets stood at ¥547.4 billion, up ¥64.0 billion, or 13.2%, from a year earlier.

Current assets rose ¥34.3 billion, or 19.9%, to ¥206.7 billion. Major factors included a ¥16.1 billion rise in inventories due to hikes in the prices of raw materials and fuels, as well as a ¥14.1 billion increase in trade notes and trade accounts accompanying growth in net sales.

Property, plant and equipment amounted to ¥225.5 billion, up ¥24.2 billion, or 12.0%, from a year earlier. This was primarily due to a ¥24.4 billion in construction in progress, reflecting new capital expenditures.

Liabilities

Total liabilities amounted to ¥305.0 billion, up ¥50.4 billion, or 19.8%, from a year earlier. The rise stemmed mainly from an increase in long-term debt (including current portion) due to purchases of property, plant, and equipment, as well as an increase in short-term loans. Together, long-term and short-term borrowings increased ¥49.7 billion.

Interest-bearing debt increased ¥39.7 billion, to ¥163.8 billion. The ratio of interest-bearing debt to total assets climbed 4.2 percentage points, to 29.9%.

Equity

Total equity at fiscal year-end totaled ¥242.4 billion.

Total shareholders' equity (total equity minus minority interests) amounted to ¥216.0 billion, and the shareholders' equity ratio was 39.5%.

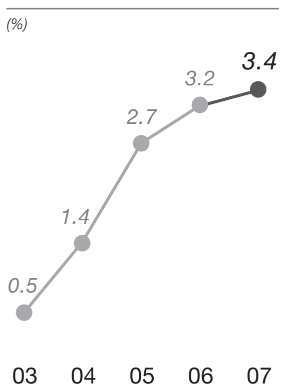
Cash Flows

Cash and cash equivalents at fiscal year-end stood at ¥14.0 billion, down ¥0.4 billion, or ¥2.7%, from a year earlier.

Cash from operating activities

Net cash provided by operating activities amounted to ¥25.5 billion, down ¥7.2 billion, or 22.1%, from the previ-

Return on Assets



ous fiscal year. Major factors included increases in notes and accounts receivable and inventories, which led to an increase in working capital.

Cash from investing activities

Net cash used in investing activities totaled ¥54.2 billion, down ¥5.8 billion, or 9.7% from the previous fiscal year. The primary factor was a decrease in capital expenditures associated with the acquisition of property, plant, and equipment.

Cash from financing activities

Net cash provided by financing activities was ¥26.9 billion, up ¥7.4 billion, or 37.6%, from the previous year. Major factors were increases in proceeds from long-term and short-term borrowings.

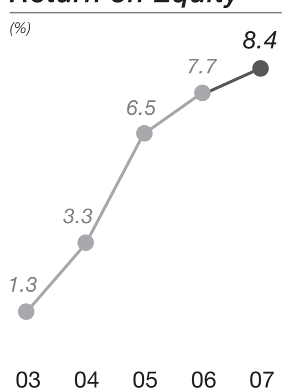
Business Risks

Business risks that may potentially have significant influence on investor decisions include not only risks common to industrial sectors, such as changes in macroeconomic and political conditions, but also the following types of factors. Items listed in this annual report do not necessarily comprise all of the risks related to the business of the Daicel Group.

Trends in currency exchange rates

The Company's ratio of overseas sales to consolidated net sales is increasing year by year (35.5% in fiscal 2007), and the Company's results can be more easily influenced by trends in currency exchange rates than previously. We generally believe that depreciation of the yen has a positive effect on performance, while appreciation of the yen has a negative effect on our performance. Though the Company executes forward currency exchange contracts and other

Return on Equity



risk-hedging activities, this does not guarantee that such exchange risks can be completely avoided.

Risks in expanding overseas business development

The Company is broadening its overseas business development, centered on China and the rest of Asia as well as in North America, Europe and elsewhere. However, risks are inherent in the case of overseas operations, such as unforeseen legal and regulatory changes, vulnerability of industrial infrastructure, difficulties in hiring and retaining qualified employees, or social or political instability caused by acts of terrorism and war. In the event that any of these risks arise and cause disruption to overseas business operations, there is the possibility that Daicel Group's consolidated performance and business plans would be affected.

Swings in raw material (methanol) prices

The Daicel Group purchases a large volume of methanol, the raw material for its core products, such as acetic acid and polyacetal. We apply mechanisms to consistently purchase methanol at a relatively low price, such as entering long-term contracts and investing in methanol-producing companies. Upswings in the methanol market may negatively affect Group performance however.

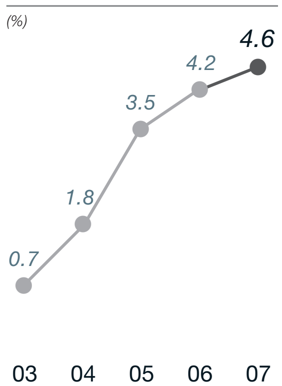
Swings in other raw material prices

Daicel goes to great lengths to absorb sustained raw material and fuel price increases by switching to raw materials and fuels that are less expensive and more stable in price, making cost savings from improved manufacturing, and revising product sales prices. However, there is a limit as to how much can be absorbed. In the event of escalating costs that exceed certain limits, there is the possibility that this would have a negative impact on Group performance.

Quality guarantee and product liability

Daicel has established a quality guarantee structure and

Ratio of Net Income to Net Sales



strives to assure product safety. As a precaution, we also carry product liability insurance. However, in cases where products manufactured by the Company are found to be the cause of damage, the Company's performance may be negatively impacted.

Industrial accidents

The Company consistently conducts safety and disaster prevention activities and strives daily to assure the safety of its manufacturing plants and other facilities. However, in cases where fires, explosions, or other industrial accidents or disasters occur, the Company's performance may be negatively affected.

Earthquakes and natural disasters

One of the Group's primary manufacturing facilities, the Fuji Plant of Polyplastics Co., Ltd., is in a region that requires reinforced countermeasures for disaster prevention related to the anticipated Tokai earthquake. We conduct earthquake-training drills and take countermeasures to protect equipment there. We also practice disaster preparedness and emergency training drills at other facilities. However, in the event that significant damage is incurred by a natural disaster, Group results may be negatively affected.

Risks from product and technological obsolescence

Depending on the industry, product cycles are rapid and there is a possibility that sales volumes decrease beyond initial expectations, R&D expenses not be recouped and income from Daicel's businesses deteriorate. Moreover, intense pressure to reduce sales prices cannot be always be sufficiently covered by cost reductions, which also could cause income from Daicel's businesses to decline.

Risk from violent market fluctuations

In the event of excess of supply caused by such factors as large-scale plants being constructed by other companies, or a drastic decline in demand caused by abnormal economic conditions, there is the possibility that Daicel's income from its businesses could deteriorate.

Outlook for Fiscal 2008

While the Japanese economy is expected to continue expanding, such factors as a sustained escalation in raw material and fuel costs, rising interest rates, and deepening turmoil in international affairs give no grounds for optimism in terms of business conditions.

The business environment in the chemical industry remains wrought with difficulties, brought about by sales price revisions in response to the escalating costs of raw materials and fuel, the further need for selection and focus in operations, the need to maintain cost competitiveness and strengthen R&D, environmental safety concerns, and other problems that need to be addressed.

Under these circumstances, the Daicel Group's performance outlook depends on a number of factors: continued growth in demand for TAC for use in LCD films, an increase in sales volume of engineering plastics, a significant rise in sales volume for automobile air bag inflators, upward sales price revisions to keep pace with the rising costs of raw materials and fuel, and efforts to reduce costs. For fiscal 2008, Daicel is forecasting net sales of ¥415.0 billion, operating income of ¥36.5 billion, recurring profit of ¥33.5 billion, and net income of ¥16.5 billion.

Should the above-mentioned targets be successfully achieved, this would mean record highs in terms of net sales and operating income (marking the tenth consecutive period of increased operating income).

These forecasts have been calculated taking into account an anticipated ¥3.0 billion increase in depreciation expenses in depreciation stemming from changes to the depreciation system.

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2007	2006	**2007**
Assets			
Current assets:			
Cash and cash equivalents	**¥ 13,958**	¥ 14,350	**$ 118,288**
Marketable securities (Note 3)	**25**	63	**212**
Receivables:			
Trade notes	**7,899**	6,943	**66,941**
Trade accounts	**89,511**	76,356	**758,568**
Unconsolidated subsidiaries and associated companies	**6,469**	4,034	**54,822**
Allowance for doubtful receivables	**(229)**	(204)	**(1,941)**
Inventories (Note 4)	**75,622**	59,512	**640,865**
Deferred tax assets (Note 8)	**4,438**	3,072	**37,610**
Account receivable for expropriation (Note 15)	**919**	2,363	**7,788**
Other current assets	**8,058**	5,855	**68,288**
Total current assets	**206,670**	172,344	**1,751,441**
Property, plant and equipment (Notes 5 and 14)**:**			
Land	**27,609**	27,849	**233,975**
Buildings and structures	**133,804**	134,639	**1,133,932**
Machinery and equipment	**466,618**	454,191	**3,954,390**
Construction in progress	**56,181**	31,825	**476,110**
Total	**684,212**	648,504	**5,798,407**
Accumulated depreciation	**(458,699)**	(447,143)	**(3,887,280)**
Net property, plant and equipment	**225,513**	201,361	**1,911,127**
Investments and other assets:			
Investment securities (Note 3)	**82,784**	77,954	**701,559**
Investments in and advances to unconsolidated subsidiaries and associated companies (Note 3)	**7,992**	7,396	**67,729**
Deferred tax assets (Note 8)	**812**	697	**6,881**
Account receivable for expropriation (Note 15)	**5,364**	6,282	**45,458**
Other assets	**18,297**	17,435	**155,059**
Total investments and other assets	**115,249**	109,764	**976,686**
Total	**¥ 547,432**	¥ 483,469	**$ 4,639,254**

See notes to consolidated financial statements.

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2007	2006	**2007**
Liabilities and equity			
Current liabilities:			
Short-term bank loans (Note 5)	**¥ 41,089**	¥ 23,066	**$ 348,212**
Current portion of long-term debt (Note 5)	**18,715**	29,323	**158,602**
Payables:			
Trade notes	**1,565**	1,474	**13,263**
Trade accounts	**54,257**	47,866	**459,805**
Construction	**5,474**	8,691	**46,390**
Unconsolidated subsidiaries and associated companies	**3,224**	2,022	**27,322**
Income taxes payable (Note 8)	**6,908**	7,466	**58,542**
Other current liabilities	**21,324**	13,512	**180,712**
Total current liabilities	**152,556**	133,420	**1,292,848**
Long-term liabilities:			
Long-term debt (Note 5)	**103,981**	71,665	**881,195**
Liability for retirement benefits (Note 6)	**8,691**	7,894	**73,652**
Deferred tax liabilities (Note 8)	**18,865**	16,750	**159,873**
Deferred gain from expropriation (Note 15)	**19,309**	22,580	**163,636**
Other long-term liabilities	**1,621**	2,270	**13,737**
Total long-term liabilities	**152,467**	121,159	**1,292,093**
Minority interests		31,110	
Commitments and contingent liabilities (Notes 11 and 16)			
Equity (Notes 7 and 17)**:**			
Common stock, —authorized 1,450,000,000 shares issued 364,942,682 shares in 2007 and 2006	**36,275**	36,275	**307,415**
Capital surplus	**31,575**	31,573	**267,585**
Retained earnings	**112,970**	98,483	**957,373**
Unrealized gain on available-for-sale securities	**34,234**	32,704	**290,119**
Deferred gain (loss) on derivatives under hedge accounting	**37**		**313**
Foreign currency translation adjustments	**2,074**	(156)	**17,576**
Treasury stock —at cost 3,107,676 shares in 2007 and 3,001,241 shares in 2006	**(1,193)**	(1,099)	**(10,110)**
Total	**215,972**	197,780	**1,830,271**
Minority interests	**26,437**		**224,042**
Total equity	**242,409**		**2,054,313**
Total	**¥547,432**	¥483,469	**$4,639,254**

Consolidated Statements of Income

Daicel Chemical Industries, Ltd. and Consolidated Subsidiaries
Years ended March 31, 2007, 2006 and 2005

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2007	2006	2005	**2007**
Net sales	**¥381,423**	¥335,520	¥306,335	**$3,232,398**
Cost of sales (Note 9):	**289,563**	248,791	225,324	**2,453,924**
Gross profit	**91,860**	86,729	81,011	**778,474**
Selling, general and administrative expenses (Note 9)	**55,461**	53,159	52,458	**470,008**
Operating income	**36,399**	33,570	28,553	**308,466**
Other income (expenses):				
Interest and dividend income	**1,371**	873	638	**11,619**
Gain on sales of securities	**3**	594		**26**
Equity in earnings of unconsolidated subsidiaries and associated companies	**701**	450	619	**5,941**
Interest expense	**(3,051)**	(2,029)	(2,096)	**(25,856)**
Foreign exchange gain (loss)	**713**	793	(127)	**6,042**
Gain on sales of plant for expropriation (Note 15)			26,388	
Provision for deferred gain from expropriation (Note 15)			(26,388)	
Reversal of deferred gain from expropriation (Note 15)	**3,271**	3,807		**27,720**
Subsidies from municipal governments (Note 14)	**1,350**	2,218	40	**11,441**
Reduction of cost of property, plant and equipment (Notes 14 and 15)	**(4,621)**	(6,025)	(40)	**(39,161)**
Loss on dispositions of property, plant and equipment	**(1,290)**	(1,367)	(2,007)	**(10,932)**
Loss on revaluation of property, plant and equipment			(1,060)	
Past period service cost of employees' retirement benefit (Note 6)		(1,190)		
Impairment loss on fixed assets	**(139)**	(1,150)		**(1,178)**
Compensation received for the transfer of facilities (Note 15)		197		
Other-net	**(1,522)**	(1,355)	(2,140)	**(12,899)**
Other income (expenses)-net	**(3,214)**	(4,184)	(6,173)	**(27,237)**
Income before income taxes and minority interests	**33,185**	29,386	22,380	**281,229**
Income taxes (Note 8):				
Current	**12,312**	10,417	6,881	**104,339**
Deferred	**(312)**	1,115	1,094	**(2,644)**
Total income taxes	**12,000**	11,532	7,975	**101,695**
Minority interests in net income	**3,747**	3,633	3,561	**31,754**
Net income	**¥ 17,438**	¥ 14,221	¥ 10,844	**$ 147,780**

	Yen			U.S. dollars
Per share information (Notes 2 and 10):				
Net income	**¥ 48.19**	¥ 39.16	¥ 29.82	**$ 0.41**
Cash dividends applicable to the year	**8.00**	8.00	8.00	**0.07**

See notes to consolidated financial statements.

	Outstanding number of shares of common stock	Millions of yen									
		Common stock	Capital surplus	Retained earnings	Unrealized gain on available-for-sale securities	Deferred gain (loss) on derivatives under hedge accounting	Foreign currency translation adjustments	Treasury stock	Total	Minority interests	Total equity
Balance, April 1, 2004	361,923,856	¥ 36,275	¥ 31,377	¥ 79,203	¥ 17,419		¥ (2,839)	¥ (956)	¥ 160,479		¥ 160,479
Effect of initial inclusion of certain subsidiaries in consolidation				(195)					(195)		(195)
Net income				10,844					10,844		10,844
Cash dividends, ¥6.00 per share				(2,170)					(2,170)		(2,170)
Bonuses to directors and corporate auditors				(13)					(13)		(13)
Repurchase of treasury stock	(432,099)							(105)	(105)		(105)
Disposal of treasury stock	7,849		2					3	5		5
Net increase in unrealized gain on available-for-sale securities					2,737				2,737		2,737
Net change in foreign currency translation adjustments							(357)		(357)		(357)
Balance, March 31, 2005	361,499,606	36,275	31,379	87,669	20,156		(3,196)	(1,058)	171,225		171,225
Effect of initial inclusion of certain subsidiaries in consolidation				(97)					(97)		(97)
Net income				14,221					14,221		14,221
Cash dividends, ¥9.00 per share				(3,255)					(3,255)		(3,255)
Bonuses to directors and corporate auditors				(55)					(55)		(55)
Repurchase of treasury stock	(118,531)							(86)	(86)		(86)
Disposal of treasury stock	560,366		194					45	239		239
Net increase in unrealized gain on available-for-sale securities					12,548				12,548		12,548
Net change in foreign currency translation adjustments							3,040		3,040		3,040
Balance, March 31, 2006	361,941,441	¥ 36,275	¥ 31,573	¥ 98,483	¥ 32,704		¥ (156)	¥ (1,099)	¥ 197,780		¥ 197,780

		Millions of yen									
	Outstanding number of shares of common stock	Common stock	Capital surplus	Retained earnings	Unrealized gain on available-for-sale securities	Deferred gain (loss) on derivatives under hedge accounting	Foreign currency translation adjustments	Treasury stock	Total	Minority interests	Total equity
Balance, March 31, 2006	361,941,441	¥ 36,275	¥ 31,573	¥ 98,483	¥ 32,704		¥ (156)	¥ (1,099)	¥ 197,780		¥ 197,780
Reclassified balance as of March 31, 2006 (Note 2)										¥ 31,110	31,110
Effect of initial inclusion of certain subsidiaries in consolidation				(1)					(1)		(1)
Net income				17,438					17,438		17,438
Cash dividends, ¥8.00 per share				(2,895)					(2,895)		(2,895)
Bonuses to directors and corporate auditors				(55)					(55)		(55)
Repurchase of treasury stock	(110,954)							(96)	(96)		(96)
Disposal of treasury stock	4,519		2					2	4		4
Net change in the year					1,530	¥ 37	2,230		3,797	(4,673)	(876)
Balance, March 31, 2007	**361,835,006**	**¥ 36,275**	**¥ 31,575**	**¥112,970**	**¥ 34,234**	**¥ 37**	**¥ 2,074**	**¥ (1,193)**	**¥ 215,972**	**¥ 26,437**	**¥ 242,409**

	Thousands of U.S. dollars (Note 1)									
	Common stock	Capital surplus	Retained earnings	Unrealized gain on available-for-sale securities	Deferred gain (loss) on derivatives under hedge accounting	Foreign currency translation adjustments	Treasury stock	Total	Minority interests	Total equity
Balance, March 31, 2006	$307,415	$267,568	$834,602	$277,153		$ (1,322)	$ (9,314)	$1,676,102		$1,676,102
Reclassified balance as of March 31, 2006 (Note 2)									$263,644	263,644
Effect of initial inclusion of certain subsidiaries in consolidation			(9)					(9)		(9)
Net income			147,780					147,780		147,780
Cash dividends, $0.07 per share			(24,534)					(24,534)		(24,534)
Bonuses to directors and corporate auditors			(466)					(466)		(466)
Repurchase of treasury stock							(813)	(813)		(813)
Disposal of treasury stock		17					17	34		34
Net change in the year				12,966	$313	18,898		32,177	(39,602)	(7,425)
Balance, March 31, 2007	**$307,415**	**$267,585**	**$957,373**	**$290,119**	**$313**	**$17,576**	**$(10,110)**	**$1,830,271**	**$224,042**	**$2,054,313**

See notes to consolidated financial statements.

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2007	2006	2005	**2007**
Operating activities:				
Income before income taxes and minority interests	**¥ 33,185**	¥ 29,386	¥ 22,380	**$ 281,229**
Adjustment for:				
Income taxes-paid	**(12,957)**	(8,650)	(3,233)	**(109,805)**
Income taxes-refunded			1,840	
Depreciation and amortization	**23,774**	22,484	22,490	**201,475**
Impairment loss on fixed assets	**139**	1,150		**1,178**
Loss on dispositions of property, plant and equipment	**1,290**	1,367	2,007	**10,932**
Loss on revaluation of property, plant and equipment			1,060	
Provision for deferred gain from expropriation			26,388	
Gain on sales of plant for expropriation			(26,388)	
Reduction of cost of property	**4,621**	6,025		**39,161**
Reversal of deferred gain from expropriation	**(3,271)**	(3,807)		**(27,721)**
Subsidies from municipal governments	**(1,350)**	(2,218)		**(11,441)**
Gain on sales of securities	**(3)**	(594)	(33)	**(26)**
Equity in earnings of unconsolidated subsidiaries and associated companies	**(701)**	(450)	(619)	**(5,941)**
Changes in assets and liabilities:				
Notes and accounts receivable	**(13,371)**	(4,474)	(6,636)	**(113,313)**
Inventories	**(15,127)**	(6,472)	(6,687)	**(128,195)**
Notes and accounts payable	**6,637**	(604)	8,711	**56,246**
Other-net	**2,668**	(363)	404	**22,611**
Net cash provided by operating activities	**25,534**	32,780	41,684	**216,390**
Investing activities:				
Capital expenditures	**(55,316)**	(59,018)	(25,377)	**(468,780)**
Payment for purchases of investment securities	**(2,846)**	(2,225)	(3,290)	**(24,119)**
Proceeds from sales and redemption of investment securities	**63**	3,057	600	**534**
Proceeds from sales of property, plant and equipment	**2,081**	180	352	**17,636**
Decrease (increase) in investments in and advances to unconsolidated subsidiaries and associated companies	**(686)**	(1,190)	(3,793)	**(5,814)**
Proceeds from sales of plant for expropriation	**2,363**	3,150	16,987	**20,025**
Proceeds from suspense receipts for expropriation	**207**	275	1,862	**1,754**
Payment for suspense payments for expropriation	**(39)**	(219)		**(330)**
Subsidies from municipal governments	**1,864**	1,629		**15,797**
Payment for long-term prepaid expense		(4,300)		
Other	**(1,875)**	(1,369)	1,729	**(15,890)**
Net cash used in investing activities	**(54,184)**	(60,030)	(10,930)	**(459,187)**
Financing activities:				
Net change in short-term bank loans	**17,633**	4,925	(5,659)	**149,432**
Proceeds from issuance of long-term debt	**51,881**	33,574	7,395	**439,669**
Repayments of long-term debt	**(30,919)**	(13,101)	(24,187)	**(262,025)**
Dividends paid	**(2,895)**	(3,255)	(2,170)	**(24,534)**
Dividends paid to minority interests	**(8,661)**	(2,841)	(2,325)	**(73,398)**
Payment for purchases of treasury stock	**(95)**	(86)	(83)	**(805)**
Other	**4**	372	597	**34**
Net cash provided by (used in) financing activities	**26,948**	19,588	(26,432)	**228,373**
Effect of foreign currency translation adjustments on cash and cash equivalents	**891**	1,797	(88)	**7,551**
Net increase (decrease) in cash and cash equivalents	**(811)**	(5,865)	4,234	**(6,873)**
Cash and cash equivalents of newly consolidated subsidiaries, beginning of year	**420**	3,575	169	**3,560**
Cash and cash equivalents, beginning of year	**14,350**	16,640	12,237	**121,610**
Cash and cash equivalents, end of year	**¥ 13,959**	¥ 14,350	¥ 16,640	**$ 118,297**
Noncash investing and financing activities:				
Assets increased by consolidation of previously unconsolidated subsidiaries	**¥ 2,767**	¥ 330	¥ 678	**$ 23,449**
Liabilities increased by consolidation of previously unconsolidated subsidiaries	**2,775**		277	**23,517**

See notes to consolidated financial statements.

1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements of Daicel Chemical Industries, Ltd. (the "Company") have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations and in conformity with accounting principles generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

On December 27, 2005, the Accounting Standards Board of Japan (the "ASBJ") issued a new accounting standard for the statement of changes in equity, which is effective for fiscal years ending on or after May 1, 2006. The consolidated statement of shareholders' equity, which was previously voluntarily prepared in line with the international accounting practices, is now required under generally accepted accounting principles in Japan ("Japanese GAAP") and has been renamed "the consolidated statement of changes in equity" in the current fiscal year.

In preparing the consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications have been made in the 2006 financial statements to conform to the classifications used in 2007.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which the Company is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥118 to $1, the approximate rate of exchange at March 31, 2007. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

2. Summary of Significant Accounting Policies

a. Consolidation—The consolidated financial statements as of March 31, 2007 include the accounts of the Company and its 53 significant (51 in 2006, 46 in 2005) subsidiaries (together, the "Companies").

During the year ended March 31, 2005, one newly established subsidiary was included in consolidation. One existing subsidiary was included as a result of an increase of its operations.

During the year ended March 31, 2006, two newly established subsidiaries were included in consolidation. Three existing subsidiaries were included as a result of an increase of its operations.

During the year ended March 31, 2007, two existing subsidiaries were included as a result of an increase of its operations.

Under the control or influence concept, those companies in which the Company, directly or indirectly, is able to exercise control over operations are fully consolidated, and those companies over which the Companies have the ability to exercise significant influence are accounted for by the equity method.

Investments in 10 (11 in 2006, 11 in 2005) unconsolidated subsidiaries and 6 (6 in 2006, 6 in 2005) associated companies are accounted for by the equity method. One subsidiary was excluded from the equity method as a result of its liquidation. Investments in the remaining unconsolidated subsidiaries and associated companies are stated at cost. If the equity method of accounting had been applied to the investments in these companies, the effect on the accompanying consolidated financial statements would not be material.

Cost in excess of the net assets of a subsidiary acquired is amortized on a straight-line basis over three years.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Companies and associated companies accounted for by the equity method has been eliminated.

b. Cash Equivalents—Cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value. Cash equivalents include time deposits, certificates of deposits and mutual funds investing in bonds that represent short-term investments, all of which mature or become due within three months of the date of acquisition.

c. **Marketable and Investment Securities**—Marketable and investment securities are classified and accounted for, depending on management's intent, as follows: i) trading securities, which are held for the purpose of earning capital gains in the near term are reported at fair value, and the related unrealized gains and losses are included in earnings, ii) held-to-maturity debt securities, in which the Companies have the positive intent and ability to hold to maturity are reported at amortized cost and iii) available-for-sale securities, which are not classified as either of the aforementioned securities, are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported as a separate component of equity. Non-marketable available-for-sale securities are stated at cost determined by the moving-average method.

All of the Companies' securities are classified as available-for-sale securities.

For other than temporary declines in fair value, investment securities are reduced to net realizable value by a charge to income.

d. **Inventories**—Inventories are substantially stated at cost, determined by the moving average cost method.

e. **Property, Plant and Equipment**—Property, plant and equipment are stated at cost. Depreciation of property, plant and equipment of the Company and its consolidated domestic subsidiaries is computed substantially by the declining-balance method while the straight-line method is applied to buildings acquired after April 1, 1998. Consolidated foreign subsidiaries primarily apply the straight-line method to property, plant and equipment. The range of useful lives is principally from 3 to 75 years for buildings and structures and from 4 to 15 years for machinery and equipment. Property, plant and equipment are carried at cost, less gains deferred on the sale and replacement of certain assets.

f. **Long-lived Assets**—In August 2002, the Business Accounting Council (BAC) issued a Statement of Opinion, *"Accounting for Impairment of Fixed Assets,"* and in October 2003 the ASBJ issued ASBJ Guidance No. 6 *"Guidance for Accounting Standard for Impairment of Fixed Assets."* These new pronouncements were effective for fiscal years beginning on or after April 1, 2005 with early adoption permitted for fiscal years ending on or after March 31, 2004. The Companies adopted the new accounting standard for important of fixed assets as of April 1, 2005. The Companies review its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

g. **Retirement and Pension Plans**—A certain subsidiary records retirement allowances for directors and corporate auditors to state the liability at the amount that would be required if all directors and corporate auditors retired at each balance sheet date. Amounts payable to directors and corporate auditors upon retirement are subject to the approval of shareholders.

Prior to April 1, 2006, no provisions were recorded for retirement allowances for directors and corporate auditors. Effective April 1, 2006, one subsidiary changed its method of accounting for such retirement benefits to the accrual basis. The effect of this change was to decrease income before income taxes and minority interests for the year ended March 31, 2007 by ¥137 million ($1,161 thousand), which included a cumulative effect of ¥174 million ($1,475 thousand) at March 31, 2006. This cumulative effect was included in other expenses in the 2007 consolidated statement of income.

h. **Foreign Currency Transactions**—All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the exchange rates at the balance sheet date. The foreign exchange gains and losses from translation are recognized in the income statement to the extent that they are not hedged by forward exchange contracts.

i. Foreign Currency Financial Statements—The balance sheet accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the current exchange rate as of the balance sheet date except for equity, which is translated at historical rates.

Revenue and expense accounts of consolidated foreign subsidiaries are translated into yen at the average exchange rates.

Differences arising from such translation are shown as "Foreign currency translation adjustments" as a separate component of equity.

j. Presentation of Equity—On December 9, 2005, the ASBJ issued a new accounting standard for presentation of equity. Under this accounting standard, certain items which were previously presented as liabilities are now presented as components of equity. Such items include stock acquisition rights, minority interests, and any deferred gain or loss on derivatives accounted for under hedge accounting. This standard is effective for fiscal years ending on or after May 1, 2006. The consolidated balance sheet as of March 31, 2007 is presented in line with this new accounting standard.

k. Bonuses to Directors and Corporate Auditors—Prior to the fiscal year ended March 31, 2005, bonuses to directors and corporate auditors were accounted for as a reduction of retained earnings in the fiscal year following approval at the general shareholders meeting. The ASBJ issued ASBJ Practical Issues Task Force (PITF) No. 13, *"Accounting Treatment for Bonuses to Directors and Corporate Auditors,"* which encouraged companies to record bonuses to directors and corporate auditors on the accrual basis with a related charge to income, but still permitted the direct reduction of such bonuses from retained earnings after approval of the appropriation of retained earnings.

The ASBJ replaced the above accounting pronouncement by issuing a new accounting standard for bonuses to directors and corporate auditors on November 29, 2005. Under the new accounting standard, bonuses to directors and corporate auditors must be expensed and are no longer allowed to be directly charged to retained earnings. This accounting standard is effective for fiscal years ending on or after May 1, 2006. The companies must accrue bonuses to directors and corporate auditors at the year end to which such bonuses are attributable.

The Company adopted the new accounting standard for bonuses to directors and corporate auditors from the year ended March 31, 2007. The effect of adoption of this accounting standard was to decrease income before income taxes and minority interests for the year ended March 31, 2007 by ¥73 million ($619 thousand).

l. Leases—All leases are accounted for as operating leases. Under Japanese accounting standards for leases, finance leases that are deemed to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the lessee's financial statements.

m. Research and Development—Research and development costs are included in "Cost of sales" and "Selling, general and administrative expenses" as incurred.

n. Income Taxes—The provision for income taxes is computed based on the pretax income included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

o. Appropriations of Retained Earnings—Appropriations of retained earnings are reflected in the financial statements for the following year upon shareholders' approval.

p. Derivatives and Hedging Activities—The Companies use derivative financial instruments, including foreign exchange forward contracts, interest rate swaps and foreign currency swaps as a means of hedging exposure to foreign exchange and interest rate risks. The Companies do not enter into derivatives for trading or speculative purposes.

All derivatives are recognized as either assets or liabilities and measured at fair value, and gains or losses on derivative transactions are recognized in the income statement. For derivatives used for hedging purposes, if such derivatives qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, gains or losses on those derivatives are deferred until maturity of the hedged transactions.

Long-term debt and trade accounts denominated in foreign currencies, for which foreign exchange forward contracts or foreign currency swaps are used to hedge the foreign currency fluctuation, are translated at the contracted rate if the forward contracts or the swap contracts qualify for specific hedge accounting. Interest rate swaps are utilized to hedge interest rate exposures of long-term debt. Swaps that qualify for hedge accounting are measured at market value at the balance sheet date and unrealized gains or losses are deferred until maturity and included in other liabilities or assets.

q. **Per Share Information**—Basic net income per share is computed by dividing net income available to common shareholders, which is more precisely computed than under previous practices, by the weighted-average number of common shares outstanding for the period, retroactively adjusted for stock splits.

Diluted net income per share is not disclosed because the Company has no securities or warrants that may cause an additional issue of common shares.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years including dividends to be paid after the end of the year, retroactively adjusted for stock splits.

r. **New Accounting Pronouncement**

Measurement of Inventories—Under Japanese GAAP, inventories are currently measured either by the cost method, or at the lower of cost or market. On July 5, 2006, the ASBJ issued ASBJ Statement No. 9, *"Accounting Standard for Measurement of Inventories,"* which is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted. This standard requires that inventories held for sale in the ordinary course of business be measured at the lower of cost or net selling value, which is defined as the selling price less additional estimated manufacturing costs and estimated direct selling expenses. The replacement cost may be used in place of the net selling value, if appropriate. The standard also requires that inventories held for trading purposes be measured at the market price.

Lease Accounting—On March 30, 2007, the ASBJ issued ASBJ Statement No. 13, *"Accounting Standard for Lease Transactions,"* which revised the existing accounting standard for lease transactions issued on June 17, 1993.

Under the existing accounting standard, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized, however, other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the note to the lessee's financial statements.

The revised accounting standard requires that all finance lease transactions should be capitalized. The revised accounting standard for lease transactions is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted for fiscal years beginning on or after April 1, 2007.

Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements—Under Japanese GAAP, a company currently can use the financial statements of foreign subsidiaries which are prepared in accordance with generally accepted accounting principles in their respective jurisdictions for its consolidation process unless they are clearly unreasonable. On May 17, 2006, the ASBJ issued ASBJ Practical Issues Task Force (PITF) No. 18, *"Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements."* The new task force prescribes: 1) the accounting policies and procedures applied to a parent company and its subsidiaries for similar transactions and events under similar circumstances should in principle be unified for the preparation of the consolidated financial statements, 2) financial statements prepared by foreign subsidiaries in accordance with either International Financial Reporting Standards or the generally accepted accounting principles in the United States tentatively may be used for the consolidation process, 3) however, the following items should be adjusted in the consolidation process so that net income is accounted for in accordance with Japanese GAAP unless they are not material;

(1) Amortization of goodwill
(2) Actuarial gains and losses of defined benefit plans recognized outside profit or loss
(3) Capitalization of intangible assets arising from development phases
(4) Fair value measurement of investment properties, and the revaluation model for property, plant and equipment, and intangible assets
(5) Retrospective application when accounting policies are changed
(6) Accounting for net income attributable to a minority interest

The new task force is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted.

3. Marketable and Investment Securities

Marketable and Investment securities as of March 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Current:			
Trust fund investments and other	**¥ 25**	¥ 63	**$ 212**
Non-current:			
Equity securities	**¥79,825**	¥75,902	**$676,483**
Government and corporate bonds	**999**	395	**8,466**
Trust fund investments and other	**1,960**	1,657	**16,610**
Total	**¥82,809**	¥78,017	**$701,771**

The carrying amounts and aggregate fair values of investment securities at March 31, 2007 and 2006 were as follows:

	Millions of yen			
	2007			
	Cost	Unrealized gains	Unrealized losses	Fair value
Equity securities	**¥19,734**	**¥57,508**	**¥73**	**¥77,169**
Debt securities	**1,000**		**1**	**999**
Trust fund investments and other	**977**	**605**	**0**	**1,582**

	Millions of yen			
	2006			
	Cost	Unrealized gains	Unrealized losses	Fair value
Equity securities	¥18,061	¥55,024	¥1	¥73,084
Trust fund investments and other	995	693	0	1,688

	Thousands of U.S. dollars			
	2007			
	Cost	Unrealized gains	Unrealized losses	Fair value
Equity securities	$167,237	$487,356	$619	$653,974
Debt securities	8,475		8	8,467
Trust fund investments and other	8,280	5,127	0	13,407

Securities whose fair values are not readily determinable as of March 31, 2007 and 2006 were as follows:

	Carrying Amount		
	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Available-for-sale:			
Equity securities	¥2,656	¥2,796	$22,509
Debt securities	375	420	3,178
Trust fund investments and other	28	30	237
Total	¥3,059	¥3,246	$25,924

Proceeds from sales of available-for-sale securities for the years ended March 31, 2007, 2006 and 2005 were ¥98 million ($831 thousand), ¥3,057 million and ¥600 million, respectively. Gross realized gains and losses on these sales, computed on the moving average cost basis, were ¥3 million ($25 thousand) and ¥0 million ($0 thousand), respectively for the year ended March 31, 2007 and ¥622 million and ¥28 million, respectively for the year ended March 31, 2006 and ¥81 million and ¥1 million, respectively for the year ended March 31, 2005.

The carrying values of debt and other securities by contractual maturities classified as available-for-sale at March 31, 2007 are as follows:

	Millions of yen	Thousands of U.S. dollars
Due in one year or less	¥ 25	$ 212
Due after one year through five years	409	3,466
Due after five years through ten years	140	1,187
Due after ten years	125	1,059
Total	¥699	$5,924

Investments in and advances to unconsolidated subsidiaries and associated companies at March 31, 2007 and 2006 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Investments	¥6,559	¥6,171	$55,585
Advances	1,433	1,225	12,144
Total	¥7,992	¥7,396	$67,729

4. Inventories

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

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Finished products	**¥35,038**	¥28,728	**$296,933**
Semi-finished products and work in process	**13,964**	12,530	**118,339**
Raw materials	**23,130**	15,561	**196,017**
Supplies	**3,490**	2,693	**29,576**
Total	**¥75,622**	¥59,512	**$640,865**

5. Short-term Bank Loans and Long-term Debt

Short-term bank loans were principally represented by bank overdrafts. Weighted average per annual interest rates of short-term bank loans at March 31, 2007 and 2006 were 2.22% and 2.09%, respectively.

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

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
3.0% bonds due 2007		¥ 10,000	
0.84% bonds due 2009	**¥ 10,000**	10,000	**$ 84,746**
2.2% bonds due 2010	**10,000**	10,000	**84,746**
1.6% bonds due 2013	**10,000**	10,000	**84,746**
Unsecured loans from banks and other financial institutions, due through 2017, with interest rates ranging from 0.64% to 6.36% for 2007 (from 0.50% to 6.07% for 2006)	**64,616**	42,185	**547,593**
Collateralized loans from banks and other financial institutions, due through 2014, with interest rates ranging from 0.55% to 5.67% for 2007 (from 0.55% to 5.76% for 2006)	**28,080**	18,803	**237,966**
Total	**122,696**	100,988	**1,039,797**
Less current portion	**(18,715)**	(29,323)	**(158,602)**
Long-term debt, less current portion	**¥103,981**	¥ 71,665	**$ 881,195**

At March 31, 2007, annual maturities of long-term debt were as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars
2008	**¥ 18,715**	**$ 158,602**
2009	**26,754**	**226,729**
2010	**27,287**	**231,246**
2011	**11,666**	**98,864**
2012	**9,186**	**77,847**
2013 and thereafter	**29,088**	**246,509**
Total	**¥122,696**	**$1,039,797**

At March 31, 2007, property, plant and equipment with a total net book value of ¥58,487 million ($495,653 thousand) was pledged as collateral for long-term debt issued in Japan.

The unsecured long-term bank debt of ¥21,142 million ($179,169 thousand) contain the following financial restriction agreement during its payment period. The agreement provides that the amount of shareholder's equity ¥137,300 million ($1,163,559 thousand) at every end of fiscal year and semi-annual interim period.

6. Retirement and Pension Plans

The Company and certain consolidated subsidiaries have lump-sum severance payment plans and non-contributory trusted pension plans for employees. Additionally, the Company has a "Retirement Benefit Trust."

Under most circumstances, employees terminating their employment are entitled to retirement benefits determined based on the rate of pay at the time of termination, years of service and certain other factors. Such retirement benefits are made in the form of a lump-sum severance payment from the Company or from certain consolidated subsidiaries and annuity payments from a trustee. Employees are entitled to larger payments if the termination is involuntary, by retirement at the mandatory retirement age, by death, or by voluntary retirement at certain specific ages prior to the mandatory retirement age.

The liability for employees' retirement benefits at March 31, 2007 and 2006 consisted of the followings:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Projected benefit obligation	**¥ 33,029**	¥ 32,002	**$ 279,906**
Fair value of plan assets	**(27,768)**	(23,659)	**(235,322)**
Unrecognized actuarial loss	**2,550**	(684)	**21,610**
Net liability	**7,811**	7,659	**66,194**
Prepaid benefit costs	**743**	235	**6,297**
Liability for retirement benefit	**¥ 8,554**	¥ 7,894	**$ 72,491**

The components of net periodic benefit costs for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Service cost	**¥1,891**	¥1,635	**$16,025**
Interest cost	**585**	561	**4,958**
Expected return on plan assets	**(312)**	(256)	**(2,644)**
Recognized actuarial loss	**192**	327	**1,627**
Past period service cost of employees' retirement benefit		1,190	
Net periodic benefit costs	**¥2,356**	¥3,457	**$19,966**

Past period service cost of employees' retirement benefit, ¥1,190 million ($10,171 thousand) (included in other expense) was caused by the revision of the calculation premises for employees' retirement in past years.

Assumptions used for the years ended March 31, 2007 and 2006 were set forth as follows:

	2007	2006
Discount rate	**2.0%**	2.0%
Expected rate of return on plan assets	**1.0%**	1.0%
Recognition period of actuarial gain/loss	**10 years**	10 years

Retirement allowances for directors and corporate auditors are paid subject to approval of the shareholders in accordance with the Japanese Corporate Law. The Company recorded a liability for its unfunded retirement allowance plan covering all of its directors and corporate auditors. The annual provisions for retirement allowances for directors and corporate auditors for the years ended March 31, 2007 was ¥137 million ($1,161 thousand).

7. Equity

On and after May 1, 2006, a new corporate law (the "Corporate Law") became effective, which reformed and replaced the Code with various revisions that would, for the most part, be applicable to events or transactions which occur on or after May 1, 2006 and for the fiscal years ending on or after May 1, 2006. The significant changes in the Corporate Law that affect financial and accounting matters are summarized below;

(a). Dividends

Under the Corporate Law, companies can pay dividends at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders meeting. For companies that meet certain criteria such as; (1) having the Board of Directors, (2) having independent auditors, (3) having the Board of Corporate Auditors, and (4) the term of service of the directors is prescribed as one year rather than two years of normal term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends in kind) if the company has prescribed so in its articles of incorporation. However, the Company cannot do so because it does not meet all the above criteria.

The Corporate Law permits companies to distribute dividends-in kind (non-cash assets) to shareholders subject to a certain limitation and additional requirements.

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. Under the Code, certain limitations were imposed on the amount of capital surplus and retained earnings available for dividends. The Corporate Law also provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

(b). Increases/decreases and transfer of common stock, reserve and surplus

The Corporate Law requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus) depending on the equity account charged upon the payment of such dividends until the total of aggregate amount of legal reserve and additional paid-in capital equals 25% of the common stock. Under the Code, the aggregate amount of additional paid-in capital and legal reserve that exceeds 25% of the common stock may be made available for dividends by resolution of the shareholders. Under the Corporate Law, the total amount of additional paid-in capital and legal reserve may be reversed without limitation of such threshold. The Corporate Law also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts under certain conditions upon resolution of the shareholders.

(c). Treasury stock and treasury stock acquisition rights

The Corporate Law also provides for companies to purchase treasury stock and dispose of such treasury stock by resolution of the Board of Directors. The amount of treasury stock purchased cannot exceed the amount available for distribution to the shareholders which is determined by specific formula.

Under the Corporate law, stock acquisition rights, which were previously presented as a liability, are now presented as a separate component of shareholders' equity.

The Corporate Law also provides that companies can purchase both treasury stock acquisition rights and treasury stock. Such treasury stock acquisition rights are presented as a separate component of shareholders' equity or deducted directly from stock acquisition rights.

On December 9, 2005, the ASBJ issued a new accounting standard for presentation of equity. Under this accounting standard, certain items which were previously presented as liabilities are now presented as components of equity. Such items include stock acquisition rights, minority interest, and any deferred gain or loss on derivatives accounted for under hedge accounting. This standard is effective for fiscal years endings on or after May 1, 2006.

8. Income Taxes

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in normal effective statutory tax rates of approximately 41%, 41% and 41% for the years ended March 31, 2007, 2006 and 2005. Foreign subsidiaries are subject to income tax of the countries in which they operate.

A reconciliation between the normal effective statutory tax rate for the years ended March 31, 2007, 2006 and 2005 and the actual effective tax rate reflected in the accompanying consolidated statements of income was as follows:

	2007	2006	2005
Normal effective statutory tax rate	**41%**	41%	41%
Expenses not deductible for income tax purposes		1	1
Current operating losses of subsidiaries		3	
Loss on investments in subsidiaries			(1)
Equity in earnings of associated companies		(1)	(1)
Tax credit primarily for research and development expenses	**(3)**	(3)	(2)
Return tax	**(2)**		
Other-net		(2)	(2)
Actual effective tax rate	**36%**	39%	36%

The tax effects of significant temporary differences and tax loss carryforwards which resulted in deferred tax assets and liabilities at March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Deferred tax assets:			
Accrued enterprise taxes	**¥ 616**	¥ 595	**$ 5,220**
Accrued bonuses	**1,728**	1,626	**14,644**
Liabilities for retirement benefits	**8,034**	7,958	**68,085**
Investment securities	**2,416**	2,388	**20,475**
Tax loss carryforwards	**1,023**	1,006	**8,669**
Intercompany profits	**5,209**	4,634	**44,144**
Other	**3,270**	2,379	**27,712**
Less valuation allowance	**(865)**	(1,140)	**(7,331)**
Deferred tax assets	**¥21,431**	¥19,446	**$181,618**
Deferred tax liabilities:			
Unrealized gain on available-for-sale securities	**¥23,552**	¥22,755	**$199,593**
Tax purpose reserves regulated by Japanese tax law	**988**	869	**8,373**
Undistributed earnings of foreign subsidiaries	**3,583**	2,508	**30,364**
Securities contributed to employees' retirement benefit trust	**4,603**	4,585	**39,009**
Other	**2,320**	1,710	**19,661**
Deferred tax liabilities	**¥35,046**	¥32,427	**$297,000**
Net deferred tax liabilities	**¥13,615**	¥12,981	**$115,382**

9. Research and Development Costs

Research and development costs included in "Cost of sales" and "Selling, general and administrative expenses" were ¥11,717 million ($99,297 thousand), ¥11,221 million and ¥11,219 million for the years ended March 31, 2007, 2006 and 2005, respectively.

10. Net Income Per Share

The computation of net income per common share is based on the weighted average number of shares outstanding. The average number of common shares in the computation was 361,892,421, 361,760,918 and 361,650,372 for the years ended March 31, 2007, 2006 and 2005, respectively.

11. Leases

(Lessee)

Finance Leases:

Total lease payments under finance leases that do not deem to transfer ownership of the leased property to the lessee were ¥339 million ($2,873 thousand), ¥289 million and ¥356 million for the years ended March 31, 2007, 2006 and 2005, respectively.

Pro forma information of leased property under finance leases that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen			
As of March 31, 2007	Buildings and structures	Machinery and equipment	Other assets	Total
Acquisition cost	**¥272**	**¥2,099**		**¥2,371**
Accumulated depreciation	**184**	**1,111**		**1,295**
Net leased property	**¥ 88**	**¥ 988**		**¥1,076**

	Thousands of U.S. dollars			
As of March 31, 2007	Buildings and structures	Machinery and equipment	Other assets	Total
Acquisition cost	**$2,305**	**$17,788**		**$20,093**
Accumulated depreciation	**1,559**	**9,415**		**10,974**
Net leased property	**$ 746**	**$ 8,373**		**$ 9,119**

	Millions of yen			
As of March 31, 2006	Buildings and structures	Machinery and equipment	Other assets	Total
Acquisition cost	¥196	¥1,925	¥4	¥2,125
Accumulated depreciation	102	806	4	912
Net leased property	¥ 94	¥1,119	¥0	¥1,213

The amount of acquisition cost under finance leases includes the imputed interest expense.

Obligations under finance leases as of March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Due within one year	**¥ 289**	¥ 300	**$2,449**
Due after one year	**786**	913	**6,661**
Total	**¥1,075**	¥1,213	**$9,110**

The amount of obligations under finance leases includes the imputed interest expense.

Depreciation expense, which is not reflected in the accompanying consolidated statements of income, computed by the straight-line method was ¥339 million ($2,873 thousand), ¥289 million and ¥356 million for the years ended March 31, 2007, 2006 and 2005, respectively.

Operating Leases:

Obligations under non-cancelable operating leases as of March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Due within one year	**¥340**	¥105	**$2,881**
Due after one year	**369**	14	**3,127**
Total	**¥709**	¥119	**$6,008**

The amount of obligations under operating leases includes imputed interest expense.

There is no impairment loss allocated to leased assets.

(Lessor)

Finance Leases:

These finance leases that do not transfer ownership of leased property to the lessee are subleases.

Future rental income under such finance leases as of March 31, 2007 and 2006 was as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Due within one year	**¥2**		**$17**
Due after one year	**5**		**42**
Total	**¥7**		**$59**

The amount of future rental income under subleases includes the imputed interest income.

12. Derivatives

The Companies enter into foreign exchange forward contracts and foreign currency swaps, in the normal course of business, to reduce the exposure to fluctuations in foreign exchange rates. The Companies also enter into interest rate swap agreements as a means of managing interest rate exposure. The Companies do not hold or issue derivatives for trading or speculative purposes.

Foreign exchange forward contracts, interest rate swaps and foreign currency swaps are subject to market risk, which is the exposure created by potential fluctuations in market conditions. Because the counterparties to the Companies' derivatives are limited to major international financial institutions, the Companies do not anticipate any losses arising from credit risk. Derivative transactions entered into by the Companies have been made in accordance with internal policies which regulate the authorization of such transactions.

The Companies had the following derivatives contracts outstanding at March 31, 2007 and 2006:

	Millions of yen						Thousands of U.S. dollars		
	2007			2006			2007		
	Contract amount	Fair value	Unrealized gain (loss)	Contract amount	Fair value	Unrealized gain (loss)	Contract amount	Fair value	Unrealized gain (loss)
Foreign currency forward contracts:									
Selling U.S.$	**¥3,273**	**¥3,313**	**¥ (40)**	¥ 3,952	¥3,984	¥ (32)	**$27,737**	**$28,076**	**$ (339)**
Selling Thai Baht				113	114	(1)			
Buying U.S.$	**466**	**471**	**5**				**3,949**	**3,991**	**42**
Foreign currency swaps:									
Receiving Japanese yen, paying U.S.$	**2,500**	**(166)**	**(166)**	2,500	(167)	(167)	**21,186**	**(1,407)**	**(1,407)**
Interest rate swaps:									
Fixed rate payment, floating rate receipt				15,000	(67)	(67)			

Foreign exchange forward contracts or interest rate swaps or foreign currency swaps which qualify for hedge accounting and such amounts which are assigned to the associated assets and liabilities and are recorded on the balance sheet are excluded from disclosure of market value information.

The contract or notional amounts above do not represent the amounts exchanged by the parties and do not measure the Companies' exposure to credit or market risk.

13. Related Party Transactions

The Company sells Cellulose acetate and polymer to FUJIFILM Corporation whose president has served as one of the Company's directors since June, 2005. On October 2, 2006, FUJIFILM Corporation was founded and succeeded the business operation of Fuji Photo Film Co., Ltd.

The sales to FUJIFILM Corporation (Fuji Photo Film Co., Ltd.) for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Sales	**¥16,611**	¥9,675	**$140,771**

These balances due to FUJIFILM Corporation (Fuji Photo Film Co., Ltd.) at March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	**2007**
Notes and accounts receivable	**¥3,422**	¥3,002	**$29,000**

14. Municipal Government Subsidies

The Companies received various incentives from municipal governments in the form of subsidies for purchases of property, plant and equipment. Such subsidies were accounted for as income as received. The same amount is charged to income and deducted from the cost of property, plant and equipment when the property, plant and equipment subject to the subsidies are acquired.

15. Expropriation

During the year ended March 31, 2005, in connection with expropriations for public expressway construction, the Companies signed an agreement with Hanshin Expressway Public Corporation to sell certain land and certain facilities related to its Sakai Plant which produced a gain for the Companies of ¥26,388 million ($246,617 thousand). Under Japanese tax regulations, the Companies are allowed to defer this gain by recording it as a deferred gain under long-term liabilities. When replacement property and plant facilities are acquired, the deferred gain is reversed and the same amount is credited against the cost of such property, plant and equipment.

16. Contingent Liabilities

Contingent liabilities at March 31, 2007 for loans guaranteed amounted to ¥5,243 million ($44,432 thousand). Loans guaranteed are principally those of unconsolidated subsidiaries, associated companies and employees.

Contingent liabilities at March 31, 2007 for cession of a trade notes amounted to ¥366 million ($3,102 thousand).

17. Subsequent Event

The following plan for appropriations of retained earnings for the year ended March 31, 2007 was approved at the Shareholders' General Meeting of the Company held on June 28, 2007:

	Millions of yen	Thousands of U.S. dollars
Cash dividends, ¥4 ($0.03) per share	¥1,448	$12,271

18. Segment Information

Information about operations in industry segments, geographic segments and sales to foreign customers of the Companies for the years ended March 31, 2007, 2006 and 2005 is as follows:

I. Operations in Industry Segments

	Millions of yen							
Year ended March 31, 2007	Cellulosic derivatives	Organic chemicals	Plastics and films	Pyrotechnic devices	Functional products and others	Total	Corporate and eliminations	Consolidated
Sales to outside customers	¥ 63,501	¥ 93,839	¥161,881	¥55,496	¥ 6,706	¥381,423		¥381,423
Intersegment sales	2,355	14,126	29		11,876	28,386	¥ (28,386)	
Total sales	65,856	107,965	161,910	55,496	18,582	409,809	(28,386)	381,423
Total cost and expenses	54,226	96,641	147,135	49,449	17,657	365,108	(20,084)	345,024
Operating income	¥ 11,630	¥ 11,324	¥ 14,775	¥ 6,047	¥ 925	¥ 44,701	¥ (8,302)	¥ 36,399
Total asset	¥118,803	¥ 93,690	¥159,234	¥59,965	¥ 9,704	¥441,396	¥106,036	¥547,432
Depreciation	4,549	5,881	7,473	4,393	327	22,623	646	23,269
Impairment loss on fixed assets			66			66	73	139
Capital investments	32,267	5,499	4,677	4,227	224	46,894	5,164	52,058

	Thousands of U.S. dollars							
Year ended March 31, 2007	Cellulosic derivatives	Organic chemicals	Plastics and films	Pyrotechnic devices	Functional products and others	Total	Corporate and eliminations	Consolidated
Sales to outside customers	$ 538,144	$795,246	$1,371,873	$470,305	$ 56,830	$3,232,398		$3,232,398
Intersegment sales	19,957	119,712	246		100,644	240,559	$(240,559)	
Total sales	558,101	914,958	1,372,119	470,305	157,474	3,472,957	(240,559)	3,232,398
Total cost and expenses	459,542	818,991	1,246,907	419,059	149,636	3,094,135	(170,203)	2,923,932
Operating income	$ 98,559	$ 95,967	$ 125,212	$ 51,246	$ 7,838	$ 378,822	$ (70,356)	$ 308,466
Total asset	$1,006,805	$793,983	$1,349,441	$508,178	$ 82,237	$3,740,644	$ 898,610	$4,639,254
Depreciation	38,551	49,839	63,331	37,229	2,771	191,721	5,475	197,196
Impairment loss on fixed assets			559			559	619	1,178
Capital investments	273,449	46,602	39,636	35,822	1,898	397,407	43,763	441,170

Year ended March 31, 2006	Millions of yen							
	Cellulosic derivatives	Organic chemicals	Plastics and films	Pyrotechnic devices	Functional products and others	Total	Corporate and eliminations	Consolidated
Sales to outside customers	¥55,899	¥84,435	¥142,556	¥44,090	¥ 8,540	¥335,520		¥335,520
Intersegment sales	2,222	10,989	37		10,267	23,515	¥ (23,515)	
Total sales	58,121	95,424	142,593	44,090	18,807	359,035	(23,515)	335,520
Total cost and expenses	47,290	85,947	129,421	37,473	17,490	317,621	(15,671)	301,950
Operating income	¥10,831	¥ 9,477	¥ 13,172	¥ 6,617	¥ 1,317	¥ 41,414	¥ (7,844)	¥ 33,570
Total asset	¥86,828	¥82,909	¥149,738	¥52,786	¥10,908	¥383,169	¥100,300	¥483,469
Depreciation	4,131	6,426	6,887	3,434	290	21,168	780	21,948
Impairment loss on fixed assets		895	15			910	240	1,150
Capital investments	30,154	5,461	6,960	12,678	340	55,593	6,358	61,951

Year ended March 31, 2005	Millions of yen							
	Cellulosic derivatives	Organic chemicals	Plastics and films	Pyrotechnic devices	Functional products and others	Total	Corporate and eliminations	Consolidated
Sales to outside customers	¥50,132	¥79,087	¥133,390	¥36,605	¥ 7,121	¥306,335		¥306,335
Intersegment sales	1,942	11,083	49		10,082	23,156	¥ (23,156)	
Total sales	52,074	90,170	133,439	36,605	17,203	329,491	(23,156)	306,335
Total cost and expenses	42,409	83,310	120,430	30,063	16,723	292,935	(15,153)	277,782
Operating income	¥ 9,665	¥ 6,860	¥ 13,009	¥ 6,542	¥ 480	¥ 36,556	¥ (8,003)	¥ 28,553
Total asset	¥57,894	¥82,321	¥135,949	¥39,730	¥10,323	¥326,217	¥ 87,276	¥413,493
Depreciation	4,127	7,062	6,770	3,069	348	21,376	840	22,216
Capital investments	4,398	5,209	10,583	4,449	190	24,829	850	25,679

Cellulosic derivatives include cellulose acetate, acetate tow for cigarette filters and water-soluble polymers. Organic chemicals include acetic acid and its derivatives, fine chemical products and optical resolution columns. Plastics and films include SAN and ABS resins and alloys, and packaging and performance films. Pyrotechnic devices include ammunition, solid propellants and rocket propulsion, aircrew emergency-escape systems and inflators for automobile air bag safety equipment. Functional products include membranes.

Cost and expenses of Corporate and Eliminations for the years ended March 31, 2007, 2006 and 2005 included unallocated corporate costs of ¥8,302 million ($70,356 thousand), ¥7,844 million and ¥8,003 million, respectively. The unallocated corporate costs consisted primarily of research and development costs and headquarters administration costs.

Assets of Corporate and Eliminations at March 31, 2007, 2006 and 2005 included ¥109,500 million ($927,966 thousand), ¥103,234 million and ¥89,803 million of corporate assets, respectively, consisting primary of cash and cash equivalents, investment in securities, research and development-related equipment and headquarters administration-related assets.

II. Geographical Segments

Year ended March 31, 2007	Millions of yen					
	Japan	Asia	Other	Total	Corporate and eliminations	Consolidated
Sales to outside customers	**¥290,832**	**¥66,187**	**¥24,404**	**¥381,423**		**¥381,423**
Intersegment sales	**46,302**	**9,423**	**1,741**	**57,466**	**¥ (57,466)**	
Total sales	**337,134**	**75,610**	**26,145**	**438,889**	**(57,466)**	**381,423**
Operating expenses	**301,514**	**67,462**	**25,212**	**394,188**	**(49,164)**	**345,024**
Operating income	**¥ 35,620**	**¥ 8,148**	**¥ 933**	**¥ 44,701**	**¥ (8,302)**	**¥ 36,399**
Total assets	**¥354,702**	**¥77,617**	**¥27,264**	**¥459,583**	**¥ 87,849**	**¥547,432**

Year ended March 31, 2007	Thousands of U.S. dollars					
	Japan	Asia	Other	Total	Corporate and eliminations	Consolidated
Sales to outside customers	**$2,464,678**	**$560,907**	**$206,813**	**$3,232,398**		**$3,232,398**
Intersegment sales	**392,390**	**79,856**	**14,754**	**487,000**	**$ (487,000)**	
Total sales	**2,857,068**	**640,763**	**221,567**	**3,719,398**	**(487,000)**	**3,232,398**
Operating expenses	**2,555,203**	**571,712**	**213,661**	**3,340,576**	**(416,644)**	**2,923,932**
Operating income	**$ 301,865**	**$ 69,051**	**$ 7,906**	**$ 373,822**	**$ (70,356)**	**$ 308,466**
Total assets	**$ 3,005,949**	**$657,771**	**$231,051**	**$3,894,771**	**$ 744,483**	**$4,639,254**

Year ended March 31, 2006	Millions of yen					
	Japan	Asia	Other	Total	Corporate and eliminations	Consolidated
Sales to outside customers	¥264,621	¥54,480	¥16,419	¥335,520		¥335,520
Intersegment sales	42,455	7,964	460	50,879	¥(50,879)	
Total sales	307,076	62,444	16,879	386,399	(50,879)	335,520
Operating expenses	273,778	55,125	16,082	344,985	(43,035)	301,950
Operating income	¥ 33,298	¥ 7,319	¥ 797	¥ 41,414	¥ (7,844)	¥ 33,570
Total assets	¥308,288	¥69,577	¥19,885	¥397,750	¥ 85,719	¥483,469

Year ended March 31, 2005	Millions of yen					
	Japan	Asia	Other	Total	Corporate and eliminations	Consolidated
Sales to outside customers	¥244,897	¥48,754	¥12,684	¥306,335		¥306,335
Intersegment sales	39,185	6,081	315	45,581	¥(45,581)	
Total sales	284,082	54,835	12,999	351,916	(45,581)	306,335
Operating expenses	254,159	49,447	11,755	315,361	(37,579)	277,782
Operating income	¥ 29,923	¥ 5,388	¥ 1,244	¥ 36,555	¥ (8,002)	¥ 28,553
Total assets	¥273,985	¥54,553	¥11,594	¥340,132	¥ 73,361	¥413,493

Major countries or areas in the categories Asia and Other are as follows:

Asia: China, Singapore, Hong-Kong, Thailand, Taiwan, Malaysia

Other: North America, Europe

Cost and expenses of Corporate and Eliminations for the years ended March 31, 2007, 2006 and 2005 included unallocated corporate costs of ¥8,302 million ($70,356 thousand), ¥7,844 million and ¥8,003 million, respectively. The unallocated corporate costs consisted primarily of research and development costs and headquarters administration costs.

Assets of Corporate and Eliminations at March 31, 2007, 2006 and 2005 included ¥109,500 million ($927,966 thousand), ¥103,234 million and ¥89,803 million of corporate assets, respectively, consisting primary of cash and cash equivalents, investment in securities, research and development-related equipment and headquarters administration-related assets.

III. Sales to Foreign Customers

Sales to foreign customers for the years ended March 31, 2007, 2006 and 2005 consisted of the following:

	Millions of yen			Thousands of U.S. dollars
	2007	2006	2005	**2007**
Asia	**¥ 92,185**	¥ 76,705	¥70,249	**$ 781,229**
Other	**43,032**	31,336	24,037	**364,678**
Total	**¥135,217**	¥108,041	¥94,286	**$1,145,907**

Major countries or areas in the categories Asia and Other are as follows:

Asia: China, Hong Kong, Thailand, Korea, Singapore, Taiwan

Other: Europe, North America, Africa, Oceania, the Middle East, Latin America

Deloitte.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of Daicel Chemical Industries, Ltd.:

We have audited the accompanying consolidated balance sheets of Daicel Chemical Industries, Ltd. and consolidated subsidiaries as of March 31, 2007 and 2006, and the related consolidated statements of income, changes in equity, and cash flows for each of the three years in the period ended March 31, 2007, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Daicel Chemical Industries, Ltd. and consolidated subsidiaries as of March 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2007, in conformity with accounting principles generally accepted in Japan.

Our audits also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 1. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

Deloitte Touche Tohmatsu

June 28, 2007

Principal Subsidiaries and Affiliates *(As of July 31, 2007)*

Domestic Operations

	Paid-in capital (Millions of yen)	The Company's equity ownership (%)	Principal business
Kyodo Sakusan Co., Ltd.	3,000	54	Manufacture and sale of acetic acid Joint-venture company with Mitsubishi Gas Chemical Co., Inc.; Denki Kagaku Kogyo K.K.; Chisso Corporation; and Kyowa Hakko Chemical Co., Ltd.
Dainichi Chemical Corp.	450	100	Manufacture and sale of industrial-use coating resins, non-tin anti-stain compounds, and fine chemicals
Polyplastics Co., Ltd.	3,000	55	Manufacture and sale of polyacetal resin, polybutylene terephthalate (PBT) resin, liquid crystal polymer, and polyphenylene sulfide resin Joint-venture company with Ticona Limited Liability Company of the United States
WinTech Polymer Ltd.*1	2,000	33	Manufacture and sale of polybutylene terephthalate (PBT) resin and glass fiber-reinforced PET (FR-PET) resin Joint-venture company with Teijin Limited
Dainippon Plastics Co., Ltd.	859	60	Manufacture and sale of plastic products
Daipla System Technology Co., Ltd.*2	120	60	Manufacture and sale of molds for injection molding
Sheedom Co., Ltd.*3	120	60	Manufacture and sale of plastic sheet products
Daicel Polymer Ltd.	100	100	Manufacture and sale of SAN resin, ABS resin, high-performance polymer alloy, and polystyrene sheet
Daicel-Degussa Ltd.	340	50	Manufacture and sale of polyamide 12 resin Joint-venture company with Degussa Japan Co., Ltd.
Daicel Pack Systems, Ltd.	45	100	Manufacture and sale of paper and plastic buffers, vacuum- and pressure-molded plastics, and industrial and food packaging
Daicel Value Coating Ltd.	40	100	Manufacture and sale of barrier films Custom coating business
Mikuni Plastics Co., Ltd.	315	100	Manufacture, processing, and sale of various plastic products
Daicel Novafoam Ltd.	97	100	Manufacture and sale of foamed plastics
Daicel Safety Systems Inc.	80	100	Manufacture of inflators for automobile air bags
Japan Shotshell Ltd.	150	100	Manufacture and sale of shotgun shells for sport shooting and hunting
Daicel Finance Ltd.	1,000	100	Supervision and implementation of finance and asset management operations for Daicel Group companies
Daicel Logistics Service Co., Ltd.	267	100	Warehousing and transportation
Daicen Membrane-Systems Ltd.	30	55	Manufacture and sale of separation membranes, including ultrafiltration membrane modules, and design, manufacture, and sale of equipment and systems related to ultrafiltration membrane modules
Daicel FineChem Ltd.	70	100	Sale of water-soluble polymers, synthetic resins, and other industrial products, and manufacture, processing, and sale of resin-based construction materials as well as floor coverings and exterior furnishings Manufacture and sale of celluloid, acetate plastics products, and household products

*1 60% owned by Polyplastics Co., Ltd.
*2, 3 100% owned by Dainippon Plastics Co., Ltd.

International Operations

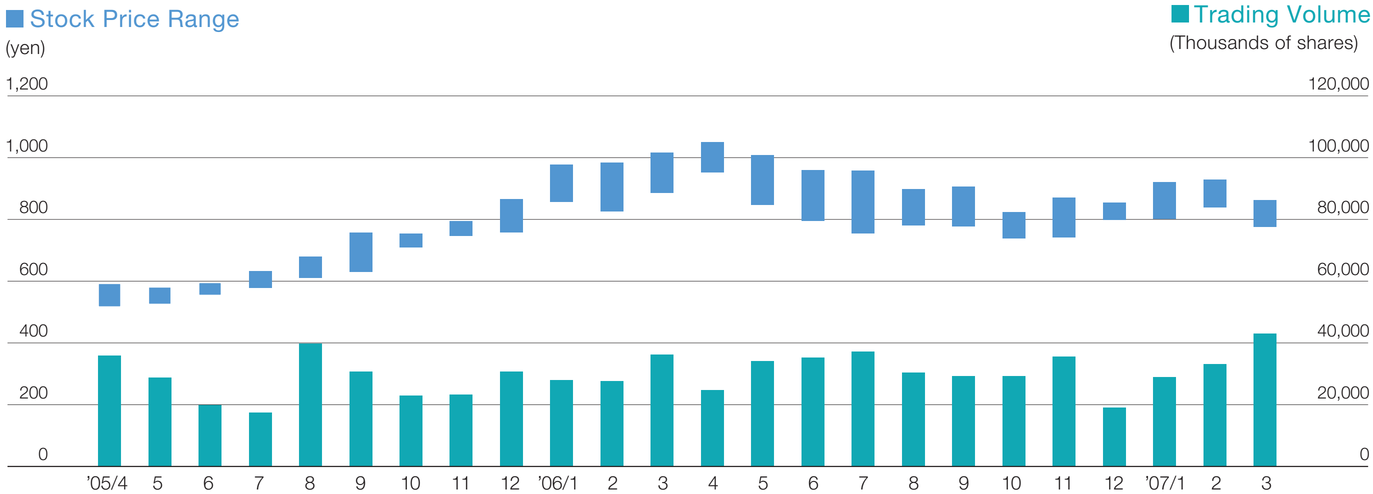
	Paid-in capital	The Company's equity ownership (%)	Principal business
Ningbo Da-An Chemical Industries Co., Ltd.*4	RMB272mil	30	Manufacture and sale of cellulose acetate and acetic anhydride
Xi'an Huida Chemical Industries Co., Ltd.*4	RMB88mil	30	Manufacture and sale of acetate tow for cigarette filters
Chiral Technologies, Inc.	US$8.8mil	100	Sale of chiral separation columns and provision of technical services related to optical active compounds
Chiral Technologies Europe S.A.S.	€2.1mil	100	Sale of chiral separation columns and provision of technical services related to optical active compounds
Daicel Nanning Food Ingredients Co., Ltd.*5	US$33.61mil	100	Manufacture and sale of sorbic acid and potassium sorbate
Polyplastics Taiwan Co., Ltd.*6	NT$1,590mil	41	Manufacture and sale of engineering plastics
Polyplastics Asia Pacific Sdn. Bhd.*7	RM159mil	55	Manufacture and sale of engineering plastics
PTM Engineering Plastics (Nantong) Co., Ltd.*8	RMB386mil	39	Manufacture and sale of engineering plastics Joint-venture company with Mitsubishi Gas Chemical Co., Inc.; Korea Engineering Plastics Co., Ltd.; and Ticona Limited Liability Company
Shanghai Daicel Polymers, Ltd.*9	RMB76.52mil	100	Sale and compounding of plastics
Daicel Polymer (Hong Kong) Ltd.*10	HK$1.0mil	100	Manufacture and sale of SAN resin, ABS resin, high-performance polymer alloy, and polystyrene sheet
Daicel Polymer Trading (Shanghai) Ltd.*11	RMB1.66mil	100	Sale of compound resin, polystyrene sheet and other chemical products
Topas Advanced Polymers GmbH*12	€0.1mil	80	Manufacture, sale and research of cyclic olefin copolymer
Topas Advanced Polymers, Inc.*13	US$0.01mil	80	Sale of cyclic olefin copolymer
Daicel Safety Systems America, LLC*14	US$15mil	66	Manufacture and sale of inflators for automobile air bags Joint-venture company with TG North America Corporation
Daicel Safety Systems Europe Sp. z o. o.	PLN5mil	100	Manufacture and sale of inflators for automobile air bags
Daicel Safety Systems (Jiangsu) Co.,Ltd.*15	US$15mil	100	Manufacture and sale of inflators for automobile air bags
Daicel Safety Systems (Thailand) Co., Ltd.	THB270mil	100	Manufacture and sale of inflators for automobile air bags
Daicel Safety Technologies America,Inc	US$8.5mil	100	Manufacture of inflator components for automobile air bags
Daicel Safety Technologies (Thailand) Co., Ltd.	THB800mil	100	Manufacture of inflator components for automobile air bags
Daicel Chemical (China) Investment Co., Ltd.	US$47.11mil	100	Management of Manufacturing and marketing operations in China
Daicel Chemical (Asia) Pte. Ltd.	S$9.59mil	100	Management of marketing operations in Southeast Asia
Daicel (Hong Kong) Ltd.	HK$1.5mil	100	Management of marketing operations in Hong Kong and southern China
Daicel (U.S.A.), Inc.	US$51.9mil	100	Management of marketing operations in North America
Daicel (Europa) GmbH	€0.15mil	100	Management of marketing operations in Europe

*4 30% owned by Daicel Chemical (China) Investment Co., Ltd.
*5, *15 100% owned by Daicel Chemical (China) Investment Co., Ltd.
*6 75% owned by Polyplastics Co., Ltd.
*7 100% owned by Polyplastics Co., Ltd.
*8 70% owned by Polyplastics Co., Ltd.
*9 90% owned by Daicel Chemical Industries, Ltd and 10% owned by Daicel Chemical (China) Investment Co., Ltd.
*10 100% owned by Daicel Polymer Ltd.
*11 50% owned by Daicel Polymer Ltd. and 50% owned by Daicel Polymer (Hong Kong) Ltd.
*12 55% owned by Daicel Chemical Industries, Ltd and 45% owned by Polyplastics Co., Ltd.
*13 100% owned by Topas Advanced Polymers GmbH
*14 66% owned by Daicel (U.S.A.), Inc.

Corporate Data *(As of March 31, 2007)*

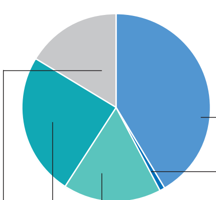
Incorporated	September 8, 1919
Common Stock	
Authorized:	1,450,000,000 shares
Issued:	364,942,682 shares
Capital:	¥36,275 million
Listings:	Tokyo Stock Exchange and Osaka Securities Exchange
Transfer Agent:	The Chuo Mitsui Trust & Banking Co., Ltd. 33-1, Shiba 3-chome, Minato-ku, Tokyo 105-8574, Japan
Number of Shareholders:	23,502
Independent Auditor	Deloitte Touche Tohmatsu
Osaka Head Office (As of August, 2007)	Mainichi Intecio., 4-5, Umeda 3-chome, Kita-ku, Osaka 530-0001, Japan Tel: +81-6-6342-6111 Fax: +81-6-6342-6118 *The Osaka Sales Office was integrated into the Osaka Head Office along with the transfer of the Osaka Head Office to a new location.
Tokyo Head Office (As of August, 2007)	2-18-1, Konan Minato-ku, Tokyo 108-8230, Japan Tel: +81-3-6711-8111 Fax: +81-3-6711-8100

Stock Price Range & Trading Volume



Note: Share price and trading volume reflect Company shares traded on the Tokyo Stock Exchange.

Composition of Stockholders



	Thousands of shares	%
Financial institutions	150,950	41.4
Securities companies	3,149	0.9
Other dcmestic corporatins	61,441	16.8
Foregin investors	89,890	24.6
Individual & other investors	59,511	16.3

Note: Treasury stock is included in the "Individual & other investors" category.

Major Shareholders (Top10)

	Number of shares (unit: 1,000 shares)	% of total shares issued
Japan Trustee Services Bank, Ltd. (Trust Account)	33,542	9.19
The Master Trust Bank of Japan, Ltd. (Trust Account)	27,101	7.43
Nippon Life Insurance Company	16,813	4.61
Toyota Motor Corporation	15,000	4.11
Fuji Photo Film Co., Ltd.	10,915	2.99
Mitsui Sumitomo Insurance Co., Ltd.	9,003	2.47
Nippon Life Insurance Company (Special pension fund account)	8,354	2.29
Mitsui & Co., Ltd.	7,560	2.07
Sumitomo Mitsui Banking Corporation	7,096	1.94
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	6,503	1.78

DAICEL CHEMICAL INDUSTRIES, LTD.

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