SUMITOMO BAKELITE CO., LTD.

ANNUAL REPORT 2004

Profile

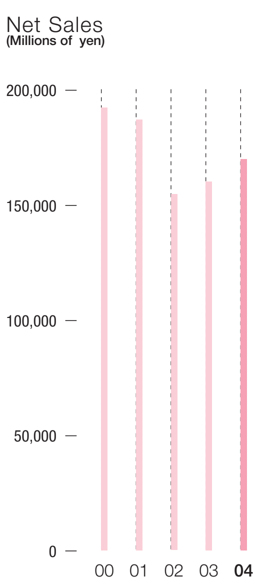
The phenolic resin Bakelite, one of the oldest plastics in use today, was developed about 100 years ago by a Belgian-American, Dr. Leo H. Baekeland. Shortly thereafter, Sumitomo Bakelite became the first Japanese company to succeed in the industrial production of the material. Ever since, the Company has led the plastics processing field, providing customers with an ever-widening variety of superior products and technologies. Today, Sumitomo Bakelite is moving decisively to develop more sophisticated technologies that will provide current and future generations with the highest quality products available.

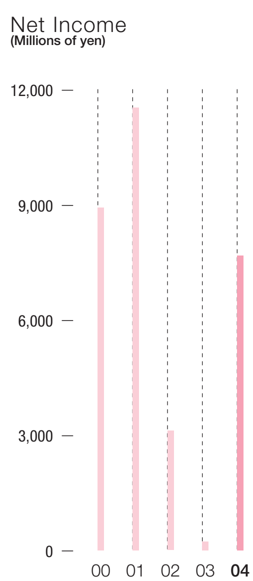
Contents

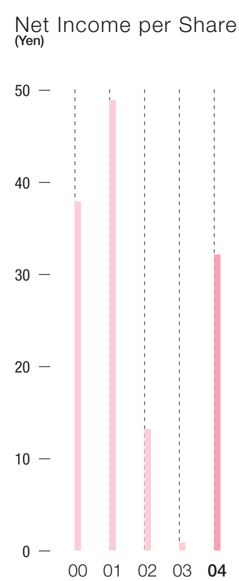
Financial Highlights

Years ended March 31	Millions of yen			Thousands of U.S. dollars (Note)
	2004	2003	2002	2004
Net Sales	¥ 170,249	¥ 160,379	¥ 154,771	$ 1,610,681
Net Income	7,702	255	3,122	72,867
Total Assets	244,712	198,320	209,512	2,315,156
Shareholders' Equity	117,433	114,442	121,978	1,111,003
	Yen			U.S. dollars (Note)
Net Income per Share	¥ 32.14	¥ 0.87	¥ 13.18	$ 0.30
Diluted Net Income per Share	29.28	–	12.33	0.28
Cash Dividends per Share	10.00	10.00	10.00	0.09

Note: U.S. dollar amounts are translated from yen at the rate of ¥105.7 to US$1, the approximate exchange rate prevailing at March 31, 2004.







President's Message

Tomitaro Ogawa
President

During fiscal 2004, ended March 31, 2004, the Japanese economy showed clear signs of a recovery in the second half, owing to increased capital investment driven by demand for digital home electronics and cellular phones, as well as by a rebound in stock prices and a pickup in consumer spending. The global economy was favorable with firm growth in the United States and Asian economies.

In Sumitomo Bakelite Co., Ltd.'s main businesses and related industries, semiconductors showed vigorous activity throughout the fiscal year, backed by demand so strong that supply could not keep up with demand for some types of digital home electronics and cellular phones. Production of automobiles in Japan remained solid.

In this operating environment, Sumitomo Bakelite made every effort to promote restructuring while bolstering and expanding core businesses. As a result, consolidated net sales amounted to ¥170,249 million (US$1,611 million), an increase of ¥9,870 million (US$93 million) from the previous fiscal year. Operating income rose ¥8,565 million (US$81 million) to ¥14,928 million (US$141 million). Recurring profit grew ¥8,508 million (US$80 million) to ¥13,731 million (US$130 million). Net

income totaled ¥7,702 million (US$73 million), an increase of ¥7,447 million (US$70 million) year on year.

Despite the cause for concern in the global economy, such as worsened conditions in the Middle East, we expect the U.S. economy to strongly recover and China to continue growing as the world's main export region. The Japanese economy is expected to remain on a path to recovery overall, as conditions bottom out.

Under these circumstances, Sumitomo Bakelite is focusing management efforts on the following four issues of paramount importance.

First, Sumitomo Bakelite aims to strengthen its core businesses, which are: semiconductor, information and telecommunication applications; high-performance plastic applications; and quality-of-life applications. At the end of the fiscal year under review, Sumitomo Bakelite made Tsutsunaka Plastic Industry Co., Ltd. into a subsidiary. We intend to pursue synergistic effects in the quality-of-life applications business through stronger collaboration with this subsidiary.

Second, we will further promote cost reductions by continuing to emphasize overseas production of precision molded products, medical devices, flexible printed circuit boards, epoxy resin copper-clad laminates, and other products. We will strive to build a rock-solid management foundation that is more immune to the economic vagaries of any given geographical region by raising the ratio of overseas production to over 50%.

Third, we aim to develop a higher responsiveness to customer demands from the perspective of quality, delivery, and cost by leveraging our global network of production bases.

Lastly, we aim to maintain our high level of commitment to contributing to society and protecting the environment.

While pursuing these measures, Sumitomo Bakelite plans to reform the Board of Directors by reducing the number of directors. As a part of this effort, we have introduced an Executive Officer system. Sumitomo Bakelite is reforming overall management in an aim to clarify the separation of decision-making and business-execution oversight from business execution.

On behalf of Sumitomo Bakelite, I thank you for your ongoing support.

June 2004

Tomitaro Ogawa
President

Major Developments

1 Acquisition of Fers Resins, S.A. in Spain

Fers Resins Headquarters in Spain

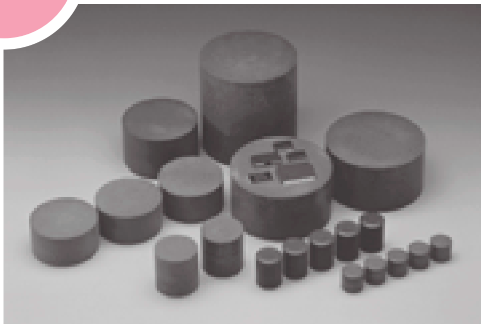
In August 2003, Sumitomo Bakelite acquired Fers Resins, S.A. and its affiliates in Spain. Fers Resins mainly handles friction resins that are used in automobile components. As a result of the acquisition, Sumitomo Bakelite's phenolic resins business has extended its coverage over the entire European marketplace.

2 Tsutsunaka Plastic Industry Co., Ltd. Made into a Subsidiary

Tsutsunaka Plastic Industry's "SUNLOID PC" is widely used in domes, window canopies and other structures for natural lighting.

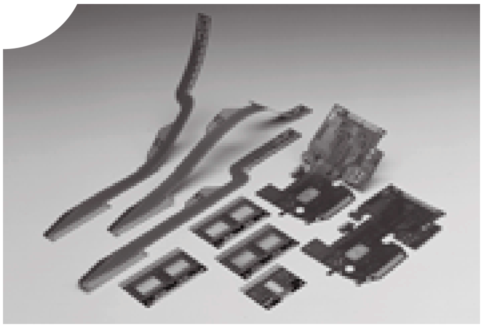
In March 2004, Sumitomo Bakelite turned Tsutsunaka Plastic Industry Co., Ltd. into a subsidiary. Tsutsunaka Plastic Industry Co., Ltd. engages in the production and sale of various plastic sheets and the construction of sheet waterproofing projects, and will play a central role in the quality-of-life applications business, a core business of the Sumitomo Bakelite Group.

3 Expanding Our Lineup of Environmentally Friendly Products



G Series of self-extinguishing epoxy encapsulation materials for semiconductors

SUMILITE RESIN® PR environmentally friendly phenolic resins



Environmentally friendly flexible printed circuit boards

Sumitomo Bakelite aims to expand its lineup of environmentally friendly products. Such products already in the lineup include the G Series of self-extinguishing epoxy encapsulation materials for semiconductors that do not use a flame retardant and the GS Series of environmentally friendly copper-clad laminates. Also among these are CRC positive photosensitive wafer-coating materials that are water soluble, environmentally friendly flexible printed circuit boards, new SUMILITE RESIN® PR environmentally friendly phenolic resins, and SUMIKON® PM phenolic resin molding compounds for warm sprue and warm runner. Sales of these environmentally friendly products have sharply increased recently to account for more than 10% of net sales.

In March 2004, the G Series of self-extinguishing epoxy encapsulation materials for semiconductors was recognized as an environmentally friendly chemical product through the Environment Minister Award.

Consolidated Balance Sheets

Sumitomo Bakelite Company, Limited and Consolidated Subsidiaries
March 31, 2004 and 2003

	Millions of yen		Thousands of U.S. dollars (Note 1)
ASSETS	2004	2003	2004
Current assets:			
Cash and cash equivalents	¥ 37,966	¥ 29,361	$ 359,186
Trade receivables:			
Notes	11,589	6,548	109,640
Accounts	46,712	31,980	441,930
Allowance for doubtful accounts	(458)	(462)	(4,333)
Inventories (Notes 3 and 7)	24,698	22,246	233,661
Deferred tax assets (Note 9)	2,039	1,403	19,290
Other current assets	4,631	3,348	43,814
Total current assets	127,177	94,424	1,203,188
Property, plant and equipment (Note 8)**:**			
Land	12,160	7,539	115,043
Buildings and structures	69,177	57,177	654,465
Machinery and equipment	129,758	104,288	1,227,606
Construction in progress	2,578	2,793	24,390
	213,673	171,797	2,021,504
Accumulated depreciation	(124,502)	(95,871)	(1,177,881)
Net property, plant and equipment	89,171	75,926	843,623
Goodwill	3,118	1,629	29,499
Investments and other assets:			
Investment securities (Note 5):			
Unconsolidated subsidiaries and affiliates	4,658	15,399	44,068
Other	14,161	3,268	133,974
Long-term loans receivable:			
Unconsolidated subsidiaries and affiliates	1,149	1,194	10,870
Employees and other	143	189	1,353
Deferred tax assets (Note 9)	947	2,132	8,959
Other assets	5,103	4,968	48,279
Allowance for doubtful accounts	(915)	(809)	(8,657)
Total investments and other assets	25,246	26,341	238,846
	¥ 244,712	¥198,320	$ 2,315,156

See accompanying notes.

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen 2004	Millions of yen 2003	Thousands of U.S. dollars (Note 1) 2004
Current liabilities:			
Short-term debt (Note 8)	¥ 22,090	¥ 16,308	$ 208,988
Long-term debt due within one year (Note 8)	522	270	4,939
Trade payables:			
Notes	8,048	5,195	76,140
Accounts	30,783	20,927	291,230
Accrued expenses	6,546	5,278	61,930
Income taxes payable (Note 9)	1,917	1,699	18,136
Deferred tax liabilities (Note 9)	–	74	–
Other current liabilities	5,704	2,811	53,963
Total current liabilities	75,610	52,562	715,326
Long-term liabilities:			
Long-term debt due after one year (Note 8)	21,061	20,587	199,253
Deferred tax liabilities (Note 9)	2,945	914	27,862
Retirement benefits:			
Employees (Note 10)	4,931	4,861	46,651
Directors and statutory auditors	719	485	6,802
Other long-term liabilities	2,104	152	19,905
Total long-term liabilities	31,760	26,999	300,473
Contingent liabilities (Note 14)			
Minority interests	19,909	4,317	188,354
Shareholders' equity (Note 11)**:**			
Common stock:			
Authorized —800,000,000 shares			
Issued —237,673,694 shares in 2004 and 2003	27,055	27,055	255,960
Capital surplus	25,270	25,270	239,073
Retained earnings	66,686	62,192	630,899
Net unrealized holding gains (losses) on securities	2,298	(509)	21,740
Foreign currency translation adjustments	(3,758)	532	(35,553)
Treasury stock, at cost	(118)	(98)	(1,116)
Total shareholders' equity	117,433	114,442	1,111,003
	¥244,712	¥198,320	$2,315,156

Consolidated Statements of Income

Sumitomo Bakelite Company, Limited and Consolidated Subsidiaries
Years ended March 31, 2004, 2003 and 2002

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2004	2003	2002	2004
Net sales (Note 13)	¥170,249	¥160,379	¥154,771	$1,610,681
Costs and expenses:				
Cost of sales (Note 13)	119,834	117,276	115,557	1,133,718
Selling, general and administrative expenses (Note 13)	35,487	36,740	33,893	335,733
	155,321	154,016	149,450	1,469,451
Operating income (Note 13)	14,928	6,363	5,321	141,230
Other income (expenses):				
Interest and dividend income	406	299	711	3,841
Interest expense	(403)	(393)	(736)	(3,813)
Equity in losses of affiliated companies	(886)	(738)	(260)	(8,382)
Loss on sale/disposal of property	(273)	(243)	(161)	(2,583)
Gain on sale of investment securities	–	182	1,996	–
Loss on devaluation of investment securities	(373)	(393)	(539)	(3,529)
Foreign exchange gain (loss), net	41	(458)	548	388
Cost of business acquisition (Note 4)	(144)	–	(1,018)	(1,362)
Lawsuit expense	(2,468)	–	–	(23,349)
Retirement benefit expenses	–	(4,212)	(3,014)	–
Gain on securities contributed to employees' retirement benefit trust (Note 2)	–	904	2,035	–
Gain on termination of employees' retirement benefit trust (Note 2)	1,217	–	–	11,514
Other, net	(380)	(190)	(205)	(3,595)
	(3,263)	(5,242)	(643)	(30,870)
Income before income taxes and minority interests	11,665	1,121	4,678	110,360
Income taxes (Note 9):				
Current	1,845	2,410	1,612	17,455
Deferred	1,542	(1,546)	(209)	14,589
	3,387	864	1,403	32,044
Minority interests	(576)	(2)	(153)	(5,449)
Net income	¥ 7,702	¥ 255	¥ 3,122	$ 72,867

	Yen			U.S. dollars (Note 1)
Amounts per share of common stock:				
Net income	¥32.14	¥ 0.87	¥13.18	$0.30
Diluted net income	29.28	–	12.33	0.28
Cash dividends applicable to the year	10.00	10.00	10.00	0.09

See accompanying notes.

Consolidated Statements of Shareholders' Equity

Sumitomo Bakelite Company, Limited and Consolidated Subsidiaries
Years ended March 31, 2004, 2003 and 2002

		Millions of yen					
	Thousands of shares of common stock	Common stock	Capital surplus	Retained earnings	Net unrealized holding gains (losses) on securities	Foreign currency translation adjustments	Treasury stock
Balance at March 31, 2001	236,864	¥26,827	¥24,948	¥63,120	¥ 16	¥ (325)	¥ (1)
Net income	–	–	–	3,122	–	–	–
Adjustments from translation of foreign currency financial statements	–	–	–	–	–	4,777	–
Adoption of new accounting standard for financial instruments	–	–	–	–	1,517	–	–
Treasury stock	–	–	–	–	–	–	(14)
Cash dividends paid (¥10 per share)	–	–	–	(2,368)	–	–	–
Bonuses to directors and statutory auditors	–	–	–	(88)	–	–	–
Shares issued upon conversion of bonds	275	90	90	–	–	–	–
Increase in retained earnings due to addition of consolidated subsidiaries	–	–	–	267	–	–	–
Balance at March 31, 2002	237,139	26,917	25,038	64,053	1,533	4,452	(15)
Net income	–	–	–	255	–	–	–
Net unrealized holding losses arising during the year	–	–	–	–	(2,042)	–	–
Adjustments from translation of foreign currency financial statements	–	–	–	–	–	(3,920)	–
Treasury stock	–	–	–	–	–	–	(83)
Cash dividends paid (¥10 per share)	–	–	–	(2,373)	–	–	–
Bonuses to directors and statutory auditors	–	–	–	(70)	–	–	–
Shares issued upon conversion of bonds	423	138	138	–	–	–	–
Shares issued by share exchange (Note 11)	112	–	94	–	–	–	–
Increase in capital surplus due to sale of treasury stock	–	–	0	–	–	–	–
Decrease in retained earnings due to addition of consolidated subsidiaries	–	–	–	(49)	–	–	–
Decrease in retained earnings due to exception of consolidated subsidiaries	–	–	–	(103)	–	–	–
Other (Note 2)	–	–	–	479	–	–	–
Balance at March 31, 2003	237,674	27,055	25,270	62,192	(509)	532	(98)
Net income	–	–	–	7,702	–	–	–
Net unrealized holding gains arising during the year	–	–	–	–	2,807	–	–
Adjustments from translation of foreign currency financial statements	–	–	–	–	–	(4,290)	–
Treasury stock	–	–	–	–	–	–	(20)
Cash dividends paid (¥10 per share)	–	–	–	(2,375)	–	–	–
Bonuses to directors and statutory auditors	–	–	–	(51)	–	–	–
Increase in capital surplus due to sale of treasury stock	–	–	0	–	–	–	–
Decrease in retained earnings due to addition of consolidated subsidiaries	–	–	–	(849)	–	–	–
Other	–	–	–	67	–	–	–
Balance at March 31, 2004	237,674	¥27,055	¥25,270	¥66,686	¥ 2,298	¥(3,758)	¥(118)

		Thousands of U.S. dollars (Note 1)					
	Thousands of shares of common stock	Common stock	Capital surplus	Retained earnings	Net unrealized holding gains (losses) on securities	Foreign currency translation adjustments	Treasury stock
Balance at March 31, 2003	237,674	$255,960	$239,073	$588,382	$ (4,816)	$ 5,033	$ (927)
Net income	–	–	–	72,867	–	–	–
Net unrealized holding gains arising during the year	–	–	–	–	26,556	–	–
Adjustments from translation of foreign currency financial statements	–	–	–	–	–	(40,586)	–
Treasury stock	–	–	–	–	–	–	(189)
Cash dividends paid ($0.09 per share)	–	–	–	(22,469)	–	–	–
Bonuses to directors and statutory auditors	–	–	–	(482)	–	–	–
Increase in capital surplus due to sale of treasury stock	–	–	0	–	–	–	–
Decrease in retained earnings due to addition of consolidated subsidiaries	–	–	–	(8,032)	–	–	–
Other	–	–	–	633	–	–	–
Balance at March 31, 2004	237,674	$255,960	$239,073	$630,899	$21,740	$(35,553)	$(1,116)

See accompanying notes.

Consolidated Statements of Cash Flows

Sumitomo Bakelite Company, Limited and Consolidated Subsidiaries
Years ended March 31, 2004, 2003 and 2002

	Millions of yen			Thousands of U.S. dollars (Note 1)
	2004	2003	2002	2004
Cash flows from operating activities:				
Net income	¥ 7,702	¥ 255	¥ 3,122	$ 72,867
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	9,746	10,650	10,074	92,204
Loss on sale/disposal of property, plant and equipment	273	243	161	2,583
Gain on sale of investment securities	–	(182)	(1,996)	–
Minority interests	576	2	153	5,449
Gain on termination of employees' retirement benefit trust	(1,217)	–	–	(11,514)
Loss on devaluation of investment securities	373	393	539	3,529
Equity in losses of affiliated companies	886	738	260	8,382
Deferred income taxes	1,542	(1,546)	(209)	14,589
Decrease (increase) in notes and accounts receivable	(1,113)	5,568	11,486	(10,530)
Decrease (increase) in inventories	2,165	(2,050)	2,118	20,482
Decrease in other current assets	427	763	1,154	4,040
Decrease in notes and accounts payable	(2,267)	(564)	(9,840)	(21,447)
(Decrease) increase in income taxes payable	(210)	143	(2,319)	(1,987)
(Decrease) increase in other current liabilities	250	(350)	(1,643)	2,365
(Decrease) increase in retirement benefits	(2,182)	2,602	(28)	(20,643)
Other, net	1,072	868	670	10,142
Net cash provided by operating activities	18,023	17,533	13,702	170,511
Cash flows from investing activities:				
Purchases of investment securities (Note 4)	(3,582)	(1,389)	(2,739)	(33,888)
Proceeds from sale of marketable securities and investment securities	0	330	8,023	0
Purchases of property, plant and equipment	(6,489)	(10,576)	(12,080)	(61,391)
Proceeds from sale of property, plant and equipment	199	451	760	1,883
Payment for business acquisition (Note 4)	(517)	–	(2,484)	(4,891)
Proceeds from purchase of investment securities with change in scope of consolidation (Note 4)	4,076	–	(69)	38,562
Increase in short-term loans receivable (Note 4)	(3,893)	–	–	(36,831)
Decrease (increase) in long-term loans receivable	64	(155)	657	605
Other	328	(710)	88	3,103
Net cash used in investing activities	(9,814)	(12,049)	(7,844)	(92,848)
Cash flows from financing activities:				
Increase in short-term debt	4,221	1,974	1,836	39,934
Repayments of long-term debt	(292)	(634)	(1,116)	(2,763)
Cash dividends paid	(2,852)	(2,851)	(2,434)	(26,982)
Proceeds from issuance of stock to minority interests	500	–	666	4,730
Other	(20)	(86)	(14)	(189)
Net cash provided by (used in) financing activities	1,557	(1,597)	(1,062)	14,730
Effect of exchange rate changes on cash and cash equivalents	(1,557)	(525)	1,105	(14,730)
Net increase in cash and cash equivalents	8,209	3,362	5,901	77,663
Cash and cash equivalents at beginning of year	29,361	27,224	20,420	277,777
Increase in cash and cash equivalents due to addition of consolidated subsidiaries	539	154	903	5,099
Decrease in cash and cash equivalents due to exception of consolidated subsidiaries	–	(288)	–	–
Other (Note 2)	(143)	(1,091)	–	(1,353)
Cash and cash equivalents at end of year	¥37,966	¥29,361	¥27,224	$359,186
Supplemental information on cash flows:				
Cash paid during the year for:				
Interest	¥ 390	¥ 399	¥ 771	$ 3,690
Income taxes	2,054	2,266	3,931	19,432
Non-cash investing and financing activities:				
Conversion of convertible bonds into common stock and capital surplus	–	276	180	–
Increase in capital surplus due to share exchange	–	94	–	–

See accompanying notes.

Notes to Consolidated Financial Statements

Sumitomo Bakelite Company, Limited and Consolidated Subsidiaries

1. Basis of presenting consolidated financial statements

Sumitomo Bakelite Company, Limited (the "Company") is a Japanese corporation, one of the affiliated companies of Sumitomo Chemical Co., Ltd., which directly owns 20.7% (at March 31, 2004) of the Company's voting shares. The Company and its consolidated domestic subsidiaries maintain their accounts and records in accordance with the provisions set forth in the Japanese Commercial Code (the "Code") and accounting principles and practices generally accepted in Japan ("Japanese GAAP"). The accounts of consolidated overseas subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries of domicile. Certain Japanese GAAP are different from International Accounting Standards and standards in other countries in certain respects, as to application and disclosure requirements.

The accompanying consolidated financial statements are the translation of the audited consolidated financial statements of the Company which were prepared in accordance with Japanese GAAP and were filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Securities and Exchange Law.

In preparing the accompanying consolidated financial statements, certain reclassifications have been made in the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. The consolidated statements of shareholders' equity for 2004, 2003 and 2002 have been prepared for the purpose of inclusion in the accompanying consolidated financial statements, although such statements were not required for domestic purposes and were not filed with the regulatory authorities.

The translations of the Japanese yen amounts into U.S. dollars are included solely for the convenience of readers, using the prevailing exchange rate at March 31, 2004, which was ¥105.7 to US$1. The convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

2. Summary of significant accounting policies

Consolidation

The consolidated financial statements include the accounts of the Company and its significant subsidiaries (44 subsidiaries in 2004, 31 subsidiaries in 2003 and 32 subsidiaries in 2002). All significant intercompany balances and transactions have been eliminated in consolidation.

Investments in significant affiliated companies (7 affiliates in 2004, 8 affiliates in 2003 and 2002, generally 20%-50% owned), over which the Company has the ability to exercise significant influence over operating and financial policies are stated at cost adjusted for equity in undistributed earnings and losses since acquisition.

Investments in the other unconsolidated subsidiaries and affiliated companies are stated at cost, because the Company's equity in the income or losses of these companies is not significant.

In the elimination of investments in subsidiaries, the assets and liabilities of the subsidiaries, including the portion attributable to minority shareholders, are evaluated using the fair value at the time the Company acquired control of the respective subsidiaries.

The excess of the cost over underlying net equity of investments in consolidated subsidiaries and other companies accounted for by the equity method at the date of acquisition is charged to income as incurred. However, when it is significant, it is deferred and amortized on a straight-line basis over a period of five years from the date of acquisition.

The fiscal year of the Company begins on April 1 and ends at March 31. On the other hand, all consolidated overseas subsidiaries and some domestic subsidiaries have fiscal years ending mainly at December 31.

Up to the fiscal year ended March 31, 2002, the consolidated financial statements had included their financial statements for the year ended December 31, and certain adjustments had been made for the effects of significant transactions or other events that had occurred from January 1 to March 31.

At the beginning of the fiscal year ended March 31, 2003, the Companies changed the consolidated closing date for all consolidated overseas subsidiaries and one domestic subsidiary as of that date from December 31 to March 31.

As a result of this change, net income for these companies for the three-month period ended March 31, 2002, amounting to ¥479 million, was not reflected in the consolidated statement of income but in the consolidated statement of shareholders' equity for the year ended March 31, 2003. In addition, this change also gave effect to the statement of cash flows and decreased cash and cash equivalents by ¥1,091 million for the year ended March 31, 2003.

Cash and cash equivalents

In preparing the consolidated statements of cash flows, cash on hand, readily-available deposits and short-term highly liquid investments with maturities not exceeding three months at the time of purchase are considered to be cash and cash equivalents.

Securities

Securities are classified into one of the following categories based on the intent of holding, resulting in the different measurement and accounting for the changes in fair value. Held-to-maturity debt securities are stated at amortized cost. Equity securities issued by subsidiaries and affiliated companies, which are not consolidated or accounted for using the equity method, are stated at moving-average cost. Available-for-sale securities with available fair market values are stated at fair market value. Unrealized gains and unrealized losses on these securities are reported, net of applicable income taxes, as a separate component of shareholders' equity. Other available-for-sale securities with no available fair market values are stated at moving-average cost.

Significant declines in fair market value or the net asset value of held-to-maturity debt securities, equity securities, not on the equity method, issued by unconsolidated subsidiaries and affiliated companies, and available-for-sale securities, judged to be other than temporary, are charged to income.

Derivatives and hedge accounting

The Companies are required to state derivative financial instruments at fair value and to recognize changes in the fair value as gains or losses unless derivative financial instruments are used for hedging purposes.

If derivative financial instruments are used as hedges and meet certain hedging criteria, the Companies defer recognition of gains or losses resulting from changes in fair value of derivative financial instruments until the related losses or gains on the hedged items are recognized.

However, in cases where forward foreign exchange contracts are used as hedges and meet certain hedging criteria, hedging instruments and hedged items are accounted for in the following manner:

1. If a forward foreign exchange contract is executed to hedge an existing foreign currency receivable,
   (a) the difference, if any, between the Japanese yen amount of the hedged foreign currency receivable translated using the spot rate at the inception date of the contract and the book value of the receivable is recognized in the income statement in the period, which includes the inception date, and
   (b) the discount or premium on the contract (that is, the difference between the Japanese yen amount of the contract translated using the contracted forward rate and that translated using the spot rate at the inception date of the contract) is recognized over the term of the contract.
2. If a forward foreign exchange contract is executed to hedge a future transaction denominated in a foreign currency, the future transaction will be recorded using the contracted forward rate, and no gains or losses on the forward foreign exchange contract will be recognized.

Allowance for doubtful accounts

The allowance for doubtful accounts is determined by adding the uncollectible amounts, individually estimated for doubtful accounts, to the amount calculated by a certain rate, based on past collection experience.

Inventories

Inventories are accounted for mainly at cost determined by the moving-average method.

Property, plant and equipment

Property, plant and equipment are carried at cost. The Company and its consolidated domestic subsidiaries calculate depreciation principally by the declining-balance method at rates based on the estimated useful lives of assets. Buildings and structures of the Company's head office and other buildings, excluding building fixtures, acquired after March 31, 1998 are depreciated using the straight-line method. The consolidated overseas subsidiaries calculate depreciation principally by the straight-line method over estimated useful lives.

Effective April 1, 2003, some consolidated overseas subsidiaries changed the estimated useful lives of buildings, machinery and equipment. This change was made in order to conform their estimated useful lives to actual operating level. The effect of this change was to increase operating income and income before income taxes and minority interests by ¥397 million ($3,756 thousand) for the year ended March 31, 2004 as compared to the prior useful lives.

In the year ended March 31, 2004, the Company did not adopt early the new accounting standard for impairment of fixed Assets ("Opinion Concerning Establishment of Accounting Standard for Impairment of Fixed Assets" issued by the Business Accounting Deliberation Council on August 9, 2002) and the implementation guidance for the accounting standard for impairment of fixed assets (the Financial Accounting Standard Implementation Guidance No. 6 issued by the Accounting Standards Board of Japan on October 31, 2003). The new accounting standard is required to be adopted in periods beginning on or after April 1, 2005, but the standard does not prohibit earlier adoption. The Company will adopt these standards effective April 1, 2005.

The Company has begun its analysis of possible impairment of fixed assets. The Company cannot currently estimate the effect of adoption of the new standard, because the Company has not yet completed its analysis. However, adoption of the new standard could have a certain effect on the Company's financial statements.

Accounting for certain lease transactions

Finance leases, which do not transfer ownership, or those which do not have a bargain purchase option provision are accounted for in the same manner as operating leases in accordance with Japanese GAAP.

Accrued employees' bonuses

The Company and its consolidated domestic subsidiaries accrue the amounts of employees' bonuses based on estimated amounts to be paid in the subsequent period.

Bonuses to directors and statutory auditors

Bonuses to directors and statutory auditors, which are subject to shareholders' approval at the annual shareholders' meeting, are accounted for as an appropriation of retained earnings.

Employees' severance and retirement benefits

The Company and certain consolidated subsidiaries provide two types of post-employment benefit plans, unfunded lump-sum payment plans and funded non-contributory pension plans, under which all eligible employees are entitled to benefits based on the level of wages and salaries at the time of retirement or termination, length of service and certain other factors.

The liabilities and expenses for severance and retirement benefits are determined based on the amounts actuarially calculated using certain assumptions.

The Company and certain consolidated subsidiaries provided an allowance for employees' severance and retirement benefits at March 31, 2004 and 2003 based on the estimated amounts of projected benefit obligation and the fair value of the plan assets at these dates.

The Company and certain consolidated subsidiaries contributed investment securities worth ¥2,066 million and ¥2,545 million to the employees' retirement benefit trust, and the resulting gains amounting to ¥904 million and ¥2,035 million were recognized in the years ended March 31, 2003 and 2002, respectively. Prior service costs and actuarial gains and losses are mainly recognized in the statements of income when they are determined actuarially.

In fiscal 2004, the Company terminated a certain portion of the employees' retirement benefit trust, and the resulting gain amounting to ¥1,217 million ($11,514 thousand) was recognized in the year ended March 31, 2004.

Research and development

Research and development expenses are charged to income when incurred. The amounts for the years ended March 31, 2004, 2003 and 2002 were ¥10,139 million ($95,922 thousand), ¥10,234 million and ¥9,775 million, respectively.

Income taxes

The Companies recognize tax effects of temporary differences between the carrying amounts of assets and liabilities for tax and financial reporting. 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 of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

Translation of foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated into Japanese yen at year-end rates.

Translation of foreign currency financial statements

Financial statements of consolidated overseas subsidiaries are translated into Japanese yen at the year-end rates for balance sheets and at the annual average rates for statements of income, except that shareholders' equity accounts are translated at historical rates and income statement items relating to transactions with the Company at the rates used by the Company.

Amounts per share of common stock

The computations of net income per share are based on the weighted average number of shares outstanding during the relevant year.

Diluted net income per share is computed based on the average number of shares of common stock and contingent issuances of common stock from convertible bonds. Diluted net income per share in 2003 is not disclosed, because there was no latent stock that diluted net income per share at March 31, 2003.

Cash dividends per share represent the cash dividends approved by the shareholders and paid in the respective year, including payment after the year-end.

Effective April 1, 2002, the Company adopted the new accounting standard for earnings per share and related guidance (Accounting Standards Board Statement No.2, "Accounting Standard for Earnings Per Share" and Financial Standards Implementation Guidance No.4, "Implementation Guidance for Accounting Standard for Earnings Per Share," issued by the Accounting Standards Board of Japan on September 25, 2002).

Net income per share for the year ended March 31, 2002 would have been reported as follows, if this new accounting standard were applied retroactively.

Year ended March 31, 2002	Yen
Net income per share	
Basic	¥12.88
Diluted	12.06

Treasury stock and reversal of statutory reserves

Effective April 1, 2002, the Company and consolidated domestic subsidiaries adopted the new accounting standard for treasury stock and reversal of statutory reserves (Accounting Standards Board Statement No.1, "Accounting Standard for Treasury Stock and Reversal of Statutory Reserves," issued by the Accounting Standards Board of Japan on February 21, 2002).

The effect on net income of the adoption of the new accounting standard was not material.

Reclassifications

Certain prior year amounts have been reclassified to conform to the year 2004 presentation. These changes had no impact on previously reported results of operations or shareholders' equity.

3. Change in accounting policies

Effective April 1, 2002, the Company changed the method of valuation for finished goods, semi-finished goods and work in process from the weighted average method to the moving-average method. This change was made in order to strengthen the Company's monthly profit control, by means of introduction of a new cost accounting system.

The effect of this change was to increase operating income and income before income taxes and minority interests by ¥152 million for the year ended March 31, 2003 as compared to the prior method.

4. Business acquisition

(1) In the year ended March 31, 2002, the Companies acquired the research and development department, related to electronics materials, of Goodrich Corporation, and paid ¥2,484 million. In the accompanying statement of income for the year ended March 31, 2002, the Companies recognized related expenses amounting to ¥1,018 million as cost of business acquisition.

In the year ended March 31, 2004, the Companies acquired Fers Resins, S.A. and its subsidiaries, (“Fers Group”), which manufacture the industrial phenolic resins mainly used for friction materials, and an epoxy resin molding compounds business for encapsulation of semiconductor devices and related assets of Toray Industries Inc.

Components of these purchases were as follows:

	Millions of yen	Thousands of U.S. dollars
Purchase of shares of Fers Group	¥4,907	$46,424
Purchase of properties and equipment	373	3,529
Various expenses related with the acquisitions	144	1,362
	¥5,424	$51,315

In the statement of income for the year ended March 31, 2004, the Companies recognized the related expenses amounting to ¥144 million ($1,362 thousand) as cost of business acquisition. In addition, in the statement of cash flows for the year ended March 31, 2004, payment for purchase of shares of Fers Group was included in purchases of investment securities and increase in short-term receivables, amounting to ¥1,059 million ($10,019 thousand) and ¥3,848 million ($36,405 thousand), respectively.

(2) Assets and liabilities of the subsidiaries newly consolidated in 2004 by means of a tender offer at the inception of consolidation are as follows. (Tsutsunaka Plastic Industry Co., Ltd. and its 7 subsidiaries)

	Millions of yen	Thousands of U.S. dollars
Current assets	¥36,330	$343,709
Fixed assets	20,275	191,816
Total assets	¥56,605	$535,525
Current liabilities	¥21,942	$207,588
Long-term liabilities	1,891	17,890
Total liabilities	¥23,833	$225,478

5. Securities

(1) The following tables summarize acquisition costs and book values of available-for-sale securities with available fair values as of March 31, 2004 and 2003:

Securities with book values exceeding acquisition costs:

	Millions of yen		
At March 31, 2004	Acquisition cost	Book value	Difference
Equity securities	¥6,312	¥10,471	¥4,159
Bonds	56	58	2
Others	–	–	–
Total	¥6,368	¥10,529	¥4,161

	Millions of yen		
At March 31, 2003	Acquisition cost	Book value	Difference
Equity securities	¥295	¥389	¥94
Bonds	–	–	–
Others	–	–	–
Total	¥295	¥389	¥94

	Thousands of U.S. dollars		
At March 31, 2004	Acquisition cost	Book value	Difference
Equity securities	$59,716	$99,063	$39,347
Bonds	530	549	19
Others	–	–	–
Total	$60,246	$99,612	$39,366

Securities with available fair values not exceeding book values:

	Millions of yen		
At March 31, 2004	Acquisition cost	Book value	Difference
Equity securities	¥570	¥535	¥(35)
Bonds	–	–	–
Others	–	–	–
Total	¥570	¥535	¥(35)

	Millions of yen		
At March 31, 2003	Acquisition cost	Book value	Difference
Equity securities	¥3,203	¥2,278	¥(925)
Bonds	–	–	–
Others	–	–	–
Total	¥3,203	¥2,278	¥(925)

	Thousands of U.S. dollars		
At March 31, 2004	Acquisition cost	Book value	Difference
Equity securities	$5,392	$5,061	$(331)
Bonds	–	–	–
Others	–	–	–
Total	$5,392	$5,061	$(331)

The Companies recognize impairment loss for the securities, whose available fair values significantly decline more than 50% of the carrying amount. In addition, the Companies also recognize impairment loss, when the available fair values decline more than 30% to 50% of the carrying amount and such situation continues twice at the end of each semi-annual period. The amounts of impairment loss for the years ended March 31, 2004 and 2003 were ¥73 million ($691 thousand) and ¥393 million, respectively. As impairment loss was recognized in the statements of income, the above tables of available-for-sale securities exclude such securities written down to fair values.

(2) Total sales of held-to-maturity debt securities sold and the related gains and losses in the year ended March 31, 2002 were as follows:

Year ended March 31, 2002	Millions of yen
Book value	¥4,027
Sales of held-to-maturity debt securities	4,644
Gain on sale	617

The Companies sold all held-to-maturity debt securities in the year ended March 31, 2002, to appropriate financing for the establishment of subsidiaries.

(3) Total sales of available-for-sale securities sold and the related gains and losses in the years ended March 31, 2004, 2003 and 2002 were as follows:

	Millions of yen			Thousands of U.S. dollars
	2004	2003	2002	2004
Sales of available-for-sale securities	¥0	¥330	¥2,878	$0
Gains on sales of available-for-sale securities	0	182	1,554	0
Losses on sales of available-for-sale securities	–	–	175	–

(4) The following table summarizes book values of available-for-sale securities with no available fair values as of March 31, 2004 and 2003:

	Millions of yen		Thousands of U.S. dollars
At March 31	2004	2003	2004
Non-listed equity securities	¥2,783	¥585	$26,329
Non-listed convertible bonds	300	–	2,838
Others	13	16	123
Total	¥3,096	¥601	$29,290

(5) Available-for-sale securities with maturities at March 31, 2004 are as follows:

	Millions of yen				
	Within one year	Over one year but within five years	Over five years but within ten years	Over ten years	Total
Bonds					
Government bonds	–	¥ –	¥ –	–	¥ –
Corporate bonds	–	57	300	–	357
Others	–	–	–	–	–
Total	–	¥57	¥300	–	¥357

	Thousands of U.S. dollars				
	Within one year	Over one year but within five years	Over five years but within ten years	Over ten years	Total
Bonds					
Government bonds	–	$ –	$ –	–	$ –
Corporate bonds	–	539	2,838	–	3,377
Others	–	–	–	–	–
Total	–	$539	$2,838	–	$3,377

6. Derivative financial instruments

The Companies utilize derivative financial instruments such as foreign currency forward contracts to reduce market risks of fluctuations in foreign currency exchange rates on assets and liabilities. The Companies do not hold or issue derivative financial instruments for trading purposes.

The Companies are exposed to credit risk in the event of nonperformance by counterparties to derivative financial instruments, but such risk is considered minor because of the high credit rating of the counterparties.

The Companies enter into derivative financial instruments as a hedge for existing assets and liabilities denominated in foreign currencies, arising from operating activities.

According to the accounting standard for financial instruments, market value and other information on derivative financial instruments at March 31, 2004 and 2003 are not subjected to disclosure, because the Companies adopted hedge accounting for those instruments.

7. Inventories

Inventories at March 31, 2004 and 2003 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2004	2003	2004
Finished goods	¥12,732	¥11,152	$120,454
Semi-finished goods	2,332	1,876	22,062
Work in process	1,356	1,704	12,829
Raw materials and supplies	8,278	7,514	78,316
	¥24,698	¥22,246	$233,661

8. Short-term debt and long-term debt

Short-term debt consists of bank loans and commercial paper. The composition of short-term debt and its interest rates at March 31, 2004 and 2003 was as follows:

At March 31, 2004	Millions of yen	Thousands of U.S. dollars	Interest rates
Bank loans	¥10,090	$ 95,459	0.30%–4.63%
Commercial paper	12,000	113,529	0.01%
	¥22,090	$208,988	

At March 31, 2003	Millions of yen	Interest rates
Bank loans	¥11,308	0.30%–6.90%
Commercial paper	5,000	0.04%
	¥16,308	

Long-term debt at March 31, 2004 and 2003 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2004	2003	2004
1.2% domestic convertible bonds convertible into common stock at ¥716 ($7) per share due 2006	¥20,183	¥20,183	$190,946
Secured loans from banks due through 2006 with interest rates ranging from 2.08% to 2.20% at March 31, 2004	377	641	3,567
Unsecured loans from a bank and organizations due through 2011 with interest rates ranging from 1.85% to 2.96% at March 31, 2004	1,023	33	9,679
	21,583	20,857	204,192
Less amount due within one year	(522)	(270)	(4,939)
	¥21,061	¥20,587	$199,253

The indentures relating to the 1.2% domestic convertible bonds place a limitation on the payment of cash dividends which shall not exceed, on a cumulative basis, ¥3,800 million ($35,951 thousand) plus the aggregate amount of earnings of the Company (as defined in the indentures) during the years, for which the bonds are outstanding. In this connection interim cash dividends are regarded as a part of the cash dividends made in the previous period.

At March 31, 2004, the number of common stock issuable upon full conversion of outstanding convertible bonds was 28,188 thousand shares.

The annual maturities of long-term debt at March 31, 2004 were as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars
2005	¥ 522	$ 4,939
2006	534	5,052
2007	20,513	194,069
2008	3	28
2009	3	28
2010 and thereafter	8	76

At March 31, 2004, assets pledged as collateral were as follows:

	Millions of yen	Thousands of U.S. dollars
Buildings	¥2,233	$21,126
Land	139	1,315

At March 31, 2004, obligations with collateral pledged were as follows:

	Millions of yen	Thousands of U.S. dollars
Short-term debt	¥ 10	$ 95
Long-term debt	377	3,567
	387	3,662
Contingent liability	389	3,680
	¥776	$7,342

9. Income taxes

The Companies are subject to several taxes based on income, which are corporation tax, inhabitants' tax and enterprise tax. The aggregate statutory tax rates on income before income taxes were approximately 42% for the years ended March 31, 2004, 2003 and 2002.

Significant components of the Companies' deferred tax assets and liabilities as of March 31, 2004 and 2003 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2004	2003	2004
Deferred tax assets:			
Retirement benefits of employees	¥ 4,666	¥ 4,310	$ 44,144
Amortization of prior service cost of the pension plan	4,284	3,974	40,530
Excess depreciation in overseas subsidiaries	2,686	–	25,412
Tax loss carryforwards	1,392	1,124	13,169
Excess bonuses accrued	1,047	661	9,905
Cost of business acquisition	369	444	3,491
Provision for doubtful accounts	316	369	2,990
Retirement benefits of directors and statutory auditors	283	192	2,677
Unrealized gains on property, plant and equipment	247	365	2,337
Loss on devaluation of securities	215	341	2,034
Net unrealized holding losses on securities	–	337	–
Others	1,858	1,588	17,578
Total deferred tax assets	17,363	13,705	164,267
Valuation allowance	(2,808)	(1,315)	(26,566)
Net deferred tax assets	¥ 14,555	¥12,390	$ 137,701
Deferred tax liabilities:			
Additional depreciation in overseas subsidiaries	¥ (3,014)	¥ (728)	$ (28,515)
Gain on securities contributed to employees' retirement benefit trust	(2,883)	(3,229)	(27,275)
Contribution to funded non-contributory pension plan	(2,637)	(2,061)	(24,948)
Deferred gains on property, plant and equipment	(2,506)	(2,295)	(23,709)
Net unrealized holding gains on securities	(1,672)	–	(15,818)
Gain on dissolution of employees' retirement benefit trust	(927)	–	(8,770)
Others	(875)	(1,530)	(8,279)
Total deferred tax liabilities	¥(14,514)	¥ (9,843)	$(137,314)
Net deferred tax assets	¥ 41	¥ 2,547	$ 387

The differences between the statutory tax rate and the Companies' actual effective tax rate for financial statement purposes for the years ended March 31, 2004, 2003 and 2002 were as follows:

	2004	2003	2002
Statutory tax rate	42.0%	42.0%	42.0%
Permanently non-deductible expenses	2.4	10.8	2.7
Permanently non-taxable income	(5.3)	(34.5)	(4.8)
Deficits of consolidated subsidiaries	1.9	64.7	3.4
Dividend income eliminated in consolidation	8.7	67.4	–
Equity in losses of affiliated companies	3.2	27.6	–
Tax credit	(7.1)	(14.3)	–
Effect of differences between tax rates in Japan and in other countries	(16.6)	(87.3)	(12.2)
Other, net	(0.2)	0.6	(1.1)
Actual effective tax rate	29.0%	77.0%	30.0%

10. Employees' severance and pension benefits

As explained in Note 2 (Employees' severance and retirement benefits), the liabilities and expenses for severance and retirement benefits are determined based on the amounts obtained by actuarial calculations.

The liabilities for severance and retirement benefits included in the liabilities section of the consolidated balance sheets as of March 31, 2004 and 2003 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
At March 31	2004	2003	2004
Projected benefit obligation	¥ 28,689	¥ 23,413	$ 271,419
Less fair value of pension assets	(23,555)	(19,058)	(222,847)
Less unrecognized actuarial differences	(1,009)	(468)	(9,546)
Unrecognized prior service costs	708	886	6,698
Prepaid benefit expenses	98	88	927
Liability for severance and retirement benefits	¥ 4,931	¥ 4,861	$ 46,651

Severance and retirement benefit expenses, included in the consolidated statements of income for the years ended March 31, 2004, 2003 and 2002 are comprised of the following:

	Millions of yen			Thousands of U.S. dollars
	2004	2003	2002	2004
Service costs—benefits earned during the year	¥ 1,003	¥ 963	¥ 984	$ 9,489
Interest cost on projected benefit obligation	814	837	858	7,701
Expected return on plan assets	(144)	(402)	(431)	(1,362)
Amortization of actuarial differences	(601)	4,631	3,014	(5,686)
Amortization of prior service costs	(76)	(27)	–	(719)
Severance and retirement benefit expenses	¥ 996	¥6,002	¥4,425	$ 9,423
Reversal of severance and retirement benefit expenses upon dissolution of the employee retirement benefit trust	(1,065)	–	–	(10,076)
Net	¥ (69)	¥6,002	¥4,425	$ (653)

The discount rates and rates of expected return on plan assets used by the Companies are as follows:

	2004	2003	2002
Discount rate:			
Domestic companies	2.0%	3.0%	3.0%
Overseas companies	6.5%–7.3%	6.5%	7.3%–7.5%
Expected return on plan assets	0.0%	1.5%	1.5%

The estimated amount of all retirement benefits to be paid at the future retirement date is allocated equally to each service year using the estimated number of total service years. Prior service cost and actuarial gains/losses are mainly recognized in the statements of income when they are determined actuarially.

11. Shareholders' equity

Under the Code, at least 50% of the issue price of new shares is required to be designated as stated capital. The portion that is to be designated as stated capital is determined by resolution of the Board of Directors. Proceeds in excess of the amounts designated as stated capital are credited to additional paid-in capital, which is included in capital surplus.

The Code provides that an amount equal to at least 10% of cash dividends and other cash appropriations shall be appropriated and set aside as a legal reserve until the total amount of legal reserve and additional paid-in capital equals 25% of common stock. The legal reserve and additional paid-in capital may be used to eliminate or reduce a deficit by resolution of the shareholders' meeting or may be capitalized by resolution of the Board of Directors. On condition that the total amount of legal reserve and additional paid-in capital remains equal to or exceeds 25% of common stock, it is available for distribution by resolution of the shareholders' meeting. At March 31, 2004 and 2003, legal reserves of the Company amounting to ¥4,137 million ($39,139 thousand) were included in retained earnings in the accompanying consolidated financial statements.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Code.

In the year ended March 31, 2003, the Company issued shares relating to a share exchange with minority shareholders of Yamaroku Kasei Industry Co., Ltd.

12. Information on lease transactions

The following proforma amounts present the acquisition cost, accumulated depreciation and net book value of the property leased to the companies as of March 31, 2004 and 2003, which would have been reflected in the balance sheets if finance leases other than those that transfer the ownership of the leased property to the companies (which are currently accounted for in the same manner as operating leases) were capitalized.

	Millions of yen		
At March 31, 2004	Machinery and equipment	Other assets	Total
Acquisition cost, accumulated depreciation and net book value of leased assets:			
Acquisition cost	¥1,586	¥166	¥1,752
Accumulated depreciation	1,097	132	1,229
Net book value	¥ 489	¥ 34	¥ 523

At March 31, 2003	Millions of yen Machinery and equipment	Other assets	Total
Acquisition cost, accumulated depreciation and net book value of leased assets:			
Acquisition cost	¥1,308	¥139	¥1,447
Accumulated depreciation	783	97	880
Net book value	¥ 525	¥ 42	¥ 567

At March 31, 2004	Thousands of U.S. dollars Machinery and equipment	Other assets	Total
Acquisition cost, accumulated depreciation and net book value of leased assets:			
Acquisition cost	$15,005	$1,570	$16,575
Accumulated depreciation	10,379	1,248	11,627
Net book value	$ 4,626	$ 322	$ 4,948

	Millions of yen		Thousands of U.S. dollars
	2004	2003	2004
Future lease payments:			
Due within one year	¥285	¥293	$2,696
Due after one year	251	296	2,375
Total	¥536	¥589	$5,071

	Millions of yen			Thousands of U.S. dollars
	2004	2003	2002	2004
Lease payments, depreciation and interest expense:				
Lease payments	¥339	¥352	¥371	$3,207
Depreciation	287	318	341	2,715
Interest expense	44	32	30	416

An amount equal to the depreciation is calculated based on the useful life of the lease term and a residual value of zero.

An amount equal to the total interest expense is the difference between the total lease payments and the acquisition cost of leased assets, and is allocated over the lease term mainly by the interest method.

Operating leases were as follows:

	Millions of yen		Thousands of U.S. dollars
	2004	2003	2004
Future lease payments:			
Due within one year	¥ 5	¥6	$ 47
Due after one year	6	2	57
Total	¥11	¥8	$104

13. Segment information

Information by business segment for the years ended March 31, 2004 and 2003 is as follows :

Year ended March 31, 2004	Millions of yen							
	Semiconductor and display materials	Circuits and electronic component materials	High performance plastics	Quality of life products	Others	Total	Eliminations or corporate	Consolidated
Sale:								
Outside customers	¥55,494	¥40,221	¥44,395	¥29,457	¥682	¥170,249	¥ –	¥170,249
Inter-segment	25	–	1,136	418	66	1,645	(1,645)	–
Total sales	55,519	40,221	45,531	29,875	748	171,894	(1,645)	170,249
Operating expenses	43,517	37,359	44,033	27,907	503	153,319	2,002	155,321
Operating income	¥12,002	¥ 2,862	¥ 1,498	¥ 1,968	¥245	¥ 18,575	¥ (3,647)	¥ 14,928
Identifiable assets	¥50,661	¥47,364	¥53,334	¥75,261	¥756	¥227,376	¥17,336	¥244,712
Depreciation and amortization	2,659	2,743	2,635	1,189	83	9,309	324	9,633
Capital expenditures	1,702	1,400	1,946	1,238	100	6,386	228	6,614

"Eliminations or corporate" in the "Operating expenses" column of the above information included corporate expenses of ¥3,643 million ($34,465 thousand) in the year ended March 31, 2004, which consisted principally of basic research and development costs and general and administrative costs accounted by the Company.

"Eliminations or corporate" in the "Identifiable assets" column of the above information included corporate assets of ¥17,758 million ($168,004 thousand) at March 31, 2004, which consisted principally of cash, time deposits, loans receivable, investments in securities, basic research and development assets and general and administrative assets held by the Company.

As described in Note 2, some consolidated overseas subsidiaries changed the estimated useful lives of buildings, machinery and equipment from the year ended March 31, 2004.

As a result of this change, operating income increased in the High performance plastics segment by ¥397 million ($3,756 thousand).

Year ended March 31, 2003	Millions of yen							
	Semiconductor and display materials	Circuits and electronic component materials	High performance plastics	Quality of life products	Others	Total	Eliminations or corporate	Consolidated
Sale:								
Outside customers	¥49,229	¥38,310	¥42,829	¥29,386	¥625	¥160,379	¥ –	¥160,379
Inter-segment	26	–	980	467	332	1,805	(1,805)	–
Total sales	49,255	38,310	43,809	29,853	957	162,184	(1,805)	160,379
Operating expenses	40,653	38,349	42,517	28,918	801	151,238	2,778	154,016
Operating income (loss)	¥ 8,602	¥ (39)	¥ 1,292	¥ 935	¥156	¥ 10,946	¥ (4,583)	¥ 6,363
Identifiable assets	¥50,909	¥49,896	¥50,709	¥35,905	¥688	¥188,107	¥10,213	¥198,320
Depreciation and amortization	2,877	3,077	2,984	1,119	94	10,151	350	10,501
Capital expenditures	1,987	3,149	2,498	684	65	8,383	290	8,673

"Eliminations or corporate" in the "Operating expenses" column of the above information included corporate expenses of ¥4,577 million in the year ended March 31, 2003, which consisted principally of basic research and development costs and general and administrative costs accounted by the Company.

"Eliminations or corporate" in the "Identifiable assets" column of the above information included corporate assets of ¥10,464 million at March 31, 2003, which consisted principally of cash, time deposits, loans receivable, investments in securities, basic research and development assets and general and administrative assets held by the Company.

As described in Note 3, the Company changed the method of valuation for finished goods, semi-finished goods and work in process from the weighted average method to the moving-average method from the year ended March 31, 2003.

As a result of this change, operating income increased in the Semiconductor and display materials segment by ¥84 million, and decreased in the Circuits and electronic component materials segment by ¥20 million, decreased in the High performance plastics segment by ¥49 million, and increased in the Quality of life products segment by ¥97 million.

	Thousands of U.S. dollars							
Year ended March 31, 2004	Semiconductor and display materials	Circuits and electronic component materials	High performance plastics	Quality of life products	Others	Total	Eliminations or corporate	Consolidated
Sale:								
Outside customers	$525,014	$380,520	$420,009	$278,685	$6,453	$1,610,681	$ –	$1,610,681
Inter-segment	237	–	10,748	3,954	624	15,563	(15,563)	–
Total sales	525,251	380,520	430,757	282,639	7,077	1,626,244	(15,563)	1,610,681
Operating expenses	411,703	353,444	416,585	264,021	4,758	1,450,511	18,940	1,469,451
Operating income	$113,548	$ 27,076	$ 14,172	$ 18,618	$2,319	$ 175,733	$ (34,503)	$ 141,230
Identifiable assets	$479,291	$448,098	$504,579	$712,025	$7,152	$2,151,145	$164,011	$2,315,156
Depreciation and amortization	25,156	25,951	24,929	11,249	785	88,070	3,065	91,135
Capital expenditures	16,102	13,245	18,411	11,712	946	60,416	2,157	62,573

Information by geographic area for the years ended March 31, 2004, 2003 is as follows:

	Millions of yen						
Year ended March 31, 2004	Domestic	Asia	North America	Others	Total	Eliminations or corporate	Consolidated
Sale:							
Outside customers	¥ 96,865	¥49,867	¥14,529	¥ 8,988	¥170,249	¥ –	¥170,249
Inter-segment	13,104	10,253	310	108	23,775	(23,775)	–
Total sales	109,969	60,120	14,839	9,096	194,024	(23,775)	170,249
Operating expenses	99,037	52,442	15,044	9,153	175,676	(20,355)	155,321
Operating income	¥ 10,932	¥ 7,678	¥ (205)	¥ (57)	¥ 18,348	¥ (3,420)	¥ 14,928
Identifiable assets	¥192,357	¥53,309	¥16,473	¥10,114	¥272,253	¥(27,541)	¥244,712

"Eliminations or corporate" in the "Operating expenses" column of the above information included corporate expenses of ¥3,643 million ($34,465 thousand) in the year ended March 31, 2004, which consisted principally of basic research and development costs and general and administrative costs accounted by the Company.

"Eliminations or corporate" in the "Identifiable assets" column of the above information included corporate assets of ¥17,758 million ($168,004 thousand) at March 31, 2004, which consisted principally of cash, time deposits, loans receivable, investments in securities, basic research and development assets and general and administrative assets held by the Company.

As described in Note 2, some consolidated overseas subsidiaries changed the estimated useful lives of buildings, machinery and equipment from the year ended March 31, 2004.

As a result of this change, operating income increased in the Asia segment by ¥10 million ($95 thousand) and in the North America segment by ¥380 million ($3,595 thousand) and in the Others segment by ¥7 million ($66 thousand).

	Millions of yen						
Year ended March 31, 2003	Domestic	Asia	North America	Others	Total	Eliminations or corporate	Consolidated
Sale:							
Outside customers	¥ 93,445	¥44,793	¥15,790	¥6,351	¥160,379	¥ –	¥160,379
Inter-segment	12,477	4,738	460	71	17,746	(17,746)	–
Total sales	105,922	49,531	16,250	6,422	178,125	(17,746)	160,379
Operating expenses	99,529	45,581	15,967	6,410	167,487	(13,471)	154,016
Operating income	¥ 6,393	¥ 3,950	¥ 283	¥ 12	¥ 10,638	¥ (4,275)	¥ 6,363
Identifiable assets	¥154,427	¥47,365	¥18,694	¥3,935	¥224,421	¥(26,101)	¥198,320

"Eliminations or corporate" in the "Operating expenses" column of the above information included corporate expenses of ¥4,577 million in the year ended March 31, 2003, which consisted principally of basic research and development costs and general and administrative costs accounted by the Company.

"Eliminations or corporate" in the "Identifiable assets" column of the above information included corporate assets of ¥10,464 million at March 31, 2003, which consisted principally of cash, time deposits, loans receivable, investments in securities, basic research and development assets and general and administrative assets held by the Company.

As described in Note 3, the Company changed the method of valuation for finished goods, semi-finished goods and work in process from the weighted average method to the moving-average method from the year ended March 31, 2003.

As a result of this change, operating income increased in the Domestic segment by ¥152 million.

	Thousands of U.S. dollars						
Year ended March 31, 2004	Domestic	Asia	North America	Others	Total	Eliminations or corporate	Consolidated
Sale:							
Outside customers	$ 916,414	$471,779	$137,455	$85,033	$1,610,681	$ –	$1,610,681
Inter-segment	123,974	97,001	2,933	1,022	224,930	(224,930)	–
Total sales	1,040,388	568,780	140,388	86,055	1,835,611	(224,930)	1,610,681
Operating expenses	936,963	496,140	142,328	86,594	1,662,025	(192,574)	1,469,451
Operating income	$ 103,425	$ 72,640	$ (1,940)	$ (539)	$ 173,586	$ (32,356)	$ 141,230
Identifiable assets	$1,819,839	$504,342	$155,847	$95,686	$2,575,714	$(260,558)	$2,315,156

Overseas sales for the years ended March 31, 2004 and 2003 were as follows:

Year ended March 31, 2004	Millions of yen			
	Asia	North America	Other	Total
Overseas sales	¥62,343	¥14,870	¥8,536	¥ 85,749
Consolidated net sales				170,249
Percent against consolidated net sales	36.6%	8.7%	5.0%	50.3%

Year ended March 31, 2003	Millions of yen			
	Asia	North America	Other	Total
Overseas sales	¥54,490	¥15,684	¥6,546	¥ 76,720
Consolidated net sales				160,379
Percent against consolidated net sales	34.0%	9.8%	4.1%	47.9%

Year ended March 31, 2004	Thousands of U.S. dollars			
	Asia	North America	Other	Total
Overseas sales	$589,811	$140,681	$80,757	$ 811,249
Consolidated net sales				1,610,681
Percent against consolidated net sales	36.6%	8.7%	5.0%	50.3%

14. Contingent liabilities

At March 31, 2004, the Companies were contingently liable as follows:

(i) Repurchase of notes discounted and endorsed:	¥176 million	($1,665 thousand)
(ii) Repurchase of installment accounts receivable sold to a commercial finance company:	¥ 50 million	($ 473 thousand)
(iii) Guarantees for bank borrowings of employees:	¥ 2 million	($ 19 thousand)
(iv) Guarantee for bank borrowings of an association:	¥389 million	($3,680 thousand)

15. Subsequent events

At the general meeting of shareholders of the Company held on June 29, 2004, retained earnings at March 31, 2004, were appropriated as follows:

	Millions of yen	Thousands of U.S. dollars
Year-end cash dividends ¥5 ($0.04) per share	¥1,187	$11,230
Bonuses to directors and statutory auditors	70	662

Independent Auditors' Report

Sumitomo Bakelite Company, Limited and Consolidated Subsidiaries
Years ended March 31, 2004, 2003 and 2002

To the Board of Directors of
Sumitomo Bakelite Company, Limited:

We have audited the accompanying consolidated balance sheets of Sumitomo Bakelite Company, Limited (a Japanese corporation) and consolidated subsidiaries as of March 31, 2004 and 2003, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended March 31, 2004, expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to independently 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 Sumitomo Bakelite Company, Limited and consolidated subsidiaries as of March 31, 2004 and 2003, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2004, in conformity with accounting principles generally accepted in Japan.

Without qualifying our opinion, we draw attention to the following.
As explained in Note 3 to the consolidated financial statements, effective April 1, 2002, Sumitomo Bakelite Company, Limited changed the method of valuation for finished goods, semi-finished goods and work in process.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2004 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1 to the consolidated financial statements.

KPMG AZSA & Co.

KPMG AZSA & Co.

Tokyo, Japan
June 29, 2004

Environmental Accounting

Sumitomo Bakelite Company, Limited

In fiscal 2000, Sumitomo Bakelite introduced environmental accounting as an effective tool to implement business activities in line with environment conservation. Environmental accounting quantifies the cost and effect associated with environmental conservation activities. It is an excellent tool to promote environmentally conscious business activities more efficiently and enhance the understanding of our efforts through disclosure to our stakeholders.

With reference to “Environmental Accounting Guidelines 2000, 2002” released by the Ministry of the Environment, we established a framework for quantitatively measuring progress to reduce environmental burden. Under the framework, we continuously make efforts to evaluate environmental conservation activities based on our own compilation methods and enhance the effectiveness of our compilation methods through ongoing reviews and reassessment.

In fiscal 2000, we introduced environmental accounting at our five plants and two laboratories and subsequently, expanded its scope to all of our domestic business establishments including our affiliated companies (listed below).

Environmental Conservation Costs for Fiscal 2003

Activity	Investment (Millions of yen)	Expenses (Millions of yen)	Description
(A) Reduction of environmentally hazardous emissions	¥57	¥ 187	• Renovation of waste-water treatment equipment • Installation of drainage
(B) Energy conservation	28	27	• Installation of cogeneration system • Equipment of air conditioners
(C) Reduction of industrial waste, promotion of recycling, and waste treatment	10	560	• Removal of incinerator • Waste treatment
(D) Product evaluation at R&D stage	–	1,173	• R&D for environmentally friendly products
(E) Reduction of the up/downstream environmental burden	–	17	• Consignment fee to the Japan Containers and Packaging Recycling Association
(F) Environmental management activities	0	258	• Personnel cost for environmental management activities • Greening activities and maintenance for green space
(G) Contributions to social activities	–	1	• Activities for external communications
(H) Response to environmental damage	–	–	
Total	¥95	¥2,223	

Period: April 2003 to March 2004

Scope of Compilation: Sumitomo Bakelite Co., Ltd.

Amagasaki Plant, including subsidiaries and affiliated companies on the premise; Shizuoka Plant, including subsidiaries and affiliated companies on the premise; Utsunomiya Plant and Tsu Plant; Fundamental Research Laboratory and Kobe Fundamental Research Laboratory of Sumitomo Bakelite Co., Ltd.; Akita Sumitomo Bakelite Co., Ltd.; Artlite Kogyo Co., Ltd.; Tokyo Kakohin Co., Ltd.; Hokkai Taiyo Plastic Co., Ltd.; Yamaroku Kasei Industry Co., Ltd.; Kyushu Bakelite Industry Co., Ltd.

Compilation Method

- Compilations were implemented by the Company's Environmental Accounting Compilation Guideline based on Environmental Accounting Guidelines 2000, 2002 released by the Ministry of the Environment.
- With regard to the complex costs that include costs other than for environmental conservation purposes, they were compiled after deducting for costs as usual.
- Economic effects were recorded for items compiled based on substantial evidence. Such presumptive calculations as risk avoidance effects for items were excluded.
- Expenses do not include depreciation costs.
- With regard to R&D, investment outlays and expenses were compiled in environment-related categories.

Effects of Environmental Conservation in Fiscal 2003

Reduction in Environmental Burden (Compared to the previous fiscal year)	**Environmental Burden** (Fiscal 2003)
Reduction in atmospheric emissions of solvents and others 380 tons	Atmospheric emissions of solvents and others 1,018 tons
Reduction in carbon dioxide emissions 3,584 tons	Carbon dioxide emissions 123,585 tons
Reduction in industrial waste generated 1,022 tons	Industrial waste generated 7,449 tons
Reduction in landfill and external incineration of waste 1,850 tons	Landfill and external incineration of waste 563 tons

Economic Effects in Fiscal 2003

Item	**Amount** (Millions of yen)
(1) Reduction in costs due to energy conservation	¥ 42
(2) Reduction in costs through waste reduction	49
(3) Income from recycling	52
(4) Reduction in costs through internal recycling	290
(5) Reduction in costs through circulation of factory drain water	15
Total	¥448

The *Environmental Report 2004* of Sumitomo Bakelite Co., Ltd., including its environmental accounting, was independently reviewed by AZSA Sustainability Co., Ltd.

Board of Directors, Executive Officers and Corporate Auditors

Chairman
Tsuneo Moriya

President
Tomitaro Ogawa

Senior Managing Director
Iwao Yamaguchi

Managing Directors
Shigeru Hayashi
Takeichi Higashiguchi
Hideaki Ezaki

Directors
Akio Kosai
Osamu Kono

Managing Executive Officers
Takeshi Uchimura
Atsumi Okayama

Executive Officers
Toyoji Okunishi
Nobuaki Sugimoto
Tamotsu Yahata
Masuo Mizuno
Tsuneo Terasawa
Koichiro Sekine
Masaei Yamada
Shinichiro Ito
Kazuhisa Hirano
Shigeki Muto

Corporate Auditors
Takaharu Hayashi
Shoji Kosaka
Yamato Mato
Fumio Ogawa

(As of June 29, 2004)

Corporate Data

Head Office:
Tennoz Parkside Building, 2-5-8
Higashishinagawa, Shinagawa-ku,
Tokyo 140-0002, JAPAN

General Affairs Dept.
Phone: +81-(0)3-5462-3434
Facsimile: +81-(0)3-5462-4873

Corporate Finance & Planning Div.
Phone: +81-(0)3-5462-3449
Facsimile: +81-(0)3-5462-4876

Offices:
Osaka Office
2-3-47 Higashi-tsukaguchi-cho,
Amagasaki, Hyogo 661-8588, JAPAN
Phone: +81-(0)6-6429-6941
Facsimile: +81-(0)6-6427-8055

Nagoya Office
87 Choda-cho, Meito-ku,
Nagoya, Aichi 465-0027, JAPAN
Phone: +81-(0)52-726-8351
Facsimile: +81-(0)52-726-8396

Laboratories:
Fundamental Research Laboratory
495 Akiba-cho, Totsuka-ku,
Yokohama, Kanagawa 245-0052,
JAPAN
Phone: +81-(0)45-811-1661
Facsimile: +81-(0)45-812-4898

Kobe Fundamental Research Laboratory
1-1-5 Murotani, Nishi-ku,
Kobe, Hyogo 651-2241, JAPAN
Phone: +81-(0)78-992-3900
Facsimile: +81-(0)78-992-3919

Thermoplastic Products Research Laboratory
(Located at Amagasaki Plant)

Circuitry Materials Research Laboratory
(Located at Shizuoka Plant)

Molding Compound & Molding Parts Research Laboratory
(Located at Shizuoka Plant)

Industrial Resin Research Laboratory
(Located at Shizuoka Plant)

Corporate Research Center
Information & Communications Materials
Electronic Device Materials Research Laboratory I
Electronic Device Materials Research Laboratory II
Electronic Device Materials Research Laboratory III
(Located at Utsunomiya Plant)

Plants:
Amagasaki Plant
2-3-47 Higashi-tsukaguchi-cho,
Amagasaki, Hyogo 661-8588, JAPAN
Phone: +81-(0)6-6429-6941
Facsimile: +81-(0)6-6427-8055

Shizuoka Plant
2100 Takayanagi, Fujieda,
Shizuoka 426-0041, JAPAN
Phone: +81-(0)54-635-2420
Facsimile: +81-(0)54-636-0294

Utsunomiya Plant
20-7, Kiyohara-Kogyodanchi,
Utsunomiya, Tochigi 321-3231, JAPAN
Phone: +81-(0)28-667-6211
Facsimile: +81-(0)28-667-5519

Tsu Plant
5-7-1 Takachaya, Tsu,
Mie 514-0819, JAPAN
Phone: +81-(0)59-234-2181
Facsimile: +81-(0)59-234-8728

Incorporated:
January 25, 1932

Number of Employees:
2,349

Major Subsidiaries and Affiliates:
** Advanced Plastics Compound Company
* Akita Sumitomo Bakelite Co., Ltd.
* Artlite Kogyo Co., Ltd.
* Bakelite Precision Molding (Shanghai) Co., Ltd.
Bakelite Shoji (Thailand) Co., Ltd.
Bakelite Trading (Shanghai) Co., Ltd.
* BASEC Hong Kong Limited
CMK Europe N.V.
** CMK Singapore (Pte.) Ltd.
** CMKS (Malaysia) Sdn. Bhd.
* Decolanitto Corporation
* Durez Corporation
* Durez Canada Co., Ltd.
* Fenocast, S.A.
* Fers Resins, S.A.
* Hokkai Taiyo Plastic Co., Ltd.
Japan Communication Accessories Manufacturing Co., Ltd.
* Kyushu Bakelite Industry Co., Ltd.
** Nippon Denkai Co., Ltd.
Otomo Chemical Co., Ltd.
* P.T. Indopherin Jaya
** P.T. Pamolite Adhesive Industry
* Promerus, Llc.
* Rigidtex Sdn. Bhd.
* SB Durez Holding, Inc.
* SB Flex Philippines, Inc.
S.B. Information System Co., Ltd.
S.B. Recycle Co., Ltd.
* S.B. Techno-Research Co., Ltd.
SBTEG Co., Ltd.
* SNC Industrial Laminates Sdn. Bhd.
SPD Co., Ltd.
* ST Film Sheet Co., Ltd.
Sumibe Service Co., Ltd.
* Sumicarrier Singapore Pte. Ltd.
* Sumicarrier (Thailand) Co., Ltd.
* SumiDurez Singapore Pte. Ltd.
* N.V. Sumitomo Bakelite Europe S.A.
* Sumitomo Bakelite Europe (Barcelona), S.L.
* Sumitomo Bakelite Hong Kong Co., Ltd.
Sumitomo Bakelite Macau Co., Ltd.
* Sumitomo Bakelite Singapore Pte. Ltd.
* Sumitomo Bakelite (Suzhou) Co., Ltd.
* Sumitomo Bakelite (Taiwan) Co., Ltd.
* Sumitomo Bakelite Vietnam Co., Ltd.
* Sumitomo Plastics America, Inc.
** Sunbake Co., Ltd.
* Tokyo Kakohin Co., Ltd.
* Tsu-Kong Co., Ltd.
* Tsutsunaka Plastic Industry Co., Ltd.
* Yamaroku Kasei Industry Co., Ltd.

* Consolidated Subsidiaries
** Affiliates to which the equity method is applied

(As of June 29, 2004)

SUMITOMO BAKELITE CO., LTD.

Responsible Care

Printed in Japan on recycled paper