

Annual Report 2006

For the fiscal year ended March 31, 2006



DENKA
DENKI KAGAKU KOGYO KABUSHIKI KAISHA

The Denka Group, of which DENKI KAGAKU KOGYO KABUSHIKI KAISHA forms the central core, pushes forward with its daily business activities so that it can enrich people's lives and the development of society as a whole by developing and providing a broad spectrum of materials centered on chemical products. The Denka Group is making huge strides in the expansion of its businesses and technologies not only in the fields of organic materials, inorganic materials and cement, but also in areas familiar to people including the fields that constitute the very foundation of society and industry such as medicine, engineering, semi-conductors and electronics.

The globalization of economics has brought with it an integration of global market leading in turn to changes in the various constituent elements of the management environment encompassing the Denka Group. Against this background, we in the Denka Group feel that it is both our mission and goal to constantly challenge the next stage in our development to maintain unceasing growth and create corporate values as well as to establish an ongoing reputation for corporate excellence not only with our shareholders, customers and employees, but also with society and the global community. The Denka group is committed to make further leaps forward as a corporation "Trusted by Humans, Society and the Earth."

Contents

Profile	1
Financial Highlights	2
President's Message	3
DENKA Products in Life	5
Operational Review	7
Research and Development	9
Measures for Environmental Issues	10
Global Operations	11
Five-year Summary	12
Financial Review	13
Consolidated Financial Statements (Summary)	15
Corporate Data/Board of Directors	17
Shareholder Information	18

Organic Materials Business

Raw materials for synthetic resin, synthetic resin, acetic chemical products, synthetic rubber, etc.



Electronic Materials Business

Electronic components, electronic packaging materials, functional ceramics



Inorganic Materials Business

Fertilizer and inorganic chemical products, cement, special cement additives



Functional Materials and Processed Products Business

Packaging materials, housing materials, industrial materials, medical and pharmaceutical products



Disclaimer Regarding Forward-Looking Statements

This annual report contains forward-looking statements related to management's expectations about future business conditions. Actual business conditions may differ significantly from management's expectations and accordingly affect the Company's sales and profitability. Actual results may differ as a result of factors over which the Company has no control, including unexpected changes in competitive and economic conditions, government regulations, technology and other factors.

Financial Highlights

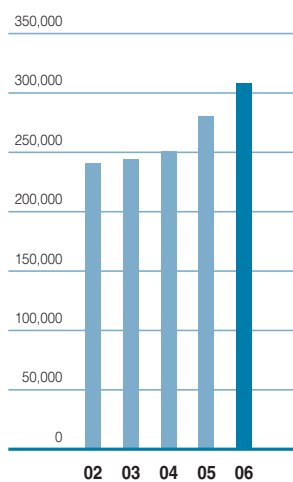
Denki Kagaku Kogyo Kabushiki Kaisha and Consolidated Subsidiaries

Millions of Yen

Years ended March 31, 2006 and 2005	2006	2005
Net Sales	¥ 307,923	¥ 280,033
Operating Income	26,069	25,585
Ordinary Profit	23,913	21,897
Net Income	15,365	13,587
Total Assets	349,689	328,248
Total Shareholders' Equity	146,148	130,715
Net Income per Share	31.08	27.70
Shareholders' Equity per Share	297.23	265.71

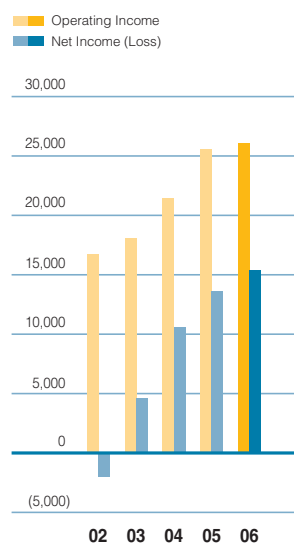
Net Sales

Millions of Yen



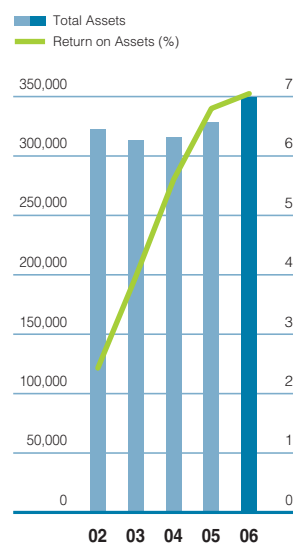
Operating Income and Net Income (Loss)

Millions of Yen



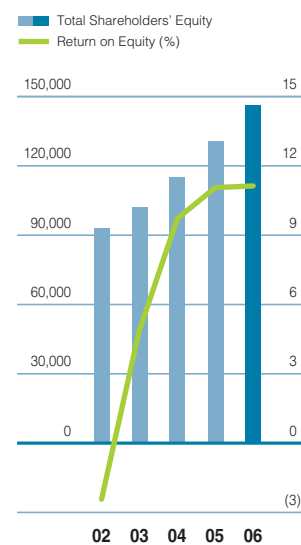
Total Assets and Return on Assets

Millions of Yen



Total Shareholders' Equity and Return on Equity

Millions of Yen



We challenge the next stage in our development and create corporate values.



Seiki Kawabata, President

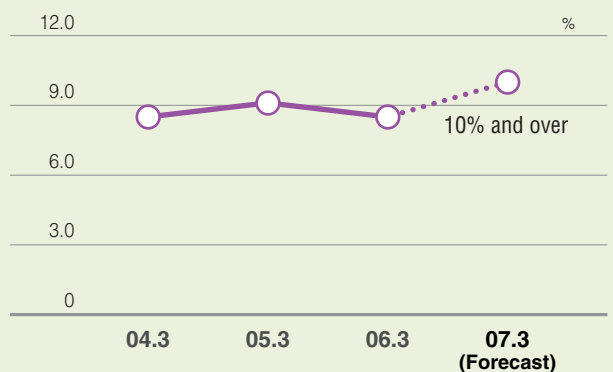
In presenting the Annual Report for the fiscal year ended March 31, 2006, I would first like to take this opportunity to say a few words.

In 2005 we celebrated the 90th anniversary of Denka's foundation. I am very pleased to say that we have recorded a fourth consecutive year of increase in net sales and earnings in this memorable fiscal year. We thank our shareholders for supporting Denka in achieving this result.

Since April 2004, we have been pursuing DENKA New Stage 2006 (NS06), a three-year plan implemented with the objective of strengthening our profitability and financial standings. To achieve this objective, we have set numerical targets for operating margin, shareholders' equity ratio and interest-bearing debt ceiling, as well as having defined strategies to grow further through aggressive investment in the three priority areas of "Electronic materials," "Functional resins" and "Processed resin products."

Operating results and DENKA New Stage 2006 plan

Operating margin



Effort to maintain unceasing growth

In the past two years of this NS06 campaign, our financial standings clearly improved as indicated by a shareholders' equity ratio of 41.79%, up 5.38 percentage points from the start of the campaign. Interest-bearing debt outstanding was reduced by ¥29.4 billion during the two-year period to ¥91 billion. An operating margin of 8.5% indicates that we now have a system in place that enables us to secure stable profits. Eyeing market needs and looking ahead for further growth in the years to come, we have been promoting synergistic effects by concentrating our electronic materials business at the Shibukawa Plant and expanding investments in our fused silica and functional resin businesses in Singapore.

While our NS06 plan has been successful, our core business areas such as limestone and carbide showed growth in both sales and earnings, and contributed considerably to overall financial results. Hence, we realize there is more

to be done and believe we need to exert greater efforts in enhancing our three priority areas. Meanwhile, raw material prices are rising due to the soaring cost of crude oil. The global economy remains unstable, interest rates are rising and likewise, the elements of uncertainty are increasing in the general business environment within which the Company operates. We therefore expect that the road ahead of us will not necessarily be smooth.

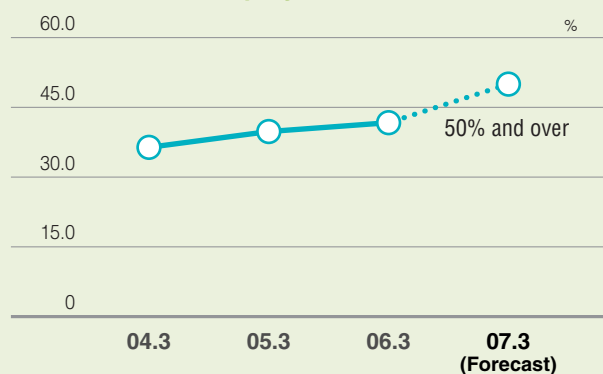
As we proceed through the final year of NS06, all of us at Denka are committed to do our best in leading an even better year. We greatly appreciate the continued understanding and support of our shareholders, investors and other stakeholders.

June 2006

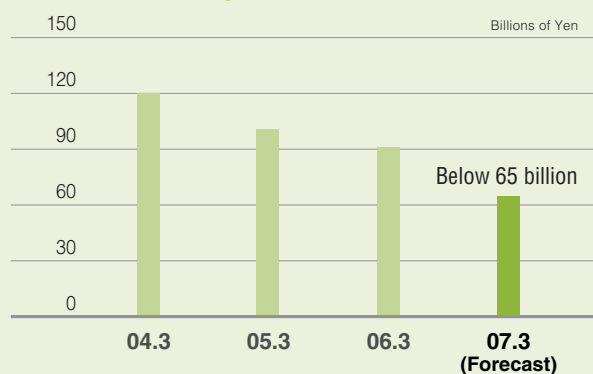


Seiki Kawabata, President

Shareholders' equity ratio

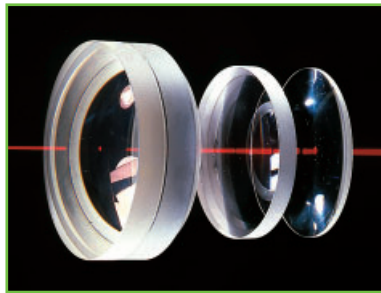


Interest-bearing debt



DENKA's materials are used in electrical home appliances essential for households and in the latest digital cameras and game devices, and through these products we contribute to the day-to-day lives of consumers.

Consumers may not be familiar with our products since many of Denka's materials are added in the manufacturing phase and are not clearly visible in the finished product. We would therefore like to introduce here a diverse selection of our product lineups in a series of familiar "living space" categories. This initial series showcases: "Denka products in life."



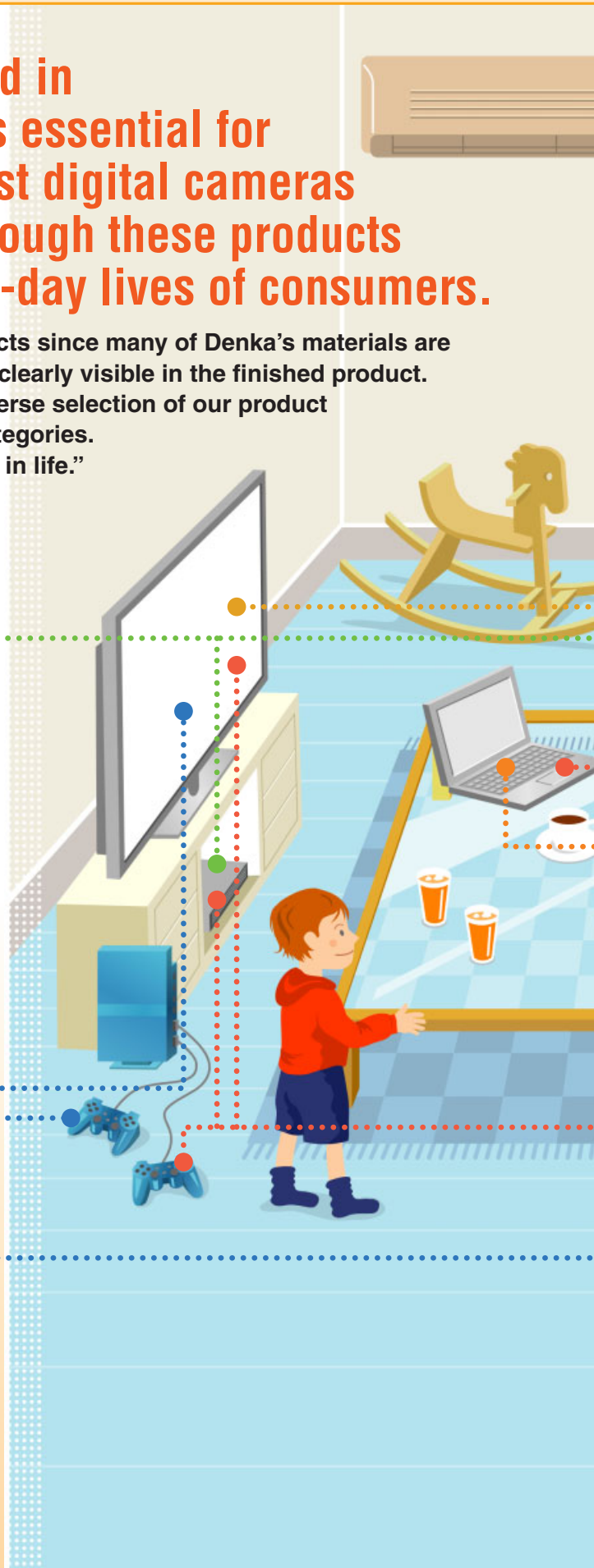
Digital cameras and DVD players
"HARD LOC OP,"
a UV light curing adhesive

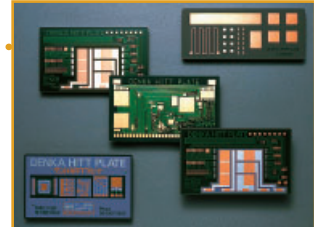
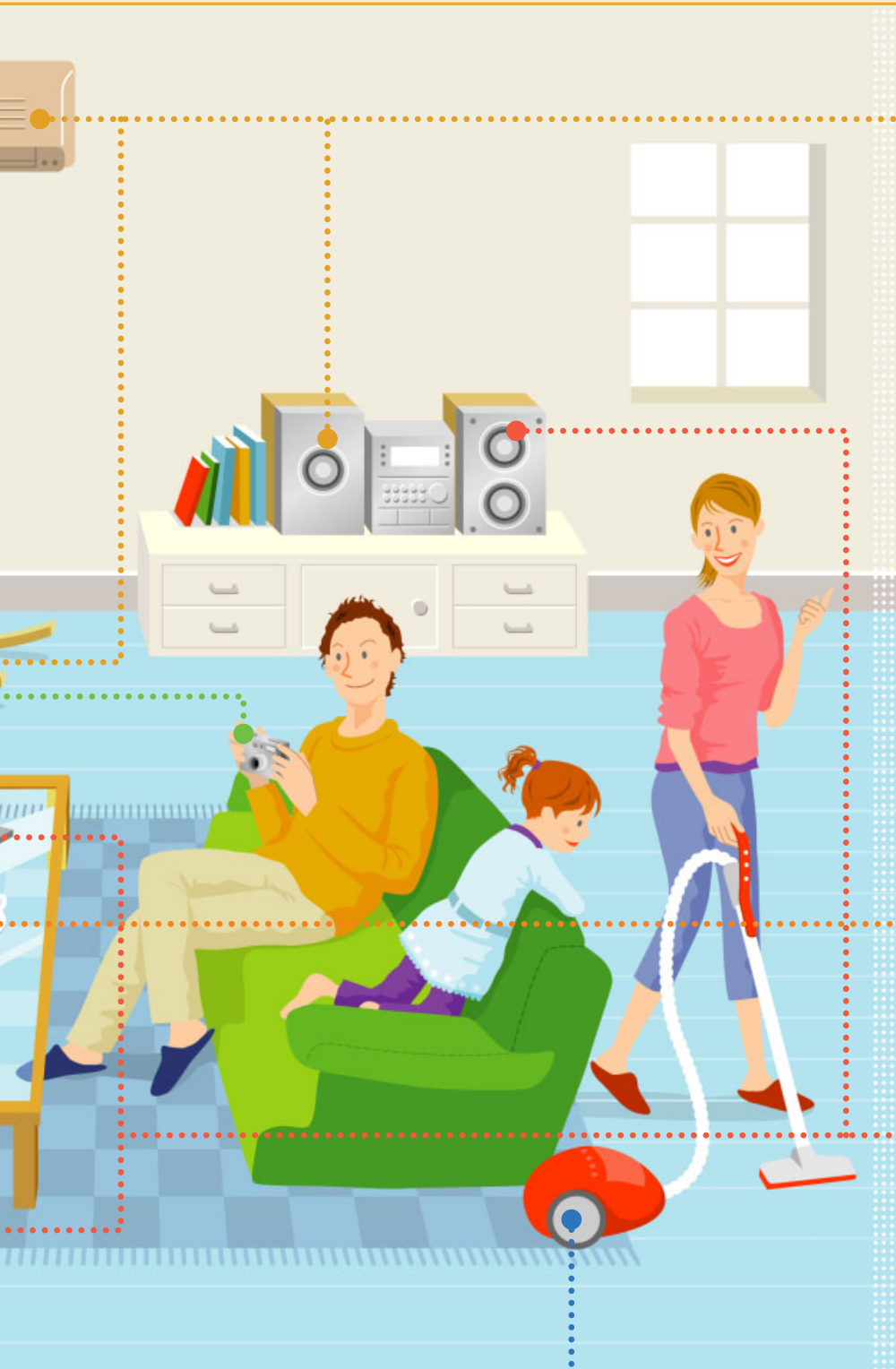
This product is an adhesive for optical parts such as digital camera lenses and pickup lenses (reading devices) in DVD players.



Flat panel display televisions,
gaming devices and vacuum cleaners
Transparent resins

This product is widely used in flat panel display televisions and transparently encased gaming devices, and in the exterior frames of other electrical home appliances such as vacuum cleaners.





Audio equipment, air conditioners and flat panel display televisions

“HITT Plate,” a highly thermally conductive aluminum substrate

This product is used as a circuit board for high current, high voltage electronic devices such as inverters for air conditioners, high fidelity amplifiers and plasma displays.



Personal computers

Fused silica filler

This product is used as a sealant to protect semiconductors in CPU, memory and other units.



PCs, DVD players and audio equipment

Thermally conductive sheets and spacers

This material is used to carry away waste heat for elimination, and is commonly attached to the CPU in personal computers, DVD pickup, audio amplifier, semiconductor power sources and similar devices.

Organic Materials Business

Earnings from styrene-monomer increased as a result of both a surge in exports, mainly to China, and product price corrections in line with the rise in raw material costs. Earnings from ultrahigh molecular weight polystyrene resin produced by Denka Singapore Private Limited also increased due to the expanded sales volume. Net sales of AS resin and versatile ABS resin increased in both domestic and overseas markets due to product price adjustments.

In the area of functional resins, exports of transparent resins expanded, mainly for optical lens applications. Sales also expanded for "CLEAREN," a special resin primarily used in shrink films on plastic bottles, and heat resistant ABS resin for automobiles also marked an increase in sales volume. In addition, corrected sale prices for key products contributed to the overall rise in net sales of functional resins.

In chemicals, the rise in sale prices for acetic acid and vinyl acetate monomer resulted in increased earnings. While price revision was made for polyvinyl alcohol (POVAL) in both domestic and overseas markets, sales dropped in terms of volume as well as in income.

In organic chemicals, the increase in net sales of chloroprene rubber for automotive and adhesive purposes was attributed to the expanded sales volume and the rise in product prices, mainly for export items. Sales volume of "ER," a special rubber highly resistant against heat and oil, soared due to high demand for automotive hose applications. Acetylene black, a conductive material, achieved increased sales supported by product price adjustments in both domestic and overseas markets.

As a result, net sales for the business amounted to ¥135,527 million, up 14.4% from the previous year.

Inorganic Materials Business

As for fertilizers, "Toretaro," a high silicate fertilizer, showed increased sales well on track. However calcium cyanamide and fused magnesium phosphate declined in sales due to the worsening of the agricultural environment. Sales from carbide increased both in volume and amount of income. While thermally resistant materials such as alumina cement sold less in volume, product price revisions pushed up their net sales values. The sales volume increased for crystalline alumina short fiber used in baking furnaces for electronic component manufacturing and in automobiles.

The net sales for cement products increased as a result of steady demand in the private sector as well as demand for reconstruction work in the disaster-hit areas of Niigata, one of Denka's major sales regions.

Sales volumes for special cement additives increased: Non-shrink grouting material was in high demand for quake-proof reinforcement work, quick-setting material for spray concrete was in demand for tunnel constructions on highways, and repair materials and acrylic adhesives were in need by repair and reinforcement businesses.

As a result, net sales for the business totaled ¥49,557 million, an increase of 6.2% from a year earlier.

Electronic Materials Business

In electronic components, sales of thermally resistant products such as electronic circuit boards and thermally conductive sheets surged for use in IT products, industrial power sources and railroad vehicles. The sales volume for "HARD LOC," a construction glue, increased mainly for automotive speaker applications

Topics

New and Additional Plant Facilities in Singapore

As part of the core strategy of "strengthening priority areas of growth" defined under its three-year DENKA New Stage 2006 plan, Denka has been promoting new product development as well as expanded production at Denka Singapore Private Limited (DSPL) and Denka Advantech Private Limited (DAPL), both affiliates in Singapore.

DSPL began in March 2005 building an additional facility for "Denka MW," a ultrahigh molecular weight polystyrene, and constructing new plants for "CLEAREN," a highly functional transparent resin used in plastic bottle labels and transparent resin (MS resin) used in flat panel displays. The MW facility started live operation in March 2006 and the two new plants are on their way to live operation, which is set to begin in the first half of fiscal 2006.

Meanwhile, DAPL began in January 2006 to expand its facility for the spherically fused silica filler used in semiconductor sealants, in response to the growing demand



Plant construction on its way (DSPL)

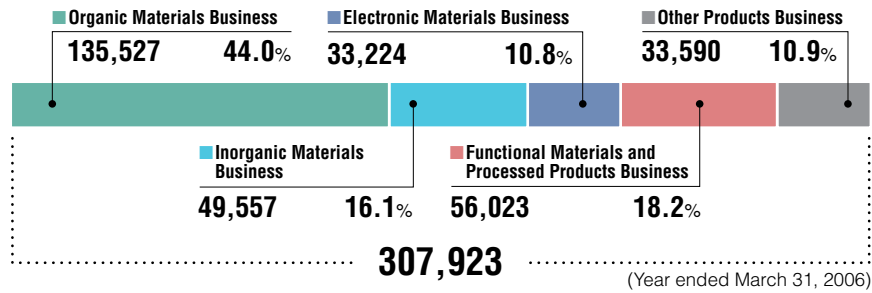


Facility for fused silica filler to be expanded (DAPL)

in both domestic and overseas markets. We are working towards our goal to have the construction work completed also in the first half of fiscal 2006.

Denka is determined to proceed with its construction efforts in a safe and timely manner to establish a system that can respond promptly and effectively to market needs as well as readily contribute to achieving good business results.

Sales by
Product
Category
(Millions of Yen)



and resulted in increased earnings. UV light curing adhesives for optical lenses also marked a higher sales volume for the year. Monosilane gas offered by Denal Silane Co., Ltd. continued to be in good demand.

In electronic packaging supplies, demand for covering tape used in transporting electronic components and for adhesive tape for semiconductors was rapidly restored in the latter half of the year under review, which led to the surge in sales volumes.

In functional ceramics, demand for high-quality spherical fused silica filler for semiconductor sealants expanded in both domestic and overseas markets, causing the Omuta Plant as well as Denka Advantech Private Limited (DAPL) in Singapore to continue operating at full production.

As a result, net sales for the business amounted to ¥33,224 million, up 11.6% from the previous year.

Functional Materials and Processed Products Business

In food packaging materials, sales increased in quantity for OPS (biaxially-oriented polystyrene sheet)

in terms of both the raw material and processed products.

Sales and earnings were down in housing materials compared to the previous year, when demand for plastic rain drainage pipes expanded due to the country being hit by major typhoons. Sales of corrugated tubes for agriculture and engineering work also declined in both volume and amount of income.

With regard to industrial materials, earnings of adhesive tape for industrial use increased, supported by strong sales and product price corrections, while sales of synthetic fiber used in wigs declined.

In pharmaceutical products, "SUVENYL," a joint function enhancer (macromolecular hyaluronic acid preparation) favorably increased in sales volume. On the other hand, a considerable portion of influenza vaccine, a core product of Denka Seiken Co., Ltd. did not pass state inspection, which resulted in a decline in sales.

As a result, net sales for the business totaled ¥56,023 million, down 0.7% from the previous year.

Live Operation at Expanded Production Facilities for Food Packaging Supplies — Aiming to further Strengthen the Processed Resin Products Business

Denka completed by February 2006 construction of a production facility for OPS (biaxially-oriented polystyrene sheet) at its Chiba Plant (Ichihara City, Chiba), and reinforcing work for the adjacent molding and processing facility of Denka Polymer Co., Ltd. Consequently production at each of these facilities has been expanding as scheduled.

OPS is a highly durable, lightweight plastic food packaging material molded and transformed into forms such as food containers, trays and lunchboxes. As the material is transparent, it increases the commercial value of the packaged contents. In addition its lightweight, non-bulky qualities facilitate the distribution process as well as being received well by consumers shopping in supermarkets and convenience stores.

Through the expansion and reinforcement of production facilities, Denka will work in collaboration with Denka Polymer to further strengthen the Group's processed resin products business.



Food packaging using OPS



Expanded OPS production facility

Expansion of Production Capacity for Special Synthetic Rubber

At its Chiba Plant, Denka has been expanding production capacity for a special synthetic rubber, "ER."

"ER" is used mainly in automotive hoses in the engine room. While cars today are designed to be kinder to the environment, the temperature in the engine compartment is rising. "ER" is highly resistant to heat and oil and can therefore be highly functional even under severe conditions. In recent years it has therefore been in growing demand in both domestic and overseas markets.

Meanwhile, to respond to the diversified needs of the automotive industry, Denka also plans to demonstrate its expertise in the effective application of chloroprene rubber in automotive parts.



Products using "ER"



"ER" production plant

1. Basic Strategy

The DENKA Group is vigorously engaged in research and development activities with an emphasis on further strengthening its proprietary technologies and developing specialized, highly functional products, focusing on its three core business fields of “Electronic materials,” “Functional resins,” and “Processed resin products.”

2. R&D Organization

DENKA’s research and development organization consists of Central Research Laboratories and five Research Centers. The Central Research Institute conducts advanced research that can be applied across the business divisions, as well as further strengthening its proprietary core technologies and expanding their applications to the related fields. Research Centers located at plant sites handle technological developments specific to the products in close contact with the manufacturing sections.

3. Results for the Fiscal Year under Review

In fiscal 2005, the group’s total research and development expenditure came to 8,808 million yen (US \$75 million), and there were 577 research staff. During the year under review, 334 patents were disclosed, and 160 patents (including utility patents) were actually registered in Japan.

R&D activities in each division during the year under review and their achievements were as follows:

(1) Organic Materials Business

The focus in research and development has been on highly value-added styrene-based functional resins. Specifically, the Company has seen results in the ongoing development of production technology for materials such as transparent resin, “CLEAREN”, and heat resistant resins, as well as improvements in quality, and new product developments.

In organic chemicals, the Company has enhanced its production technology for a range of existing products including chloroprene, “ER,” and acetylene black, as well as for newly developed products.

(2) Inorganic Materials Business

In special cement additives, the Company is working on quality improvements for products, including “NATMIC”, “TASCON”, etc., and promoting to develop additives to meet the needs for concrete materials with high durability and hyper-strength.

Among fertilizers and inorganic chemicals, the Company is engaging in research and development activities to substantively enhance alumina fibers, and business operations for products such as alumina cement, as well as fertilizer.

(3) Electronic Materials Business

In electronic components, the Company has been engaging in new product development to meet market needs in a timely manner for ceramic and metal circuit boards, heat sinks, etc., as well as developing specific-function adhesives by applying technology of UV light curing adhesives.

In functional ceramics, DENKA has been focusing on development of its ceramic filler product group including silica and alumina, and BN (boron nitride) composite products.

In electronic packaging materials, the Company’s focus is on new product development for adhesive tape used in transporting electronics components or for protecting and fastening semiconductor wafers (for transportation).

(4) Functional Materials and Processed Products Business

In packaging materials, construction materials, and processed resin products for industrial material application, the Company is utilizing its expertise in multi-layer extrusion technology and adhesive technology to promote product developments that suit the market needs.

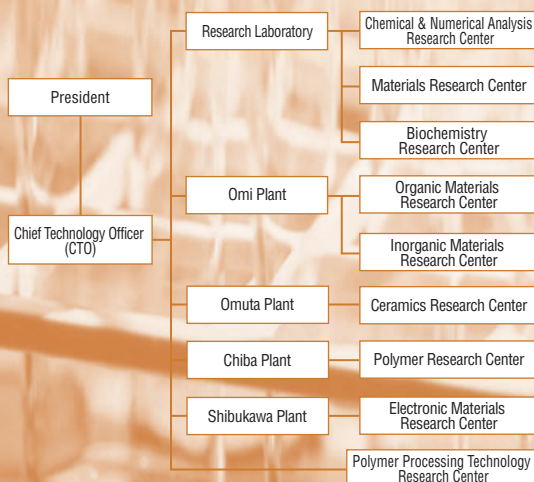
In pharmaceutical products, DENKA undertook research and development aiming to expand its share in fermented hyaluronic acid as joint function improvement agent, and also is engaging in developing new products using properties of hyaluronic acid.

Denka Seiken Co., Ltd. is conducting development in high quality human vaccines, reagents for the detection of bacteria and viruses, and clinical diagnostic reagents, etc.

(5) Other Business

Denka Engineering Co., Ltd., which is engaged in design and installation of industrial equipment, has been conducting research and development for efficient pneumatic transfer equipment for powders and granulate materials, as well as wastewater treatment facilities.

R&D Organization



Based on our philosophy, “Trusted by Humans, Society, and the Earth,” we have been contributing to people’s well-being and the progress of society by providing a number of valuable products.

In addition, since chemical substances have a potential negative impact on people’s health and the global environment, we have a responsibility to conduct our business activities while minimizing these risks.

Accordingly, we consider “environment, safety and health” as the backbone of the corporate management and have been promoting company-wide “responsible care (RC) activities,” which ensure environmental sustainability and the safety of the entire lifecycle of chemical substances from development through manufacture, distribution, use and final consumption to disposal.

In particular, we launched the secondary medium-term environmental plan with more aggressive objectives from fiscal 2005, focusing on our main target of “reducing emissions of chemical substances,” “promoting energy saving,” and “reducing waste,” and we steadily pursue our RC activities.

Reports on environmental activities in fiscal 2005 were as follows:

Reducing emissions of chemical substances

In fiscal 2005, our emissions of chemical substances designated by the PRTR* Law decreased by 35% from the previous year.

*PRTR: Pollutant Release and Transfer Register

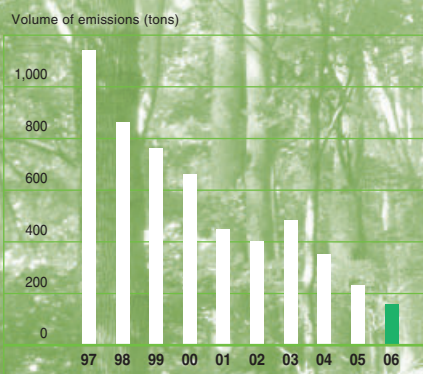
Promotion of energy saving

In fiscal 2005, our total energy consumption increased due to growth in production, which was offset by effective operation and management of equipment and curtailing some maintenance tasks in some facilities. As a result, our unit energy consumption improved by 2.5% from the previous year.

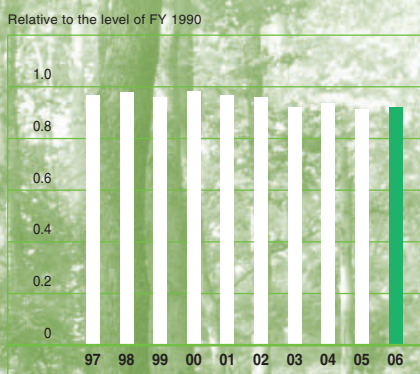
Reduction of waste

Supported by each plant’s efforts to reduce waste generation and improve the recycling rate, we achieved targeted waste reduction, and the quantity of leftover waste for final disposal in fiscal 2005 declined 1.2% year-on-year.

Emissions of chemical substances under the PRTR Law



Unit energy consumption



Excellent products with global competitiveness

The DENKA group produces various products with global competitiveness, such as chloroprene rubber (70% of the Company's production volume is shipped abroad), spherical type fused silica filler (accounting for more than 50% of the global market share; used for semiconductor encapsulation, etc.), and acetylene black (the main raw material of dry batteries). These high value-added products, based on the most advanced technologies, are highly evaluated and trusted by our customers throughout the world.

Singapore: a core basis for our international strategy

The DENKA group is pushing forward to construct new and enlarged plants for rapidly growing products in Singapore (a core basis for our international strategy), aiming to "strengthen and encourage businesses of priority growth fields," one of the most important elements of our three-year plan "DENKA New Stage 2006."

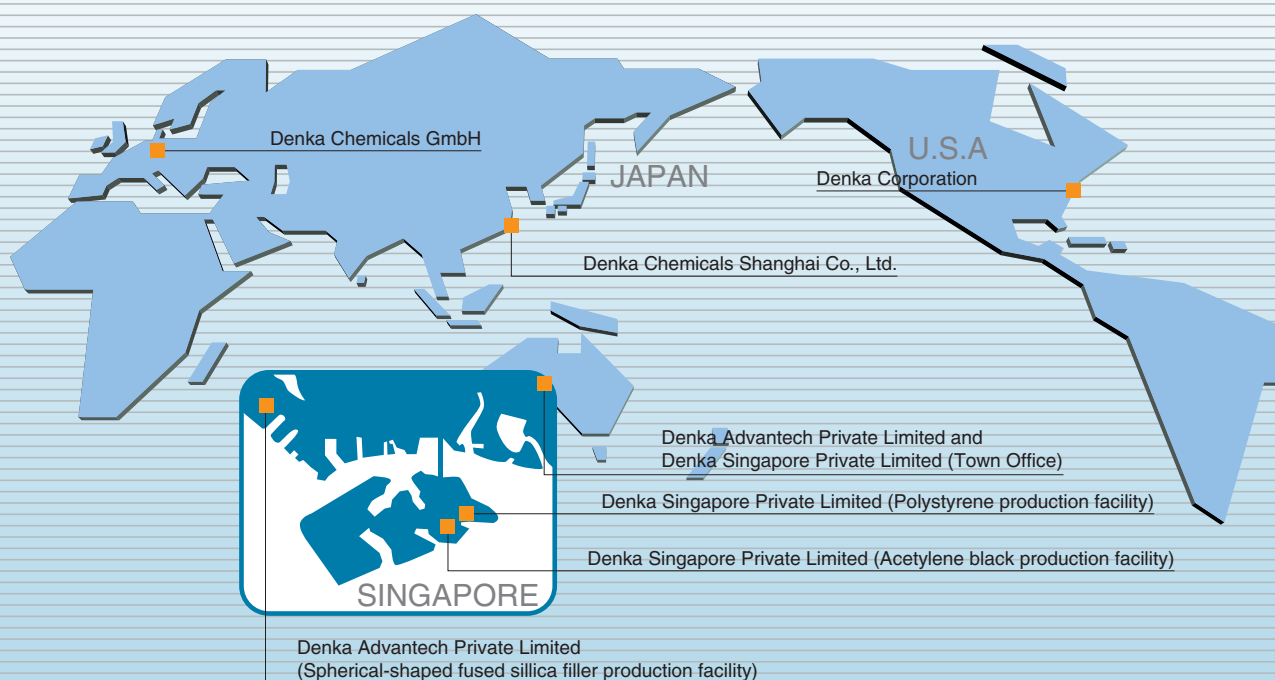
Denka Singapore Private Limited (DSPL) started operations at an expanded plant for "DENKA MW (ultrahigh molecular weight polystyrene)" in Spring 2006, and also a new plant is under construction, and scheduled to start operations in fiscal 2006, to produce "CLEAREN" (highly functional transparent resin for plastic bottle shrink labels), and transparent resin (MS resins for flat panel displays, etc.).

At the same time, Denka Advantech Private Limited (DAPL) has been promoting to expand production facilities since January 2006, to respond to the increasing demands for spherical type fused silica filler.

From Asia to the world

DENKA's global business is steadily expanding. The demand for "CLEAREN" is growing in the United States and Europe, areas with high environmental consciousness, since the product can be easily separated from plastic bottles for recycling by exploiting their different specific gravities. In China, where continuing economic growth is seen, we are developing markets and supporting sales activities of functional resins and special cement additives for construction, as well as establishing a production site for electronics-related products in Suzhou.

The Company's sales channels that cover three global areas play an indispensable role to realize international operations. Our overseas subsidiaries located in New York, Dusseldorf, Singapore and Shanghai are engaged in expanding sales of DENKA products in North America, Europe, and Asia. From Asia to the world—DENKA's global operations strategies is continuously accelerating today.



Five-year Summary

Denki Kagaku Kogyo Kabushiki Kaisha and Consolidated Subsidiaries

Although this financial section was prepared based on our 147th Business Reports, some of the parts are inconsistent with our conventional annual reports.

	2006	2005	2004	2003	2002
		Millions of yen			
Net sales	¥ 307,923	¥ 280,033	¥ 251,116	¥ 243,824	¥ 240,677
Gross profit	75,177	74,190	69,792	66,625	66,782
Operating income	26,069	25,585	21,451	18,017	16,732
Ordinary profit	23,913	21,897	17,610	12,608	8,418
Net income (loss)	15,365	13,587	10,554	4,773	(1,977)
Total assets	349,689	328,248	315,742	313,560	322,808
Total liabilities	198,069	192,084	195,699	206,791	217,450
Interest-bearing debt	91,006	101,066	120,448	140,006	149,666
Total shareholders' equity	146,148	130,715	114,964	102,105	93,099
Cash dividends	3,686	2,922	2,895	2,526	2,297
		Yen			
Net income (loss) per share	31.08	27.70	21.70	9.99	(4.31)
Shareholders' equity per share	297.23	265.71	238.13	211.45	202.67
		%			
Shareholders' equity ratio	41.79	39.82	36.41	32.56	28.84
ROE	11.10	11.06	9.72	4.89	(2.13)
ROA	7.05	6.80	5.60	3.96	2.43
Employees	4,739	4,747	4,831	4,860	5,116

Business Environment

The Japanese economy during the year under review faced concerns such as the surge in crude oil prices, but managed to show a moderately restorative curve, as evidenced by the growth of capital investments by corporations in line with improvements in corporate earnings, and also based on an upturn in consumer spending supported by the betterment of employment conditions.

In the chemical industry, both domestic and overseas demand expanded in general. However, the rise in raw material costs due to increases in crude oil and naphtha prices has been putting pressures on corporate earnings, and the correction of related product prices remains as a pending issue.

Operating Results

1. Net Sales

Denka as a group strived to expand its business and secure profit despite the prevailing economy. As a result, the group achieved on a consolidated basis total net sales of ¥307,923 million, an increase of ¥27,890 million, or 10.0%, from the previous year.

2. Operating Income

Earnings faced challenges from surging raw material prices but this was offset by efforts to revise product prices and expand sales volumes. Consequently, operating income reached ¥26,069 million, up ¥484 million, or 1.9%, from a year earlier. The operating

income ratio declined 0.6 percentage points from the previous year to 8.5%.

3. Net Income

Denka's earnings improved from higher investment income due to increased profitability at equity-method subsidiaries, and from a lower interest burden attributable to reduced interest-bearing debt. Consequently, ordinary income amounted to ¥23,913 million, a year-on-year increase of ¥2,015 million, or 9.2%.

With regard to extraordinary gains and losses, Denka recognized impairment losses of some of its idle and leased properties, while it saw gains on the sale of investment securities to eliminate interlocking holding of equity.

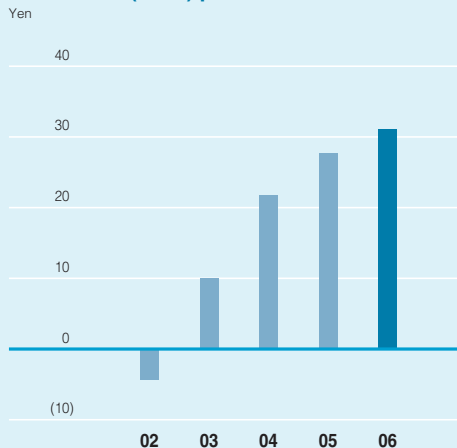
A considerable portion of the influenza vaccine produced by subsidiary Denka Seiken Co. Ltd. failed to pass state inspection, which forced Denka to record a loss from the disposal of such products. As a result, net income for the fiscal year under review amounted to ¥15,365 million, an increase of ¥1,778 million, or 13.1%, from the previous year.

Financial Position

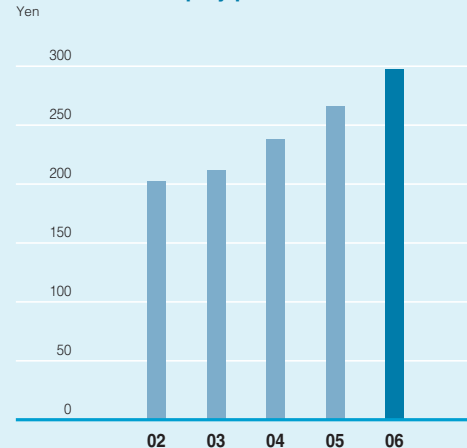
1. Total Assets

Total assets at the end of the year under review were ¥349,689 million, up ¥21,440 million from the previous year, while current assets were ¥120,683 million, an increase of ¥8,783 million from the previous year. These results are mainly attributed to higher receivables resulting from increased sales and higher inventories

Net Income (Loss) per Share



Shareholders' Equity per Share



due to increased raw material prices. Non-current assets marked a year-on-year increase of ¥12,657 million to ¥229,005 million. This result was due to an increase in tangible assets from aggressive capital investments and an increase in investment securities from improved profitability of equity-method subsidiaries and a more favorable stock market.

2. Total Liabilities

Interest-bearing debt declined ¥10,059 million from the previous year to ¥91,006 million as a consequence of maintaining capital investments within the limits of available funds and divesting assets such as investment securities. This policy served to push down the ratio of total debts to total assets by 4.8 percentage points to 26.0%. On the other hand, payables increased due to the rise in raw material prices. As a result, liabilities at the end of the year under review totaled ¥198,069 million, up ¥5,985 million from the previous year.

3. Minority Interest

Minority interest rose ¥22 million from the year before to ¥5,472 million.

4. Total Shareholders' Equity

Total shareholders' equity amounted to ¥146,148 million, an increase of ¥15,432 million from a year earlier, due to higher net income for the period and increased unrealized gains on investment securities. As a result, the shareholder equity ratio increased from 39.8% a year

earlier to 41.8%, while shareholders' equity per share rose from 265.71 yen to 297.23 yen.

Cash Flows

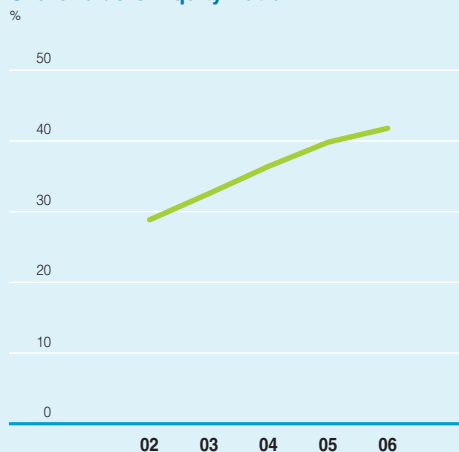
Net cash provided by operating activities during the year under review totaled ¥29,452 million, a decrease of ¥251 million from a year earlier. This result was due to increased trade receivables from higher sales and increased inventories on the back of surging raw material prices, although Denka experienced recovery in its business performance and reduction in interest payments.

Net cash used in investing activities amounted to ¥17,545 million. While Denka sold investment securities in a drive to eliminate interlocking equity holdings, the Company made aggressive capital investment efforts in high-growth business areas such as concentration of the electronic materials business, construction of facilities at Denka Singapore for production of the special resin "CLEAREN" and also for transparent resin, and expansion of production capacity for ultrahigh molecular weight polystyrene. Free cash flow, which combines operating and investing cash flows, totaled ¥11,906 million, down ¥9,284 million from the previous year.

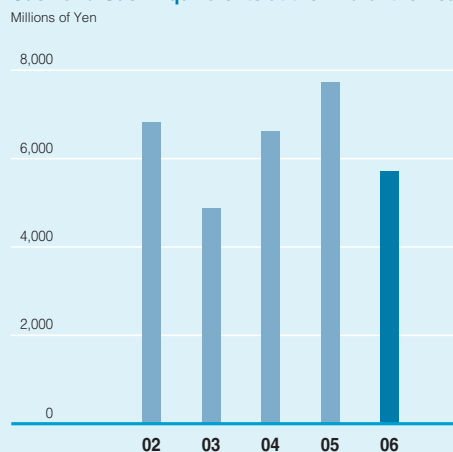
Net cash used in financing activities included ¥3,764 million in cash dividends and ¥10,116 million for repayment of interest-bearing debt in an ongoing drive to bolster the Company's financial position.

As a result, cash and cash equivalents at the end of the fiscal year came to ¥5,710 million, down ¥2,014 million from a year earlier.

Shareholders' Equity Ratio



Cash and Cash Equivalents at the End of the Year



Consolidated Financial Statements (Summary)

Denki Kagaku Kogyo Kabushiki Kaisha and Consolidated Subsidiaries

Consolidated Balance Sheets

Millions of Yen

March 31

	2006	2005
ASSETS		
Current assets	¥ 120,683	¥ 111,899
Cash and time deposit	5,755	7,758
Notes and accounts receivable, trade	66,280	59,609
Inventories	40,681	37,246
Other current assets	8,225	7,596
Allowance for doubtful accounts	(259)	(310)
Non-current assets	229,005	216,348
Property, plant and equipment	176,682	170,656
Intangible fixed assets	3,170	2,428
Investments securities	44,155	38,260
Other	5,257	5,835
Allowance for doubtful accounts	(260)	(832)
Total assets	349,689	328,248
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities	137,923	127,510
Notes and accounts payable, trade	45,344	40,156
Short-term bank loans	43,976	41,235
Commercial paper	4,000	6,000
Current portion of long-term debt	—	5,000
Other current liabilities	44,602	35,117
Long-term liabilities	60,145	64,573
Corporate bond	30,000	30,000
Long-term debt	13,029	18,830
Other long-term liabilities	17,116	15,743
Total liabilities	198,069	192,084
Minority interest in consolidated subsidiaries	5,472	5,449
Shareholders' equity		
Common stock	36,998	36,998
Capital surplus	41,551	41,549
Retained earnings	48,666	36,838
Other	18,931	15,328
Total shareholders' equity	146,148	130,715
Total liabilities and shareholders' equity	¥ 349,689	¥ 328,248

Consolidated Statements of Income

Millions of Yen

For the Years Ended March 31	2006	2005
Net sales	¥ 307,923	¥ 280,033
Cost of sales	232,745	205,843
Selling, general and administrative expenses	49,107	48,604
Operating income	26,069	25,585
Non-operating income	2,885	1,784
Non-operating expense	5,041	5,471
Ordinary Profit	23,913	21,897
Extraordinary gains	4,101	2,448
Extraordinary losses	4,998	2,671
Income before income taxes	23,016	21,675
Current	8,932	6,297
Deferred	(1,474)	1,273
Minority interest in losses of consolidated subsidiaries	192	517
Net income	¥ 15,365	¥ 13,587

Consolidated Statements of Cash Flows

Millions of Yen

For the Years Ended March 31	2006	2005
Net cash provided by operating activities	¥ 29,452	¥ 29,703
Net cash used in investment activities	(17,545)	(8,512)
Net cash used in financing activities	(13,956)	(20,156)
Effect of exchange rate changes on cash and cash equivalent	35	17
Net increase (decrease) in cash and cash equivalents	(2,014)	1,051
Cash and cash equivalents at the beginning of the year	7,724	6,630
Increase of cash and cash equivalents resulting from inclusion and exclusion of subsidiaries from consolidation	—	43
Cash and cash equivalents at the end of the year	¥ 5,710	¥ 7,724

Corporate Data

(As of March 31, 2006)

Established

May 1, 1915

Paid-in Capital

¥36,998 million

Number of Employees

4,739 (Consolidated)

2,757 (Non-Consolidated)

Directory

Head Office —

Nihonbashi Mitsui Tower, 1-1,
Nihonbashi-Muromachi 2-chome, Chuo-ku, Tokyo
103-8338, JAPAN

Main telephone: +81-3-5290-5055

Main facsimile: +81-3-5290-5059

URL: <http://www.denka.co.jp/>

Branches & Sales Offices —

Osaka, Nagoya, Fukuoka, Niigata, Toyama, Sapporo,
Sendai, Nagano, Takasaki, Shizuoka, Hiroshima,
Takamatsu, Kagoshima, Akita, Ageo

Reserch Center —

Machida (Tokyo)

Production Facilities —

Omi (Niigata), Omuta (Fukuoka), Chiba,
Shibukawa (Gunma), Ofuna (Kanagawa),
Denka Kako Co., Ltd. (Gunma)

Overseas Subsidiaries

Denka Corporation

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New York, NY 10017, U.S.A.

Telephone: 1 (212) 688-8700

Facsimile: 1 (212) 688-8727

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Denka Chemicals GmbH

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D-40211 Düsseldorf, F.R. Germany

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Facsimile: 49 (211) 329942

E-mail: info@denkagermany.de

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Denka Advantech Private Limited

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China 200336

Telephone: 86-21-6236-9090

Facsimile: 86-21-6236-8770

E-mail: k-ishizuka@denka.com.cn

Denka Advanced Materials (Suzhou) Co., Ltd.

Unit 9B, Modern Industrial Square,

Suzhou Industrial Park, Suzhou China

E-mail: ttsushima@denka.com.cn

Board of Directors and Corporate Auditors

(As of June 29, 2006)

Chairman

Toshio Hiruma

President

Seiki Kawabata

Senior Managing Directors

Higashi Ito

Yoshiaki Mikami

Managing Director

Koji Minai

Directors

Takashi Toratani

Shigetoshi Toyooka

Tetsuro Maeda

Hiromitsu Niigaki

Nobuyoshi Sakuma

Kuniaki Taketomi

Hitoshi Watanabe

Kenichi Ono

Shinsuke Yoshitaka

Mamoru Hoshi

Takashi Fukuda

Standing Corporate Auditors

Yukinori Totake

Takayasu Tanaka

Corporate Auditors

Kenichi Tsuchigame

Minoru Hatakenaka

Shareholder Information

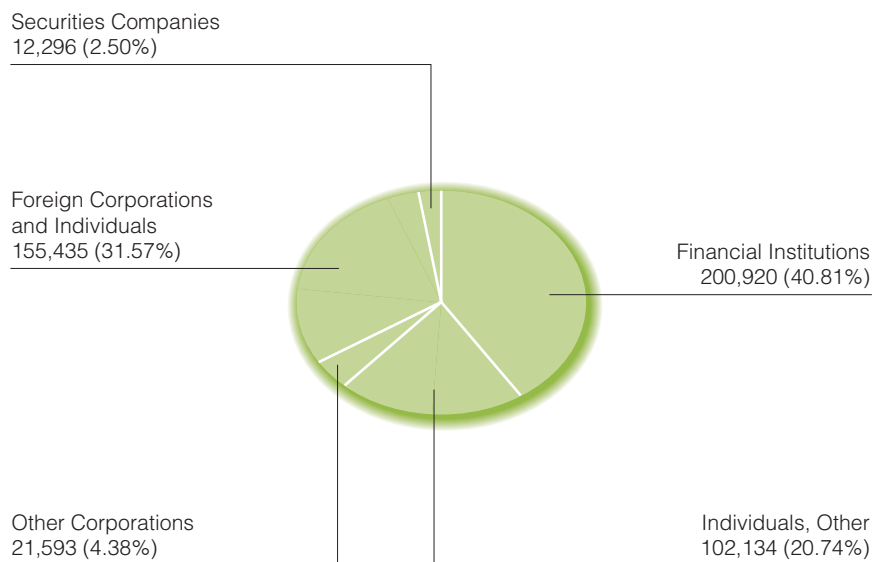
(As of March 31, 2006)

Total Number of Authorized Shares	1,584,070,000
Shares of Common Stock Issued	492,384,440
Number of Shareholders	51,092

Major Shareholders

	Number of shares held (thousands)	Percentage of shares held (%)
Japan Trustee Services Bank, Ltd. (Trust Account)	59,992	12.18
The Master Trust Bank of Japan, Ltd. (Trust Account)	32,429	6.58
The Bank of New York GCM Client Accounts E ISG	15,706	3.18
Trust & Custody Services Bank, Ltd. as trustee for Mizuho Bank Ltd. Retirement Benefit Trust Account re-entrusted by Mizuho Trust and Banking Co., Ltd	15,275	3.10
Mitsui Mutual Life Insurance, Co.	11,908	2.41
The Sumitomo Trust & Banking Co., Ltd. (Trust Account B)	10,999	2.23
National Mutual Insurance Federation of Agricultural Cooperatives	9,076	1.84
State Street Bank and Trust Company 505103	8,603	1.74
Japan Trustee Services Bank, Ltd. (Trust Account 4)	7,853	1.59
Nomura Securities Co., Ltd.	7,409	1.50

Breakdown of Shareholders (Thousand shares)



DENKA

DENKI KAGAKU KOGYO KABUSHIKI KAISHA

Nihonbashi Mitsui Tower, 1-1, Nihonbashi-Muromachi 2-chome,
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<http://www.denka.co.jp/eng/top.htm>